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Caterina Ruggeri Laderchi
Sara Savastano
Editors

Poverty and Exclusion in the Western Balkans

New Directions in Measurement and Policy

Springer

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Chapter 1
Overview: Poverty and Exclusion in the Western Balkans: New Directions in Policy and Analysis

Caterina Ruggeri Laderchi and Sara Savastano

Countries in the Western Balkans[1] are at a critical juncture. Across the region, governments are dealing with the legacy of the past, including an incomplete transition to modern market economies, while looking towards a future in the European Union (EU). The area of poverty and social exclusion – the central theme of this book – is exemplary of the challenges posed by the EU accession process. Approaches to the measurement and analysis of poverty and exclusion now adopted by EU Member States (MS) are rooted in intellectual frameworks developed over many years, backed by an institutional capacity to collect and analyze data, and linked to public policy agendas. These perspectives can open up new horizons and can provide policy makers in the Western Balkans with a deeper understanding of the profile of deprivation. Yet there is a need to assess how models and indicators adopted from the EU reflect local realities and enrich existing poverty diagnostics, how they can be made operational given existing institutional capacity, and how they can inform policy design.

[1] For the purpose of this book, the Western Balkans is defined as comprising Albania, Bosnia and Herzegovina, Kosovo, Macedonia FYR, Montenegro, and Serbia.

The findings, interpretations, and conclusions expressed in this chapter are those of the authors and do not necessarily reflect the views of the International Bank for Reconstruction and Development/ the World Bank and its affiliated organizations, or those of the executive directors of the World Bank or the governments they represent. The World Bank does not guarantee the accuracy of the data included in this work.

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The current volume brings together a selection of the papers presented at the conference. It is divided into four broad thematic areas. The first (chapters 2–4) deals principally with issues of measurement and the analytical context for research into poverty and exclusion in the Western Balkans. The second thematic area (chapters 5–8) focuses on country-level analysis. The authors draw on techniques ranging from small-area estimation and correspondence and efficiency analysis to more familiar regression and qualitative analysis. The chapters demonstrate the scope for broadening the standard toolkit of poverty measurement to capture the multidimensional aspects of deprivation at the core of the broader inclusion agenda. The third theme (covered in chapter 9–12) explores barriers to inclusion that restrict the opportunities facing some social groups. Some of these barriers can be traced to labor market effects influencing patterns of employment and wages. Others are rooted in ethnicity and urbanization. While the issues covered are by no means exhaustive, they are illustrative of the wider forces shaping prospects for the development of more inclusive societies. Our fourth thematic area (chapter 13–16) turns to the issue of the reform of the social safety nets, a major plank of the inclusion agenda. Several countries in the region have embarked on significant reforms to increase the effectiveness of these programs in the face of fiscal pressures. While new data and new analytical tools can help strengthen program design, the political economy of implementation remains challenging.

Recent developments in the Western Balkans have underscored the critical importance of public policy research on issues surrounding poverty and inclusion. Over the first half of the last decade the region experienced significant improvements in living standards. This largely reflected the impact of the ambitious economic reform program undertaken, adopted by countries of the former Yugoslavia only at the beginning of the last decade. Economic growth averaged 5 percent per year between 1999 and 2008, helping to fuel a significant reduction in poverty. An estimated 750,000 people rose above the absolute poverty line between the beginning of the decade and 2008, reflecting the strong economic performance in larger countries.

The global crisis that hit the region in late 2008 dramatically changed this encouraging picture. To varying degrees across different countries, progress on poverty and economic growth was thrown into reverse gear.[2]

The 2010 Life in Transition Survey (LITS) survey provided a valuable insight into the household-level effects of the crisis. In Montenegro over half of respondents reported that a household member had experienced wage reductions or arrears as a result of the crisis. In Macedonia FYR, one third of households reported job losses or family business closures. Respondents in Bosnia and Herzegovina (BiH) and Serbia highlighted a loss of remittances as another transmission channel from economic slowdown to reduced living standards (Bidani et al 2012, p.5).

The 2008 crisis revealed the acute vulnerability of poor households across the Western Balkans to the effects of economic downturns. That vulnerability remains

[2] The region as a whole is estimated to have contracted by 1.7% in 2009 even though GDP growth remained positive in Albania and Kosovo (World Bank 2011).

much in evidence as the economic slowdown which started in the Euro area in 2011 continues to impact the region. Economic growth projections for the region have been revised to just over 2 percent over the next couple of years, though there are significant downside risks. As economic growth remains vulnerable to slowdowns in trade, reduced flows of foreign direct investment, losses of remittance income, and the exposure of the financial sector to foreign banks (World Bank 2011) the associated risks for poverty and exclusion are high. Data suggests that by 2011 at least an estimated 230,000 people had fallen into poverty since the onset of the crisis. However, this may be an underestimate since updated data are not available for all countries. Where yearly poverty estimates are available, as in Serbia, they show that the crisis has a long tail of adverse effects on poverty, with households increasingly unable to cope with economic stress.

As the impacts of the post-2008 crisis continue to unfold, three concerns have moved to the forefront of policy debates. The first is unemployment. After declining steadily before the crisis, the incidence of unemployment is on the rise in Macedonia FYR, BiH, Montenegro and, most dramatically, in Serbia. Panel evidence for Serbia shows that low-skill sectors have been particularly affected by job losses. The same evidence also points to the "freezing" effect of the crisis on the labour market mobility, with the movement of workers between employment, unemployment and inactivity dropping significantly as the crisis progressed. Reduced mobility has emerged as a major contributory factor in driving up unemployment among those seeking work, and in restricting opportunities for economically inactive populations to rejoin the workforce (World Bank 2012).

The second concern is the asymmetric effect of the crisis on different parts of society. Where detailed evidence is available it shows that higher income groups are experiencing positive growth while poverty is rising. In the case of Serbia, asymmetry has an additional rural-urban feature. Prior to the crisis, the rise in rural incomes was contributing to poverty reduction. That picture appears to have changed, with rural areas now lagging behind in terms of economic growth.

The third concern relates to budget pressures. Fiscal deficits grew significantly across the Western Balkans as growth faltered in 2009, and they remain large. One effect is that the availability of government resources for combating poverty and social exclusion is highly constrained at a time of rising need. This has far-reaching implications for the design of social safety nets and the targeting of welfare transfers.

None of these concerns are entirely new elements. Indeed, some of the underlying pressures were visible long before the 2008 crisis struck the region. Sluggish job creation and very low activity rates placed limits on the scope for inclusive growth. Activity rates for women were particularly low while youth unemployment rates were very high. In contrast with other eastern European countries, poverty levels were much higher among the unemployed. Meanwhile, the design of social security system contributed to generating disincentives to entry into the (formal) labour force. Inequalities were already rising across much of the region, driven in part by disparities in opportunity. Poor people were disproportionately rural and with low levels of education. Despite the progress in poverty reduction up to 2008 many

households remained perilously close to the poverty line, dependent in many cases on the export of labor and remittances. The 2006 LITS found that only one-third of citizens in Western Balkans reported being satisfied with life – a lower level than that reported for most countries in Eastern Europe and Central Asia,[3] even though by the yardstick of absolute consumption poverty the Western Balkans fared relatively well when compared to other countries in the region. On the fiscal side, in several countries budgets were becoming less pro-poor. Programs directed to specific groups – known as "categorical benefits" – were growing relative to means-tested programs. Meanwhile, governments' ability to increase resources was limited. Factors as varied as capacity in the tax administration system, high levels of informal activities and tax evasion all played a role. This made revenues more dependent on tools, such as the Value Added Tax (VAT), likely to have negative distributional consequences.

As this brief synopsis indicates, the problems posed by poverty and exclusion in the Western Balkans have pre-crisis roots that have been nourished by the economic downturn. Several chapters in this book point to emerging opportunities for addressing them. In particular, the prospect of closer European integration can help support a broad reform agenda, especially in the areas of safety nets reforms and activation. Moreover, while the *acquis communautaire* can be institutionally challenging to absorb, it brings with it access to additional financial, analytical and administrative resources particularly in the field of social inclusion. In addition, the EU Member States long experimentation with analytical and statistical tools new to the region can provide useful insights to shape their own efforts to address this complex agenda.

One area in which dialogue over accession has already had a discernible impact is in the conceptualization and measurement of deprivation – the first of our thematic areas. The chapter by Maquet Engsted reviews the evolution of the EU member-state approaches to poverty and exclusion over time. The 'Europe 2020' poverty and social inclusion targets adopted by the European Council in 2010 marked the culmination of a lengthy political process. As Maquet Engsted points out, the European paradigm of social inclusion emerged as a negotiated consensus between Member States. That consensus was informed by public policy research and shaped by a political dialogue across countries with very different traditions in the analysis of social deprivation. An interesting example of the evolving nature of poverty concepts is Maquet Engsted's discussion of the shortfalls of adopting relative poverty lines. Despite their solid intellectual foundations, their application can lead to counterintuitive results when applied to the wide spectrum of realities of the EU. Maquet Engsted also traces the triad of indicators adopted for the 'Europe 2020' at risk of poverty and exclusion target – risk of poverty, material deprivation and workless households – to the political realities of different EU member-states. The way the target has been constructed has its own imperfections. As Anthony Atkinson and others have pointed out, any multidimensional measure has to address difficulties associated with overlapping deprivations. However, as Maquet Engsted notes, the social inclusion target provides

[3] For purposes of comparison, some 50 percent of households reported satisfaction with life in the new EU member states. Even the Commonwealth of Independent States reported higher levels of satisfaction with life than the Western Balkans.

a useful diagnostic tool. One of its strengths, in the eyes of the author, is the link from the measurement benchmarks to the functioning of labor markets and the design of the tax benefits system, both of which have a major bearing on patterns of exclusion. Maquet Engsted also draws attention to the wider relevance of the debate over the use of the 'budget standard' method to set a poverty line. While this method is a conceptual departure in terms of existing practices in the EU, the broad approach is similar to the consumption-based poverty measure used by the World Bank in the region. This is one area in which there may be far more scope for learning across institutions and measurement approaches than is typically recognized.

Making the transition to a social inclusion paradigm to analyze deprivation involves not just a conceptual shift, but also a process of institutional adaptation. Nowhere is this more evident than in the development of statistical systems for measuring poverty and exclusion – a theme taken up in the chapter by Carletto, Ruggeri Laderchi and Savastano. At the EU level, poverty and exclusion are monitored based on yearly Surveys of Income and Living Conditions (SILC). These surveys are complex and involve significant efforts to collect income data. The authors trace a number of improvements that have taken place over the past decade in the statistical systems in the Western Balkans, which provide their starting point in moving towards adopting SILC. While there are substantial differences between countries in terms of survey methodology, there is a consistent move towards the adoption of "SILC-like" variables to capture social exclusion. Following the recommendations of the Expert Group on Statistics in the region, which issued a report in 2009, the chapter cautions that managing the data transition will require careful consideration of local realities. As the authors point out, *what* is being measured makes a difference. For example, policy makers need to take a position on the 'income versus consumption' approach to poverty. Given the extent of informality in labor markets and the level of reliance on small holder agriculture, they argue, the measurement of income is likely to prove problematic. The authors also point out that an exclusive reliance on the SILC survey would prevent the computation of longer run poverty trends. Their recommendation is that analysts and policy-makers should adopt a flexible approach, marrying continuity and innovation through survey designs that allow for the monitoring of both income and consumption poverty. In addition to the potential benefits that might emerge from triangulation and learning, having income and consumption data for the same households would create an opportunity to explore with greater accuracy the distributional effects of growth and the effectiveness of social transfers – two important elements of an analytical agenda to address poverty and exclusion.

Chapter 4 shifts the focus towards qualitative data and research. Turk highlights the contribution that structured focus group discussions in particular can make to the understanding and analysis of poverty and exclusion. The chapter reviews the experience of a wide ranging set of qualitative studies conducted since 2009 by the World Bank, but many of its insights are of broader application (see, for example, Chapter 8 in this volume). The structured focus group approach discussed in detail by Turk follows a methodology rooted in participatory poverty measurement work pioneered by Robert Chambers. At the core of participatory poverty measurement is the idea of empowering local communities to analyze and identify priorities of action in

addressing their development challenges. From this perspective, participatory approaches have developed in parallel (if not in direct opposition) to the more mainstream type of poverty analysis, much of which takes the form of external 'experts' collecting and analyzing quantitative data. However, even when applied to extract information from respondents rather than seeking to empower them to take action, participatory approaches can make a significant contribution to our understanding of poverty and inclusion. As Turk emphasizes, this is particularly true for deprived groups that are not adequately covered in household surveys. One of the great strengths of participatory analysis is that it provides an insight into the social dynamics of exclusion and the role of public policy – a strength that Turk illustrates by reference the exclusionary mechanisms generated through social assistance programs, which she explores both in general and in relation to a specific group (the Roma). The chapter also highlights the critical role of design and methodology in generating value-added through participatory assessments. This emphasis on methodology reflects the author's belief that successful analytic work is contingent on the application of rigorously designed research tools applied to sample selection criteria that reflect local realities. Failure to put in place a robust methodology carries with it the risk that findings will be dismissed as anecdotal or inaccurate – or both. By the same token, Turk makes a compelling case for establishing participatory assessment as part of the poverty and exclusion toolkit for the Western Balkans – and for building capacity in this area.

The second set of thematic chapters considers the application of a range of measurement tools to the analysis of poverty and exclusion in the Western Balkans. In Chapter 5, Betti and co-authors present a method for constructing updated poverty maps. This work addresses an important concern. Capturing the changing profile and shifting geography of poverty and exclusion is critical for effective policy making, not least to design geographically targeted programs. However, the lack of panel data in general, and of geographically representative data in particular, has limited the ability of policy-makers and researchers to monitor the changing geography of poverty. While national censuses provide a wealth of data, the ten year long inter-censal period means that the data they provide has a limited shelf-life. The technique outlined by Betti and his co-authors has the potential not only to generate geographically disaggregated poverty maps, but to fill the gap between censuses by computing updated statistics. More work is needed to test for the robustness of the findings, but preliminary results suggest that the method predicts between-census poverty estimates with some accuracy. The findings suggest that these and similar techniques could fill data gaps and provide the information needed for effective geographically targeted interventions, such as those supported by the European Structural Funds (or geographically targeted social assistance, see Chapter 16 in this volume).

Cojocaru and Ruggeri Laderchi consider a different kind of innovation. Using data from a special "SILC-like" module developed for the 2011 Bosnian Extended Household Budget Survey (BEHBS) their chapter presents data on the distribution of risk for poverty and social exclusion in BiH, contrasting the observed pattern with those observed in EU member states. This is the first time that data on the risk of poverty and social exclusion indicators is presented for the Western Balkans.

The BEHBS module that made the exercise possible was a pilot application of a recommendation from the Expert Panel on Statistics discussed in Chapter 3. The chapter profiles the three core deprivations identified in the Europe 2020 target for poverty reduction and inclusion. It also explores the congruence between diagnostics based on these indicators and those based on consumption poverty. The authors recognize that sample size constraints the scope for deepening the analysis - and they caution against drawing generalizations. However, the chapter illustrates how the definition of poverty adopted will have a bearing on the diagnostics of deprivation and, by extension, on policy priorities. In highlighting the way in which the choice of indicators shapes the diagnostics of poverty and exclusion, Cojocaru and Ruggeri Laderchi emphasize the need to combine innovation in survey design with a degree continuity, such as by maintaining a consumption module even when adopting as new policy targets indicators based on income.

The chapter by Deutsch, Silber and Verme exploits the availability of another 'SILC-like' survey to present an assessment of social inclusion for Macedonia FYR. Departing from the EU analytical framework they identify five different domains of exclusion: employment, assets, living standards, subjective well-being and social capital. The authors arrive at an aggregate indicator of exclusion through a multi-step procedure for a range of proxy variables in each of the five domains. This allows them to generate a continuous variable which is then amenable to standard regression analysis to identify its underlying determinants. The authors conduct separate regressions for different ethnic groups. Several striking findings emerge. Using a consumption-based poverty measure, the authors find that the capital, Skopje, not only exhibits lower levels of deprivation than the rest of the country (World Bank 2009), but that it has been pulling further ahead of other regions over time. However, this chapter finds that, while consumption poverty levels are higher, exclusion levels are lower outside of Skopje. Why the apparent discrepancy? The authors interpret their findings in the light of well-being indicators included in their social exclusion framework. More specifically, they trace the lower level of exclusion reported outside of Skopje to the degree of ethnic homogeneity in different areas of the countries. If that interpretation is correct, it would suggest that there may be a potential trade-off between inclusion in one's own community (here identified by ethnicity) and inclusion at the national level.

Petrovic looks beyond quantitative analysis to develop an applied qualitative research model. Using a multi-dimensional framework, she attempts to measure deprivation in subjective well-being among participants in a public work programs in Serbia. The methodological approach in her paper – semi-structured in depth-interviews – is different from that outlined in chapter 5, though she is equally concerned to ensure appropriate representation even with a small sample and to complement the findings of quantitative work. Some of the results to emerge from the analysis have far-reaching implications for public policy, notably with respect to employment programs. Evaluations focused on narrow labor market outcomes have tended to conclude that publicly funded employment is a relatively ineffective strategy for tackling deprivation (Card et al 2009). Petrovic calls this received wisdom into question. Her broader evaluative framework, with its emphasis on subjective

well-being, finds strong positive effect associated with participation in public works programs. That effect appears to derive from the value attached by participants to the enhanced social contacts that they experience through such programs, along with the opportunity to gain skills and qualifications. An important policy message, echoing that to emerge from the Deutsch, Silber and Verme chapter, is that well-being has relational dimensions that go far beyond the parameters of deprivation identified through narrower monetary indicators of poverty.

The third set of thematic chapters covers from different perspectives some of the underlying drivers of inequality that perpetuate social exclusion. Focusing on the Serbian labor market, Koettl explores two areas with an important bearing on poverty and exclusion: namely, high levels of inactivity and informal employment. He focuses on the role of labour taxation and social benefit design in providing disincentives for formal employment. The chapter identifies a high tax wedge at lower wage levels, due to the minimum social security contributions that employees and employers are required to pay. The author argues that the associated disincentive effects are reinforced by social assistance programs under which support is withdrawn at very low levels of income. Paradoxically, therefore, mechanisms that are intended to protect workers' rights appear to reinforce social exclusion, particularly at the lower end of the earnings distribution.

Tomini and Hagen-Zanker consider a different set of potentially exclusionary mechanisms, by looking at the disruption bonds brought about by internal migration. Exploring the dynamics of the urbanization process which has accompanied recent growth in Albania, they focus on changes in the pattern of private transfers from family and friends that internal migrants receive. In particular, the paper investigates financial, in-kind and service transfers received by migrant households before and after they migrate to Tirana. Using a small-scale household survey combined with in-depth semi-structured interviews, the authors identify some of the distinctive characteristics of migration to peri-urban areas in Albania. One of the most striking features of the migration patterns that they report is the movement not just of one or two individuals in a household, but the relocation of entire extended families and villages. Despite the apparent cohesion of villages and families the original patterns of transfer change in urban areas. Households receive more frequent financial transfers partly because of the higher level of monetization in the urban economy, and partly as a consequence of the increased vulnerability that comes with a higher cost-of-living. Urban migrants are also more likely to receive transfers from friends rather than family. While siblings remain an important source of transfers for urban migrants, the role of other family members diminishes. This points to a weakening of the traditional supportive role that extended households play. As the authors note, the large reliance on informal transfers after migration calls into question the sustainability of emerging urban livelihoods in a context marked by widespread poverty and limited state support.

The chapter by Ivlevs and King examines the role of ethnic identity and how it relates to the dynamics of exclusion. The study focus on the multi-state that is post-independence Kosovo and identifies clear patterns of disadvantage across different ethnic groups. It also draws attention to significant differences in attitudes across

ethnicities, with characteristics such as age, gender, income levels, area of residence and labour market status exercising a cross-cutting influence. The findings that emerge from this chapter support those from a wider body of work cautioning against the reduction of multi-layered identities (for example, ethnicity, language, culture, religion and location) into classifications based on only one attribute (such as income or ethnicity) when explaining complex social interactions or the potential for conflict (this is a central theme in Sen 2006).

The final set of thematic chapters turns to safety nets – a key policy tool to reduce poverty and exclusion. Gotcheva and Sundaram provide a comparative assessment of the design, implementation, financing, and performance of non-contributory cash transfer programs (social assistance) across the six countries in the Western Balkan region, benchmarking their performance against similar programs in other countries in Central and Eastern Europe. The chapter has some important messages for public policy. With fiscal pressures imposing tight constraints on budgets and the economic crisis having increased social hardship, significant reforms are needed to enhance the efficiency and equity of safety net provision. The reforms this chapter calls for include cutting expenditure on non-means-tested benefits, increasing the uptake and extending the coverage of means-tested social assistance, reducing work disincentives currently built into the design of last-resort social assistance, and increasing the flexibility and responsiveness of assistance programmes to crises and shocks.

Bartlett provides a historical perspective on the development of welfare states, drawing parallels and identifying differences between the experiences of western Europe and the former communist countries of eastern Europe on the one side, and the western Balkans on the other. The author identifies three core explanatory variables shaping the evolution of welfare states: path dependency and historical experience, the transition to capitalism, industrialization and deindustrialization, and the formation of political alliances, notably those associated in former socialist states with the transition to democracy. Other than in Albania and Kosovo, the author finds that the systems which emerged in the Western Balkans have the characteristics of the post-communist regimes in the literature on welfare states. Looking to the future, the chapter argues that, despite rising poverty and acute vulnerability, the political support for further reforms of the kind advocated in Chapter 13 is lacking. It highlights the absence of a politically significant middle class and capture of benefits by particular interest groups – notably veterans – as obstacles to meaningful reform. The bleak prospects for reform are worrying since Bartlett highlights the highly regressive pattern of social assistance transfers associated with categorical benefits, along with the weak coverage and limited support provided through targeted benefits.

The last two chapters include two analytical contributions that have helped inform the design of concrete reforms. Aranderenko and co-authors use a newly developed tax and benefit micro-simulation model for Serbia (SRMOD) developed along the lines of the EUROMOD model constructed for EU member states. Their analysis provides an ex-ante assessment of the 2010 social assistance reform, which sought to increase the coverage and generosity of transfers broadly along the lines recommended in Chapter 13. The simulation exercise conducted in the chapter suggests that the legislation could be expected to improve targeting and increase

social assistance of last resort. However, there is a caveat. Despite these positive changes coverage would remain limited since the eligibility criteria for asset ownership are set at a very low benchmark level. Another concern, reinforcing those raised by Turk in Chapter 4, is the complexity of the procedure through which claimant establish eligibility. The danger is that the high transaction costs associated with entry to the system will limit take-up.

The final chapter by Ruggeri Laderchi and co-authors explores how the targeting of social assistance in Albania could be improved by using better information. Using the updated poverty map presented in Chapter 5, and a newly developed proxy means test, the authors simulate budget neutral alternative allocations of the social assistance of last resort program. The findings illustrate how there is scope for allocating better existing resources by strengthening the link between allocations and need as captured by poverty indicators at the municipal level. The chapter also recommends replacing the existing system of binary "filters" with eligibility criteria that weight different household characteristics in order to reduce the exclusionary potential of some of those filters. This direct application of new data and methodologies that have been developed over the last few years shows the potential benefits of investing in better data and tools to strengthen the informational basis for program and policy design.

The chapters in the current volume illustrate the breadth and dynamism of the research on poverty and exclusion in the Western Balkans and its potential to inform the design of more effective policies. The priorities and main findings of this research appear to be well-aligned with those identified by Maquet Engsted as emerging from EU member states, such as the importance of labour market outcomes for inclusion despite the high incidence of poverty for working families; the importance of focusing on groups which are marginalized; and the possible disincentives embedded in the tax-benefit system. Yet some distinctive element characterize research in the region, which will remain very relevant as countries move forward in the accession process.

One such an element, which is an important theme in this book, is that the move towards adopting inclusion as a guiding framework for social policy can play a constructive role in broadening the debate on deprivation, encouraging governments to look beyond simple monetary indicators to focus on the dynamics of exclusion. Benchmarking countries through a common set of measures linked to those deployed in the EU could create new opportunities for tapping into the expertise and efforts developed abroad. Yet as the authors of this volume stress, it is important that continuity with past approaches complements learning and experimentation with new ones. Indeed as methodological and conceptual developments continue, new areas for convergence and dialogue appear. One of the central messages of this book is that that there is a virtue in combining different conceptual approaches, with a wide variety of quantitative and qualitative instruments having a place in the toolkit. Another message is that there is no substitute for rigorous analysis of poverty and social exclusion. Researchers and research partnerships have a vital role to play in collecting high quality, timely and accessible data – and in sharing their work across the region. This book is intended as a modest contribution to that vital enterprise.

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Chapter 2
The European Context: Measuring Social Inclusion in the European Union

Isabelle Maquet Engsted

Introduction

In a diverse and changing Europe, the concepts of poverty and social exclusion have not developed as an abstract intellectual project, but rather as a pragmatic response to the reality of member states and the competencies of the European institution in this field.[1] Social policy statements, activities and agreements at the EU level (Commission, Council) have crystallised a negotiated understanding of these concepts, along with advances in measurement within the EU level statistical system.

Important milestones in this process have been:

(i) The first antipoverty programmes and the concomitant adoption of a common definition of poverty in 1975, where the poor were defined as "*individuals or families whose resources are so small as to exclude them from the minimum acceptable way of life of the Member State in which they live*". These initial Council conclusions and their successors focused mainly on advancing research in the field and on the exchange of good practices.

[1] Social inclusion—defined as a process to prevent and tackle poverty and social exclusion—is a concept mainly used at EU level and less in national policy-making. The UK and Ireland are notable exceptions. Social policy is a shared competence of the member states and of the EU, and its main instruments (e.g. social protection) are in the hands of member states.

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(ii) The March 2000 in Lisbon Council conclusions, stating that "*The number of people living below the poverty line and in social exclusion in the Union is unacceptable. Steps must be taken to make a decisive impact on the eradication of poverty by setting adequate targets to be agreed by the Council by the end of the year*". Since then, member states have worked together and shared experiences within the open method of coordination (OMC).[2]

(iii) The June 2010 Europe 2020 strategy under which EU heads of states and governments committed themselves *to reducing poverty and social exclusion in the EU by at least 20 million people by 2020*. This target is one of three integrated objectives (with employment and education) to contribute to inclusive growth, defined as "*building a cohesive society in which people are empowered to anticipate and manage change and consequently to actively participate in society and the economy*".

This chapter provides in the first section a brief overview of the evolution of the concepts of poverty and exclusion as reflected in different EU level policy statements. In the following ones, first a description of how this evolution was reflected in the choice of indicators and then of how this resulted in the Europe 2020 target. The final section concludes by considering the major insights from the application of the EU analytical framework for candidate and potential candidate countries that are shifting towards this paradigm to inform their policies.

[2] As social policy remains under the full competency of member states, to coordinate their action, they agree on common goals (e.g. making a decisive impact on the eradication of poverty) and on common indicators used to monitor progress and compare best practices. Member states translate the common goals into their own strategic objectives and regularly report on the policies they put in place to reach these objectives. The National Strategy Reports are analysed and assessed at EU level, and common policy conclusions drawn from this analysis are jointly adopted by the European Commission and member states in the yearly Joint Report on Social Protection and Social Inclusion. The EU runs an action programme to support mutual learning through a variety of instruments: financing of EU stakeholder networks, peer reviews on specific policy issues, independent experts network, round table, EU meeting of people experiencing poverty, transnational and awareness-raising projects, studies, data collection, etc.

Action at European level has increased political awareness of poverty and exclusion and placed the fight against poverty higher on national political agendas. It encouraged member states to critically examine their policies. It highlighted how countries perform well in certain areas, spurring on other member states to perform better. It also created a better basis for policy-making by involving a range of actors such as NGOs, social partners, local and regional authorities and those working with people in poverty. The method also allowed creating a clear consensus about a number of common key priorities in the fight against poverty and social exclusion: child poverty, active inclusion, decent housing for all, etc.

Poverty and Social Exclusion: How the Concepts Developed in the EU

The definition of poverty introduced in the EU policy framework in 1975 emphasises the lack of command over resources that can hamper full participation in society. Note that at the time, the then nine EC countries enjoyed similar levels of economic development and welfare[3] that allowed them to meet the vital and basic needs of the vast majority of their populations. The original EU approach reflected therefore a shared understanding that, in advanced and prosperous economies, the aim of governments goes beyond ensuring minimum subsistence levels for their citizens; it is also to ensure that all benefit from the general level of prosperity of the society. By referring to the national circumstances, they agreed that poverty is relative in time and place. This also implied that poverty is a matter for policies conducted at national level, such as employment, education and social protection.

Over time the definition of poverty has evolved from a lack of command over material resources defined as "*goods, cash income plus services from public and private sources*" adopted by the 1975 Council decision to encompass more explicitly "*cultural and social resources*" (1984 Council decision) beyond the material aspects. This evolution reflected a growing awareness that poverty is multidimensional.

Social exclusion appeared in the EU scene in the late 1980s, notably through a 1989 Council Resolution on "combating social exclusion". Observers of the EU coordination process note that the use of the concept at EU level was a response to the increasing resistance of some countries (namely Germany and the UK) towards any EU action in the field of poverty.[4] Poverty, especially if defined in a relative sense, was seen as a politically contentious concept, and the fight against poverty was considered a national competence, as far as it implied redistribution of resources.

Other than moving the emphasis away from poverty, the concept of social exclusion, as generally used in the EU context, had the advantage of offering a rather vague connotation. This ambiguity has been instrumental in overcoming member states' divergence of views and in keeping social policy on the EU political agenda. One observer noted that in France fighting social exclusion is seen to require actions to ensure social integration with an emphasis on the social and cultural dimension of participation (Atkinson 2000); in Germany and the Netherlands, fighting social exclusion is about reintegration in the labour market of the welfare dependant, which is very close to the "welfare to work agenda" of the UK labour government; and

[3] Between 1975 and today, socio-economic disparities between EU member states have increased dramatically. In 1975, GDP per capita varied from 92 to 113 of EC-9 average (excl. Ireland), against a variation from 45 to 131 of EU-27 average today. In 1975, social expenditure varied from 20 to 29% of GDP (excl. Ireland), against a variation from 11 to 30% of GDP today.

[4] In the UK, a heated debate took place in the late 1980s around the issue of relative vs. absolute poverty, and John Moore Thatcher, secretary of state, even argued that (absolute) poverty was largely a thing of the past in the UK.

finally in the Scandinavian countries, social exclusion refers to exclusion from the labour market, with an emphasis put on different forms of deviant behaviour. Those same differences were still visible in 2010 during the negotiations on the definition of the Europe 2020 target (M. Daly 2010).[5]

Overall, when compared to poverty, social exclusion makes more explicit that the phenomenon is multidimensional and dynamic. Since the mid-1990s, EU documents have referred to "poverty and social exclusion" Together. This reflects a common understanding wide enough to cover national variations. Central to this understanding is a shared recognition that:

- Beyond the satisfaction of basic needs, individuals should have command over the resources that are necessary to live in dignity, realize their rights, and participate in society and the economy.
- The multiple dimensions of exclusion beyond the lack of income to cover the areas of work, health, education and social and cultural participation (thereby reflecting the views of those who have broad understanding of social inclusion as a process to support social integration).
- The temporal and dynamic dimensions of the phenomenon require solutions that allow the individual to durably escape poverty, for himself and his descendants, and to overcome the barriers to his full participation in society that he may face (e.g. discrimination). This highlights the key role of labour market integration, equal opportunities and anti-discrimination policies. Over time, the labour market dimension of exclusion gained importance, notably under the influence of the countries supporting "welfare to work" solutions.
- Situations of poverty and social exclusion are relative in time and place. However, it also recognised that poverty is graduated and that the most severe forms of poverty and exclusion also need to be taken into account. Following the 2004 wave of accession and the increased diversity of the EU landscape, there has also emerged a need to reflect "absolute" differences in living standards across the EU and how economic growth affects their improvement.

Poverty and Social Exclusion: Measures and Indicators

The development of "social inclusion" indicators in support of the EU policy coordination process aims at reflecting agreed political objectives. But it also contributes to shaping the underlying concepts, not least because measurement requires precise definitions and clarity of purpose.

[5] The most adamant negotiators (DE, NL, DK, SE, CZ), insisting on the social exclusion dimension of the target, were those for which reintegration on the labour market of the welfare dependants, rather than redistributive policies, is the priority. On the other hand, the countries that insisted on defining the target on the basis of relative poverty and deprivation indicators only were those for which social integration requires access to both monetary and nonmonetary resources.

The first set of EU "social inclusion" indicators was formally adopted by the 2001 Laeken Council. Eighteen indicators were identified by the indicator's subgroup of the newly established Social Protection Committee (2000) with the support of academic work carried by Atkinson and Marlier[6] on behalf of the Belgian presidency of the Union. The exercise built on several decades of efforts to develop comparable measures of poverty and other social outcomes for EU Member States (MS), as well as on the related investments in EU harmonised social statistics.[7] The indicators were used to support EU-level policy monitoring in the context of the strategy for social inclusion, which centred on the social open method of coordination (social OMC).

The so-called "18 Laeken indicators" had a strong emphasis on relative income measures (reflecting the original definition of poverty) but covered also labour market exclusion (jobless households), regional disparities (dispersion of employment rates), education (early school leavers) and health status (life expectancy[8]). The original list was complemented over the years by indicators reflecting the multiple dimensions of exclusion, including indicators of in-work poverty, access to health care (unmet need for care), employment rate of migrants, material deprivation (access to non-monetary resources) and the quality of, and access to, housing.

In 2006, the social inclusion portfolio was merged with indicators developed to monitor the EU's strategy for modernizing social protection in the fields of pensions and health care. This resulted in a short list of fourteen overarching indicators covering the objectives of greater social cohesion, supported by adequate and sustainable social protection and inclusive labour markets (see full description of the objective in Annex 1).

The current EU approach to measuring poverty and social exclusion largely builds on an interpretation of the 2005 social inclusion objective and reflects the common understanding described in the previous section. However, a lot remains to be done to capture important aspects of deprivation, including non-monetary dimensions and the most severe forms of exclusion. The following dimensions are covered:

- The *at-risk-of-poverty rate* defined in relation to a threshold set at 60% of the national median income reflects the relative definition adopted by the Council in 1975, which refers to the minimum acceptable standard in the country in which people live. It is responsive to the effectiveness of the policies mobilised at national level to fight poverty: employment and welfare policies in particular. As it is a relative income measure, though, it can provide with counterintuitive results (Box 2.1).

[6] Atkinson A.B., Cantillon B., Marlier E., Nolan B. (2001). Social Indicators: the EU and Social Inclusion. Oxford University Press.

Atkinson A.B., Cantillon B., Marlier E., Nolan B. (2007). The EU and social inclusion: facing the challenges. The Policy Press.

[7] Comparable statistics on income and social inclusion became available at EU level before the mid-1990s, with the first results of the European Community Household Panel (1994–2001).

[8] Broken down by socio-economic status if available at national level. Comparable data on socio-economic disparities in health status are unfortunately technically difficult to obtain, and despite efforts to improve statistical availability, they are still not available at EU level.

Box 2.1 Disparities in median income and the risk-of-poverty incidence

When the social inclusion indicators were first developed, it was agreed that the poverty threshold used in each member state should be national. According to the EU definition, social exclusion is about how you compare yourself with others in the society in which you live. Pragmatically this also resonated with the acceptance that social policy is a member state responsibility rather than a policy area determined at EU level. Nevertheless, it was felt that the different at-risk-of-poverty rates needed to be put in context by the use of the poverty threshold in each country. The threshold for each member state is shown in Fig. 2.1 for an illustrative one-person household. Even if the values are expressed in purchasing power standards (PPS) to take account of the differences in the cost of living across countries, and if we consider Luxembourg as an outlier, the value of the poverty threshold in the richest countries is nearly five times higher than in the poorest.

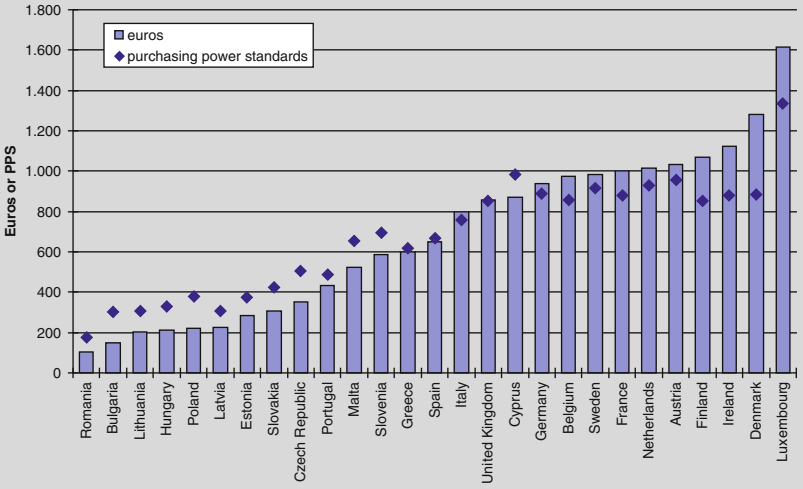

Fig. 2.1 Poverty threshold—2010 monthly disposable income for a single-person household—in Euros and in PPS. *Source*: SILC 2010, Income data 2009; except for UK, income year 2010 and for IE moving income reference period (2008–2009)

This information goes some way to meeting the concerns that the at-risk-of-poverty indicator risks being discredited. An at-risk-of-poverty rate for Luxembourg that is higher than that in the Czech and Slovak Republics needs information about the level of median household income in each country and therefore of the poverty threshold.

(continued)

Box 2.1 (continued)

Alternative methods to define poverty thresholds are being explored at EU level as a complement to the income-based poverty measures. Budget standard methods define poverty thresholds by reference to a basket of goods and services that are considered as necessary to reach an acceptable standard of living. Once agreed, the basket is valued using detailed price data. However, the selection of necessities raises a number of issues. A 2011 Commission study[9] suggests that methods based on the estimates of experts and focus groups usually produce quite "generous" baskets of goods, leading to thresholds "to be at or above relative poverty thresholds".

Table 2.1 illustrates that budget standard methods in the United Kingdom, Belgium (Flanders) and Austria resulted in amounts around or above the 60% of median income threshold. In the Netherlands, the method produced a much more "parsimonious" basket, probably because the purpose was to set a level for minimum income through parliamentary committees.

Table 2.1 Budget standard examples for a single person of working age

	UK Minimum Income Standard 2008	Netherlands NIBUD budget 2008	Ireland Vincentian 2006	Flanders CSB 2008
€ppp per year 2007 prices				
Food	2.499	1.761	2.949	1.604
Clothing	473	522	723	414
Fuel	558	881	327	1.107
Rent	3.240	3.403	2.921	4.169
Total necessities	6.770	6.566	6.921	7.294
Total budget	13.018	8.599	15.039	10.129
€ppp per year 2008				
Relative threshold	11.126	11.485	10.901	10.046 (Belgium)

Source: "The measurement of extreme poverty"—European Commission (2011) and EU-SILC

The use of budget standard methods can also help to illustrate what people living around the poverty threshold can afford in a given country or location.

Example: What can a family on 60% of the median income, adjusted for its household size, actually consume? The example of a lone mother with two children in Belgium

(continued)

[9] "The measurement of extreme poverty"—Bradshaw et al. on behalf of European Commission (2011).

Box 2.1 (continued)

	Euro/month	%
Food, clothes, shoes	508	35
Domestic goods and services	144	10
Telephone	24	2
Personal care	26	2
Health care	28	2
Transport	50	4
School	16	1
Leisure	106	8
Taxes, insurances	38	2
Rent private sector	351	25
Total budget	1.422	100

Source: B. Cantillon University of Antwerp

Methodological work in this area will continue at the EU level, and member states have been encouraged to develop this type of measures. However, the implementation of such methods at EU level raises important technical problems since the basket of goods has to take account of very different consumption patterns across countries. Ensuring that the thresholds measure comparable situation of hardship would require developed consumption data and prices harmonised at EU level, which the current framework for household budget surveys does not provide. The 2010 peer review on budget standards discussed these issues in more detail[10]; further work could build on this exchange of MS experiences.

- *Income-based indicators* reflecting the depth of poverty (poverty gap, poverty rate at different thresholds), the persistence of poverty (persistent poverty rate) or a "semi-absolute" measure of poverty (at risk of poverty anchored at a point in time) that captures the improvement of living standards resulting from economic growth.
- *Multidimensional indicators* covering poverty and social exclusion in the fields of material deprivation, work, education, health and housing, further complement these monetary indicators. Regional disparities and the specific situation of migrants are also covered.

The adoption by the Social Protection Committee of a material deprivation indicator in February 2009 was an important step in refining the measurement of social

[10] http://www.peer-review-social-inclusion.eu/peer-reviews/2010/using-reference-budgets-for-drawing-up-the-requirements-of-a-minimum-income-scheme-and-assessing-adequacy.

exclusion for two reasons.[11] Firstly, it provides a non-monetary measure of poverty—by referring to what people can afford, it implicitly takes into account the availability of accumulated resources (savings, durable goods, housing, etc.) that are not captured by current income. Secondly, it establishes an EU-wide standard since the same list of nine items is applied in all member states (thereby setting a common reference for all EU citizens). This represents a move towards an absolute rather than a relative measure, highlighting disparities in living standards across countries.

Statistical Sources to Compute Comparable Statistics on Living Conditions: The EU-SILC

The development of social inclusion indicators would not have been possible without EU investments since the early 1990s in the collection of comparable statistics on income and living conditions. The original European Community Household Panel (1994–2001) was replaced in 2005 by EU-SILC (Community Statistics on Income and Living Conditions).[12]

EU-SILC is now the reference source at EU level for social statistics and has helped strengthening EU social policy coordination by underpinning the analysis and the comparison of member states performance in the social field. A key objective of EU-SILC is to deliver robust and comparable data on total disposable household income. Income components were defined to follow as closely as possible the international recommendations of the UN "Canberra Manual".[13]

While much has been achieved more work is required to improve the measurement of poverty and social exclusion. The definition of resources needs to take into account imputed rent[14] and the value of in-kind services. The list of material deprivation items that were used in the definition of the Europe 2020 target is currently being revised to adjust the definition of material deprivation to the evolution of living standards in the EU. This should be done in time for the revision of the target in 2014. More could be done also to exploit the longitudinal component of the survey (some of the households are followed over a period of 4 years), thereby allowing better to capture the temporal dimension of poverty and exclusion. Finally, there is a strong consensus among users and producers of the data that timeliness needs to be significantly improved. The EU is exploring different options, including the possibility of producing early SILC results for key variables of the survey in cooperation with the European Statistical System[15], using alternative and more timely

[11] The deprivation indicator measures the enforced lack of at least four items from a list of nine (which include being able to pay one's rent and utility bills, facing unexpected expenses, being able to afford adequate heating and having a car, a telephone, etc.).

[12] EU-SILC Framework Regulation of the European Parliament and the Council (N°1177/2003).

[13] United Nations (2001) or http://www.lisproject.org/links/canberra/finalreport.pdf.

[14] Imputed rent is an estimate of the economic advantage of home ownership, compared to renters.

[15] European Statistical System represents Eurostat and the National Statistical Offices of the EU member states.

sources of information (such as monthly consumer surveys, the Labour Force Survey or administrative data collected through the SPC), as well as the use of micro-simulation tools to produce 'nowcasts' or forecasts of poverty trends (Euromod).

A Closer Look at the Europe 2020 Strategy and the Adoption of an EU Target to Reduce Poverty and Social exclusion

In June 2010, EU heads of states and governments committed themselves *to reducing poverty and social exclusion in the EU by at least 20 million people by 2020*.[16] Building on the work that had taken place over the last decade in terms of defining indicators of poverty and exclusion, the new EU target defined poverty and social exclusion on the basis of three main indicators: risk of poverty, material deprivation and jobless households.[17] Examining the recent dynamics of these three indicators in the EU-27 and in the EU-15 and NMS-12 (Fig. 2.2) helps clarify what they capture and why they have been included in such a central policy target. Four major findings stand out.

- First, the relative poverty rate and the severe material deprivation rate appear to capture very different aspects of poverty and exclusion. Indeed, while the first has

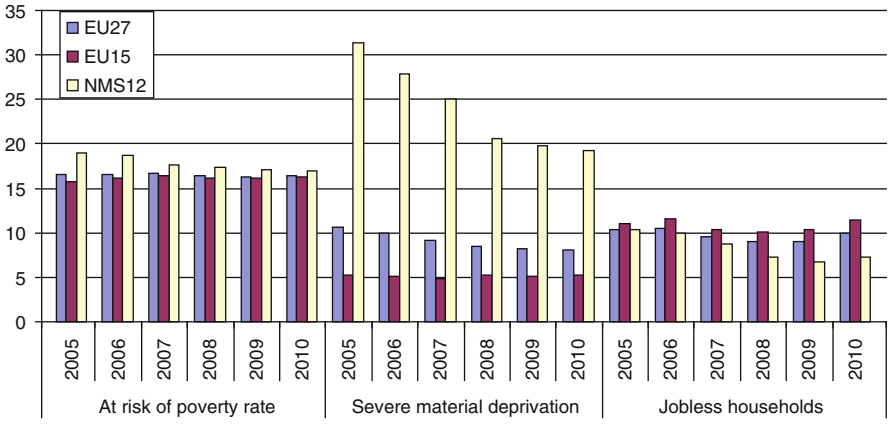

Fig. 2.2 Trends in poverty rates, material deprivation and jobless households, total population—2005–2010. *Source*: EU-SILC

[16] This target is one of three integrated objectives (with employment and education) to contribute to inclusive growth, defined as "*building a cohesive society in which people are empowered to anticipate and manage change and consequently to actively participate in society and the economy*".

[17] The indicator jobless households refers to the number of people, aged 0–59, not students, who live in a household where all adults did not work or worked less than 1 day per week in average over 12 months. This indicator is also referred to as "people living households with zero or very low work intensity".

been stagnating over the six years for which there are data, living standards in the new member states improved, when measured by severe material deprivation rates.[18] The improvement of the material deprivation rate in the new member states parallels the relative improvement of GDP per capita. The crisis has already put a halt to this improvement trend. The impact of the rise in unemployment during the Great Recession is most visible in the post-2008 increase in the percentage of jobless households, especially in the EU-15.

- Second, the risk-of-poverty measure encapsulates an approach to social exclusion aimed at capturing how people measure themselves against others in their society.[19] This might mean, as in the recent cases of Latvia, Estonia and the UK, that at times of crisis its reported incidence might decrease with the decline of median incomes to which it is anchored. The apparent improvement in relative poverty may reflect the fact that people with an income slightly below the poverty line may move above it as the line falls, even though their situation is unchanged, and may indeed have worsened. Note however that a decline in median income need not mean a decrease in this indicator, as illustrated by the cases of Spain and Slovenia.
- Third, the material deprivation indicator does capture absolute living standards. While it has remained stable at EU level in 2010, it has increased by over three percentage points for people at risk of poverty, pointing to a relative deterioration in living conditions among people with the lowest incomes. Similarly dramatic increases have been recorded in some countries where the crisis has been especially severe such as Lithuania and Latvia.
- Finally, the reversal of the decline in the incidence of jobless households closely mirrors the increase of the number of families having to rely entirely on social benefits.

In strong continuity with the overall approach adopted at European level, the Europe 2020 target recognises a multidimensional approach to fighting poverty and social exclusion. The three non-exclusive and overlapping dimensions underpinning the target make it possible to take into account the diversity of situation and priorities that prevail in the EU, notably after the accession of new member states with significantly lower GDP per capita.[20] This is illustrated by the Venn diagrams in

[18] The severe material deprivation rate provides a headcount of the number of people who cannot afford to pay their rent, mortgage or utility bills; keep their home adequately warm; face unexpected expenses; eat meat or proteins regularly; go on holiday; or afford to buy a television, a fridge, a car or a telephone. The indicator measures the percentage of the population that cannot afford at least 4 of the 9 items quoted above.

[19] By relying on definitions anchored in each country's median income, there are broad variations in the poverty lines adopted in different countries. Even if the values are expressed in purchasing power standards (PPS) to take account of the differences in the cost of living across countries, and even excluding Luxembourg as an outlier, the value of the poverty threshold in the richest countries is nearly five times higher than in the poorest.

[20] For a more detailed presentation of the new target and the diversity of populations and forms of poverty it represents, see Chap. 3 of *Employment and Social Developments in Europe 2011* (http://ec.europa.eu/social/main.jsp?catId=113&langId=en&pubId=6176&type=2&furtherPubs=yes).

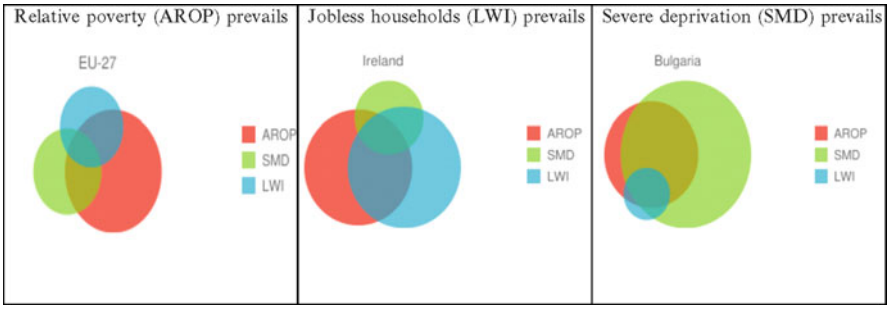

Fig. 2.3 The EU 2020 target and the heterogeneity of poverty and exclusion in member states. *Source*: EU-SILC 2010

Fig. 2.3. The diagrams represent the relative weight of the three indicators for the EU, Ireland and Bulgaria, illustrating the diverse profile of deprivation captured by the Europe 2020 target measure.

The poverty target, while an important headline figure and one that has raised the profile of the social agenda within the context of inclusive growth, does not exhaust all the facets of poverty that are part of the policy debate. Awareness-raising campaigns in the EU and the impact of the crisis have highlighted the situations of very severe forms of poverty and social exclusion that persist within the EU, such as those faced by the homeless, the Roma or people living in isolated rural areas. The Directorate General for Employment, Social Affair and Inclusion (DG EMPL) is working with diverse partners (Eurostat, the Directorate General for Regional Policies, the World Bank), to develop the specific measurement tools needed to monitor the situation of these people and other disadvantaged groups.

Another aspect that is not properly captured by the current measures concerns the role of services in actively supporting participation in society of people at risk of exclusion. DG EMPL (together with Eurostat and the OECD) is currently addressing this issue and trying to develop measures of access to services and the redistributive role of service provision.

A midterm revision of the Europe 2020 target is planned for 2015, notably to take account of the need to improve the measurement of poverty and social exclusion. The Council of Ministers has emphasised the need to improve the timeliness of data availability, to take into account the value of in-kind services and to review the list of material deprivation items in order to adjust the definition of the indicator to the evolution of living standards in the EU.

Key Policy Insights from the Analysis of Poverty and Social Inclusion in the EU Member States

Much has been learnt from the analysis of poverty and inclusion over the last decade. These key insights are briefly reviewed below:

Having a job remains the best safeguard against poverty and exclusion, since the risk of poverty faced by working age adults without work (unemployed or inactive) is more than three times higher than those in work (27% against 8%). Even before the crisis, about one third of the working age population in the EU was out of work, either unemployed or inactive. This is despite the increased participation of women as second earners and of older workers over the last decade, notably through the availability of part-time work.

Having, a job is not always a guarantee against the risk of poverty, and the working poor represent one third of the working age adults at risk of poverty. In 2010, 8% of the people in employment were living under the poverty threshold. Low pay, low skills, precarious employment and underemployment are important determinants of in-work poverty, as is work intensity in the household (i.e. situations where there are too few adults working in the household, or not working enough to earn a living) is another major factor. Single and lone parent households not working full time, as well as one-earner families, face the highest risks of poverty.

Certain groups appear to be persistently outside or at the margin of the labour market, often facing multiple barriers to entry. Factors such as low skills, care responsibilities, age, migrant background and other factors all contribute). Households in which nobody works face particularly acute challenges. There is a concern that the incidence of jobless households may become deeply entrenched, even with a resumption of growth.

The design of the tax-benefit system is a crucial determinant of income inequalities and the degree of redistribution to the poor. Important features include the progressivity of taxes and benefits, the degree of targeting and the conditionality of benefits. Evidence from member states shows that social transfers other than pensions effectively reduce poverty risks, but the degree to which they do so varies substantially across member states (ranging from a poverty reduction effect of 50% or more in some countries to 25% or less in others). This largely reflects differences in the size of expenditure, which vary from 17 to 33% of GDP. The composition of expenditure and the quality of interventions also play an important role. Available evidence also highlights a large variation across member states in net cash support to low-income households so that countries with similar levels of expenditure (excluding pensions) achieve quite different levels of poverty reduction, pointing to possible gains in efficiency. Finally, as other chapters in this volume highlight, poorly designed benefit transfers can create disincentive effects obstructing entry into labour markets.

Appendix 1. Current Formulation of the EU Policy Objectives on Social Inclusion

A.1. *The Open Method of Coordination for Social Protection and Social Inclusion*

The overarching objectives are to promote:

(a) Social cohesion, equality between men and women and equal opportunities for all through adequate, accessible, financially sustainable, adaptable and efficient social protection systems and social inclusion policies
(b) Effective and mutual interaction between the Lisbon objectives of greater economic growth, more and better jobs and greater social cohesion, and with the EU's Sustainable Development Strategy
(c) Good governance, transparency and the involvement of stakeholders in the design, implementation and monitoring of policy

The social inclusion objectives:
Among the 2006 streamlined objectives of the social OMC, the specific objective applying to the social inclusion strand is to have *a decisive impact on the eradication of poverty and social exclusion by ensuring*:

(d) Access for all to the resources, rights and services needed for participation in society, preventing and addressing exclusion and fighting all forms of discrimination leading to exclusion
(e) The active social inclusion of all, both by promoting participation in the labour market and by fighting poverty and exclusion
(f) That social inclusion policies are well coordinated and involve all levels of government and relevant actors, including people experiencing poverty, that they are efficient and effective and mainstreamed into all relevant public policies, including economic, budgetary, education and training policies and structural fund (notably ESF) programmes.

Europe 2020[21]: A Broad Definition, with a Strong Focus on Labour Market Integration

Guideline 10: Promoting social inclusion and combating poverty
The extension of employment opportunities is an essential aspect of member states' integrated strategies to prevent and reduce poverty and to promote full participation

[21] Council Decision of 21 October 2010 on guidelines for the employment policies of the member states (doc 2010/707/EU).

in society and economy. Appropriate use of the European Social Fund and other EU funds should be made to that end. Efforts should concentrate on ensuring equal opportunities, including access for all to high-quality, affordable and sustainable services, in particular in the social field. Public services (including online services, in line with guideline 4) play an important role in this respect. Member states should put in place effective anti-discrimination measures. Empowering people and promoting labour market participation for those furthest away from the labour market while preventing in-work poverty will help fight social exclusion. This would require enhancing social protection systems, lifelong learning and comprehensive active inclusion policies to create opportunities at different stages of people's lives and shield them from the risk of exclusion, with special attention to women. Social protection systems, including pensions and access to health care, should be modernised and fully deployed to ensure adequate income support and services—thus providing social cohesion—whilst remaining financially sustainable and encouraging participation in society and in the labour market.

Benefit systems should focus on ensuring income security during transitions and reducing poverty, in particular among groups most at risk from social exclusion, such as one-parent families, minorities including the Roma, people with disabilities, children and young people, elderly women and men, legal migrants and the homeless. Member states should also actively promote the social economy and social innovation in support of the most vulnerable. All measures should also aim at promoting gender equality.

Chapter 3
Measuring Poverty in the Western Balkans: Recent Trends and New Challenges

Calogero Carletto, Caterina Ruggeri Laderchi, and Sara Savastano

Introduction

As countries in the Western Balkans proceed on the path to accession to the European Union (EU), they need to strengthen their statistical tools for measuring poverty and social inclusion and align them to the requirements set forth by the European *Acquis Communautaire*. This is one of the major challenges facing Western Balkan countries in the area of statistics. As discussed by Maquet Engsted in the previous chapter, a well-established set of indicators of social inclusion has been developed at the European level, and monitoring them will increasingly become a priority. Countries in the region have progressively developed statistical systems which are currently at different stages of transition to a full European model. Adopting and implementing the statistical chapter of the *acquis* requires a modern and sophisticated administration and set of institutions, as well as a harmonized statistical system to generate statistics that are comparable across countries, over time, and across domains for different populations of interest.

While EU member countries now rely primarily on the European Union Statistics on Income and Living Conditions (EU-SILC) survey to produce on a regular basis the required indicators on poverty and other forms of deprivation, countries in the Western Balkans still measure poverty using different instruments and lag behind in terms of standardization to common methodologies. While, ultimately, for full accession, conformity to European requirements is nonnegotiable in the long run,

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because of the characteristics of many of the economies in the Western Balkans, immediate full compliance to EU-SILC may be neither feasible nor desirable. In an attempt to map a more practical and sensible pathway towards full adoption of common methods to measure poverty and social exclusion in the Western Balkans, an Expert Group (EG) composed by representatives of Eurostat, the National Institute of Statistics of Spain (INE) and Italy (ISTAT), and the World Bank was established in 2008. One of the main goals of the group was to provide some guidelines on whether and how countries in the Western Balkans at different stages of development and with different timelines towards EU accession should adopt the EU-SILC while still collecting consumption data as well as other sectoral information for policy-relevant analysis.

This chapter aims at illustrating the different methodologies for the measurement of monetary poverty currently in use in the countries in the Western Balkans, with the purpose of establishing the elements of a possible strategy to move countries toward a common methodological approach based on the recommendations of the expert group. This chapter is organized as follows: in the next section, we describe the two most commonly used aggregates for the measurement of poverty and highlight some of the theoretical and practical considerations underpinning the choice of one *vis-à-vis* the other. The following section illustrates the different options available in terms of survey instruments and how well each would fare in terms of measuring monetary welfare in the Western Balkans context. We conclude in the last section by suggesting a few points of a road map for countries to follow in their transition to a full SILC, also based on the recommendations of the EG.

Choosing the Most Relevant and Viable Concepts

Poverty is a multidimensional concept that can be captured using monetary and nonmonetary measures, as well as by means of subjective assessments of overall household well-being. Recognizing that monetary poverty is only one facet of these multiple dimensions, in this section, we focus our discussion on the conceptual underpinning and practicalities behind the choice of a particular measure of monetary welfare in the context of the Western Balkans, which we then relate to alternative options in terms of available data collection instruments.

Broadly speaking, the debate on the measurement of monetary welfare has often centered around the choice of income versus consumption as the better approximation of long term welfare (Deaton and Grosh 2000, McKay 2000). Although it is ultimately the concept of "permanent income" that one wants to capture, in many situations, there are both theoretical and practical considerations warning against the use of an income aggregate. The difficulties in measuring income have been documented by Deaton (1997), among others, who states that "the practical and conceptual difficulties of collecting good income data are severe enough to raise doubts about the value of trying." Without taking such an extreme view, but remaining conscious of the inherent difficulties of properly measuring income, there are a

number of limitations involved in constructing a convincing income aggregate. Those lie primarily in the systematic underreporting of income due to the high level of informality in employment and the heavy reliance of own production of goods and services for own consumption. In addition, income is much more subject to seasonal fluctuations than consumption, for example, because of the interannual variation of cropping seasons and the occasional nature of many informal activities. Furthermore, where many of the income earning activities are small and informal, record keeping is not common, rendering difficult the proper estimation of net returns from both farm and nonfarm activities. Finally, the sensitivity of income information can potentially result in high nonresponse rates among nonrandom segments of the population, thus leading to potential estimation bias.

As an alternative to income measurement, an aggregate gauging the total level of consumption expenditure of the household in relation to an annualized reference period is more commonly used to adequately measure household welfare. Measuring welfare using consumption expenditures, however, is not immune to problems. Despite the progress and achievements of the past few decades, no clear standards exist on best practices. For example, while collecting consumption expenditure information using a diary is often considered preferable to recall methods, no consensus exists on the specific reference period, as reflected in different countries adopting periods of varying lengths. In the case of diaries, ambiguities persist on the use of closed *vis-à-vis* open lists of expenditure items to be recorded as well as on the actual list of items included. Irrespective of the survey method or reference period used, annualization of consumption expenditure information collected through a household survey presents some challenges, particularly when the data collection is based on a single visit in the course of the year. However, consumption expenditure data, when properly collected on a fairly comprehensive list of items, is often preferred as it is easier to collect, less sensitive to exogenous shocks and seasonality, and more stable than income, particularly in contexts analogous to those in several of the countries in the region.

The choice between income and consumption is often made based on practical rather than theoretical considerations, given that neither measure is easy to collect and both are rather expensive (Deaton and Grosh 2000). However, it is important to note that the usefulness of income information goes well beyond its potential use as a measure of poverty, particularly the information on its different sources. Estimating the different components of income provides a picture of households' livelihood strategies and is fundamental to gaining a better understanding of poverty. A similar argument can be made for consumption data, since consumption and expenditure data also have multiple applications, including nutritional analysis or the study of the effect of specific categories of expenditures, such as spending by the household on the education and health of its members. Thus, despite the main limitations and the difficulties associated with collecting good-quality data on each, because of their respective analytical advantages, countries should ideally collect information on both. The question that arises is whether both types of information can and should be collected from the same households and for the same reference period. Countries in the Western Balkans are currently faced with this conundrum, as they

decide whether to adopt an income-based instrument such as the EU Statistics on Income and Living Conditions (EU-SILC) or to pursue other options such as a Household Budget Survey (HBS) or an Integrated Household Survey *à la* Living Standards Measurement Study (LSMS) surveys. In the next section, we highlight the strengths and weaknesses of the different survey instruments options and summarize some of the countries' experience to date with each type of instrument.

Picking the Right Tool in a Crowded Box

There are several surveys which collect detailed information on income and/or consumption that can be used to monitor poverty. Among these, the three most viable options for the Western Balkans are EU-SILC, LSMS, and HBS. While in this section we focus on the above three, Table 3.1 in Annex 1 provides a more detailed overview of existing surveys produced in recent years in countries in the region.

EU Statistics on Income and Living Conditions

Until 2001, the European Community Household Panel (ECHP) (1994–2001) was the primary source of information used by Eurostat to compute many indicators in the field of income, poverty, and social exclusion, such as the structural indicators of social cohesion, indicators of pension adequacy, indicators of poverty and aging, and many other indicators published on the Eurostat New Cronos database. The ECHP was a pioneering data collection instrument, launched in 1994 under a "gentlemen's agreement" between the member states. As such, it ended up suffering from several shortcomings in terms of poor availability and timelines of data, high attrition rates, nonintegration of the survey in some national statistical systems, and definitional differences across member states. To overcome some of these problems and as a result of discussions at subsequent EU summits (held in Lisbon, Nice, Stockholm, and finally Laeken), the ECHP has been replaced by the EU-SILC under the Framework Regulation 1177/2003.

The main scope of the EU-SILC is to collect cross-sectional and longitudinal data on income, social inclusion, and living conditions. In contrast to the ECHP, it does not rely on a common questionnaire but on the idea of a "framework": a harmonized list of target primary and secondary variables to be transmitted to Eurostat based on common guidelines and procedures, along with common concepts (e.g. household and income) and classifications aimed at maximizing the comparability of the information produced. The implementation of EU-SILC is compulsory for all EU member states. While for the longitudinal component a 4-year rotational panel is recommended by Eurostat, EU-SILC is meant to be implemented annually with a common component every year (primary variables) and rotating modules which are

alternated in different years (secondary variables). The EU-SILC multipurpose instrument includes information to be collected at the household and information to be collected at the individual level. For example, material deprivation indicators and housing condition information is collected at the household level; labor, education and health information is collected for persons aged 16 and over; income is collected at the individual level with great detail, though some additional components are included in the household section. Data obtained from the EU-SILC are used in the two Open Methods of Coordination (OMC) on social inclusion and pensions. For social inclusion the key indicators are those needed to monitor the poverty reduction targets of the Europe 2020 strategy (at risk of poverty rate, workless households, material deprivation, see Chapter 2 and European Commission 2010).

EU-SILC, since its launch in 2003, has become the EU reference source for income and social exclusion statistics for all member states. Coverage expanded to 15 countries by 2004 and to 25 EU plus Iceland and Norway by 2005. Among the latest countries to introduce a EU-SILC in their household survey systems are Bulgaria (which launched the EU-SILC in 2006) Romania, Turkey, and Switzerland (2007); Croatia 2008, (test implementation) (Atkinson and Marlier 2010); and the Former Yugoslav Republic of Macedonia (2010, test implementation). A few other countries such as Serbia and Albania are contemplating conducting a EU-SILC in the near future.

Living Standards Measurement Study

The Living Standards Measurement Study (LSMS) program was established by the World Bank in the early 1980s in order to explore methods for improving the type and quality of household data collected by statistical offices in developing countries for the measurement of poverty and to inform policy analysis. From its inception, one of the main objectives of the LSMS was the estimation of a consumption-based measure of welfare in conjunction with the collection of a wide range of policy-relevant sectoral information. This allows the study of the distributional impact of policies and of household and individual behavioral responses to policies and/or environmental changes. The LSMS also collects fairly comprehensive information on the different components of income at either individual (wage income) or household level (nonwage and non-earned income). Due to their multi-topic nature, LSMS surveys are well suited to analyze the relationships between sectors, for example, between farm and nonfarm activities, and to understand better the determinants of particular outcomes. As policies and environmental circumstances differ across countries, the data collection instruments are tailored to suit the needs of the local context in each country. The thematic content of the questionnaires may vary across country and over time, as policy questions and data requirements tend to differ from country to country. In terms of frequency, in light of the complexity of the instrument, the initial recommendation was to carry out an LSMS-type survey every 3–4 years. However, very few countries have been able to maintain such periodicity,

as the implementation of LSMS surveys is often demand driven and linked to uncertain and irregular funding flows.

In the Western Balkans, (Table 3.1 of Annex 1), four out of the six countries in the region have implemented at least one LSMS survey, but only Albania has conducted such surveys fairly regularly since 2002. In the case of both Bosnia-Herzegovina and Albania, the LSMS surveys were initially run as panels. The adoption of the LSMS has been fully internalized only in Albania, as after the World Bank support ended, the government sought alternative sources of funding in order to repeat the survey in 2008 and in 2012. The Albania LSMS has been particularly innovative providing a novel approach to measuring migration in household surveys, including the tracking of migrants to destination countries, introducing diaries to collect food consumption expenditures and making the microdata publicly available.

Household Budget Surveys

Household Budget Survey (HBS) are another type of survey conducted in the region with partial geographic and temporal coverage. These surveys are mainly designed to provide information for the periodic updating of the consumer price index and for harmonizing the system of national accounts, but have been used for poverty measurement as they monitor household expenditure. Despite a common focus on expenditures of private households in different population groups, the HBSs conducted in the region exhibit differences in terms of design and coverage and are not conducted yearly in all countries of the Western Balkans (see Table 3.1 in Annex 1). Some of the advantages of HBS are the high level of disaggregation of the expenditure items (based on the Classification of Individual Consumption according to Purpose or COICOP), and that the collection of expenditure data is based on diaries. In order to meet increasing data demands and lacking complementary sources of data, countries have occasionally used HBS for additional analytical purposes by expanding the thematic coverage of the survey instrument. This has been the case, for example, in Kosovo, where a migration survey linked to the HBS was run in 2009.[1] Among the limitations of the HBS for the purposes of monitoring welfare is their coverage, which in some cases is restricted (e.g. in Albania the HBS was at least initially run only in urban areas), and the fact that they do not collect food quantities.

[1] Note that as the HBSs in the region are run as continuous fieldwork, it is difficult to add on the HBS sample an ad hoc module in the same way in which it is possible to add modules to surveys which are conducted as "one shot." In Serbia, for example, the Labour Force Survey that is run twice a year is often used to add additional modules or even add purposively designed samples and modules, in order to explore specific research questions.

In summary, over the past two decades, countries in the Western Balkans have implemented a number of surveys to monitor poverty. Much has been achieved both in terms of improving the availability and quality of poverty figures, but much remains to be done in both areas, as well as in terms of standardizing the methodologies used to measure welfare. To date, most poverty estimates have been consumption based, whether from HBS- or LSMS-type surveys. However, as countries in the region continue on the path to accession, the need to comply with all chapters of the *acquis* is pushing them towards the adoption of the EU-SILC. In the next section, based on the recommendations of the Expert Group, we describe a possible road map for countries to transition to full compliance with the *acquis*, given their current data needs and the the capacity of their statistical systems.

The Transition Toward SILC

While all EU member countries have by now fully integrated EU-SILC into their statistical reporting systems, the countries in the Western Balkans are now considering adopting the survey at least as a learning experience. As recommended by the Expert Group (EG), as different countries are at different stages of development and with asymmetric horizons to accession, it seems appropriate for each one of them to take a somewhat different path toward full adoption of EU-SILC. The EG examined several examples of surveys carried out in the region in relation to those collected in other EU member countries. Such cross-country comparison was used to identify the largest common denominator in terms of data availability and frequency of data collection and to put forth recommendations on the feasibility for the countries in the region to move toward EU-SILC. One of the main issues was how to collect information for the construction of a consumption-based measure of welfare and of additional policy-relevant data similar to the type of information gathered in a typical LSMS within a system which would probably also include an HBS and eventually an EU-SILC with information on the different components of income.

While in the long-term perspective, the EU-SILC is a requirement for EU accession under the *acquis*, it was recognized that given the distant accession prospects for some of the countries, implementing a full EU-SILC would be appropriate and feasible only for few of them. The proposal was to adopt, at least in the shorter run and for countries with a more distant prospect of accession, a so-called extended HBS (HBS+, Table 3.2). This would be achieved by adding a limited number of policy-relevant modules to existing or planned HBS in order to expand the thematic coverage of the survey, including a limited set of EU-SILC-type information within the same instrument. This would allow the construction of a consumption-based measure of welfare and the collection of additional policy-relevant data. The HBS+ would include a core module with information on demographics, housing, education, health, employment, migration, and social exclusion and deprivation, and detailed modules aiming at producing fairly comparable income and consumption

measure to monitor both Laeken indicators (income based) and poverty measures based on consumption expenditure.

The EG recognized that collecting comprehensive income information within an HBS+ may not always be feasible and should be considered with extreme caution. When such income information was to be included, the guiding principle adopted was the definition proposed by the Expert Group on Household Income Statistics, aka the Canberra Group, which is also the approach followed in large part by the EU-SILC. For what concerns consumption expenditure, the main objective of the review was to assess the possibility of collecting comprehensive consumption expenditure information for the construction of consumption aggregate and an absolute poverty line while also complying with Eurostat standards and classifications. The option was considered feasible, and particularly for countries farther away from accession and with high levels of informality and relatively large agricultural sectors, poverty should continue to be measured using consumption expenditures.

Although often HBS does not contain information on quantities of goods consumed, it was suggested that the HBS for the Western Balkans should include quantities, convertible in standard units, even if that would imply reducing the number of items being considered in order to maintain the length of the module to a manageable size. As this would probably have some implications for national account purposes and the CPI updating, changes to the list and the level of disaggregation should be carried out in concurrence with national account experts.

The recommendations made by the EG have been discussed and disseminated in the region and have also been piloted in Bosnia-Herzegovina (BiH, also Chap. 6). As the data of the Extended Household Budget Survey 2011 for BiH are not yet available, it is not yet possible to analyze the success and sustainability of this experience, but the initial results are encouraging. Certain aspects of the project, such as the development of a very active data user group which made significant contributions to questionnaire development, for example, can be considered successes in themselves as the process created significant awareness about the effort to collect better and more comprehensive data for policy making and to get the statistical system ready for a future accession.

In conclusion, the EG has charted a clear path for countries in the Western Balkans to adapt their statistical system to the requirements of the *acquis*. Such path allows for flexibility, taken into consideration the different starting points and accession prospects of different countries. This approach also offers the clear advantage of continuity of existing series of poverty estimates, while gradually integrating new elements—and in particular the indicators monitored in EU Member States as part of the Europe 2020 targets—into the statistical system. A managed transition should also ensure that resources can be used efficiently, as the running in parallel of both EU-SILC surveys and HBS can prove expensive in terms of both human and financial resources.

As of today, countries appear to be approaching the statistical developments required by the accession process in different ways—though mostly along the lines of a smooth adaptation suggested by the EG. While Macedonia FYR has already introduced a EU-SILC survey in parallel with the HBS, Bosnia and Herzegovina has piloted the EHBS; Albania and Kosovo are integrating EU-SILC variables in the design of the LSMS and HBS, respectively; and Serbia is considering testing the integration of consumption modules in the SILC structure. Much will be learnt from comparing these different efforts, opening up a new area for mutual learning. To the extent that both consumption- and income-based indicators will be calculated, these experiences will also offer useful insights on the relative benefits and informational content of different poverty definitions and of anchored measures of poverty which might be relevant also for the ongoing debates taking place among EU member states.

Appendix 1

Table 3.1 Main household surveys collected in the Western Balkans

	Albania	Bosnia and Herzegovina	Kosovo	Macedonia	Montenegro	Serbia
Census	2001, 2011	1991, 2012	2011	2002	2003, 2011	2002, 2012
LSMS	2002, 2003, 2004, 2005, 2008, 2012	2001, 2002, 2003, 2004	2000			2000, 2002, 2003, 2007
HBS	2000, 2007, 2008	2004, 2006, 2007, 2008	2003–2009	2000–2009	2005–2009	2003–2009
LFS	2000–2009	2007–2011[a]	2002–2006, 2008	2000–2009	2005	2000–2009
MICS	2002, 2005	2000, 2006		2005	2000 and 2005	2000 and 2005
DHS/ RHS	2002, 2008	No	No	No	No	No
LITS	2006, 2010	2006, 2010	No	2006, 2010	2006[b], 2010	2006, 2010
UNICEF/ UNDP	2009	2009	2009	2009	2009	2009

Note: *HBS* Household Budget Survey, *HPS* Health Promotion Survey, *LFS* Labour Force Survey, *LSMS* Living Standards Measurement Survey, *MICS* Multiple Indicator Cluster Survey, *RHS* Reproductive Health Survey, *LITS* Life in Transition Surveys, *DHS* Demographic and Health Surveys

[a]Information LFS in BiH are available at http://www.fzs.ba/Eng/ars2007.htm

[b]The 2006 round was done jointly for Serbia and Montenegro

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Chapter 4
Qualitative Research to Support the Analysis of Social Inclusion in the Western Balkans

Carrie Turk

Introduction

Motivated in part by the pathway to EU accession and in part by the imperative to respond to difficult and unstable economic realities, the Western Balkans has become a dynamic policy environment. Even with the improvements in survey quality (see Chap. 3), many questions regarding the possible impacts of policy reforms on poor or more vulnerable groups remain unresolved by quantitative analysis. This is particularly true when:

- **Policy challenges are directed at, or may have impacts on, groups that are less visible in household survey datasets** such as groups that are unidentifiable in household surveys because identifiers do not exist for them or because the number of observations would be too small for meaningful analysis; households at the lower end of the income distribution who are poorly represented by average estimates of the bottom decile; and people who may somehow be excluded from the sampling processes for household surveys, such as migrants or people without formal addresses.
- **Impacts are possible at levels of aggregation or disaggregation that surveys are not designed to provide**. For instance, impacts may vary within the household according to gender or age of household members or may occur at the community level.

The findings, interpretations and conclusions expressed in this chapter are those of the author and do not necessarily reflect the views of the International Bank for Reconstruction and Development/ The World Bank and its affiliated organisations, or those of the Executive Directors of The World Bank or the governments they represent. The World Bank does not guarantee the accuracy of the data included in this work.

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- **Factors that cannot be observed in household surveys are important in determining the impacts of reforms**. For example, behaviours of individuals and households influence the positive and negative impacts of policy reforms, but incentives and motivations for these behaviours are often complex and hard to understand based on quantitative analysis. In addition, in some instances, household surveys may not be available to capture rapid change, for example, in assessing the impacts of recent economic shocks.
- **Understanding the *perceptions* of the impacts of reforms is critical to either advancing or blocking progress in policy change**. If the benefits of policy reform are less evident to citizens or certain interest groups than the costs of policy reform, there may be a need for a clear communication strategy that is well directed at addressing misinformation and misunderstandings. Questions about opinions on reforms are not routinely available in household surveys.

Qualitative research can play a key role in addressing these knowledge gaps and ensuring a comprehensive evidence base for policy design. To support its policy dialogue in the Western Balkans, and particularly in Serbia and Albania, over the last 2 years, the World Bank has designed and commissioned a number of studies, including:

- A study of the impacts of the economic crisis in Serbia, involving 18 focus groups and 15 in-depth interviews in four communities. This focused strongly on Roma households (half the focus groups) and other vulnerable groups (single mothers, internally displaced persons (IDPs) and rural households with small landholdings) IPSOS Strategic Marketing 2009).
- A study of the robustness of pensioner livelihoods in Serbia, covering 18 focus groups and 11 in-depth interviews in five parts of the country. This included elderly people in both urban and rural areas and those residents in IDP settlements and covered groups drawing pensions from different sources (IPSOS Strategic Marketing 2010b).
- A study on gender and decision-making in Serbia, contributing to a multi-country research exercise in 20 countries. This involved 16 focus groups (including two pilots) in five locations (one Roma community) and included younger adult men and women and older adult men and women in equal numbers. It also involved a community questionnaire (IPSOS Strategic Marketing 2010a).
- A study on barriers to accessing the *Ndihma Ekonomike* social assistance programme in Albania. This covered 30 focus groups in six locations (one Roma community), designed to capture a range of poverty situations (IDRA 2011a).
- Studies in Albania and Serbia, exploring the possible impacts of energy reforms on vulnerable households. In Serbia, the research involved 12 focus groups in six sites and 12 in-depth interviews with administrators of benefit schemes and energy consumers. In Albania, the research covered 30 focus groups in 12 sites (including one Roma site) and nine in-depth interviews. In Serbia, groups were divided first by location and by receipt (or not) of social assistance transfers. In Albania, groups were divided by location, by receipt (or not) of social assistance transfers and by whether participants were currently payers or defaulters on their electricity bills (IDRA 2011b, IPSOS Strategic Marketing 2011).

- A study in Albania on perceptions of the benefits and problems with disability allowances. This covered 12 focus groups in six sites, divided between beneficiaries and carers of beneficiaries of disability *allowances* and beneficiaries and carers of beneficiaries of disability *pensions* and incorporating focus groups with disabled Roma people (IDRA 2011c).
- A study, currently being piloted in Albania, to understand factors underpinning student preferences and incentives with respect to tertiary education.

This work draws its inspiration from a body of work on participatory poverty analysis, which emphasises the value of listening to people's own descriptions and definitions of poverty rather than measuring concepts of poverty that are predefined through closed-ended questions in fixed questionnaires (Norton et al. 2001). With its roots in anthropological research approaches, research techniques have been developed (much of this work pioneered by Robert Chambers during the 1980s) to respond to the challenges faced by development practitioners and have, over the last two decades, been absorbed into the mainstream toolkit of development research (Chambers 1983). This approach is therefore different from others that often rely on qualitative research, such as the focus on subjective wellbeing illustrated in Chapter 8. High profile exercises such as the *Voices of the Poor* research conducted by the World Bank (Narayan et al. 2000) have helped to popularise the use of many of the techniques described in this chapter. More recent incarnations of this work have experimented with methods that generate simple metrics as part of the exercises (e.g. Chambers 2007) and the discussions and literature around "participatory statistics".

This chapter documents some of the insights learned from these exercises, both in terms of methodology development and in terms of findings. The first section focuses on the methodological aspects of designing the research and illustrates the studies' outputs with reference to a concrete example. The next section highlights the type of insights that these studies have provided with respect to two areas which have been explored most extensively, that is, the effectiveness and impacts of social assistance of last resort and the conditions of the Roma. These practical illustrations are both interesting per se and help explaining the contribution of well-designed qualitative research for policy diagnostics. A final section concludes.

Designing the Research

Qualitative research techniques are often used to provide a rapid assessment of particular situations or groups. Their ability to generate a lot of information from a large number of people makes them extremely valuable in identifying a breadth of issues concerning social exclusion from different stakeholders. The studies under discussion in this chapter, however, were oriented around very specific questions of policy design for social inclusion, such as "can we use an existing social assistance mechanism to provide reliable support to the poor as electricity tariffs rise?" or "what will be the likely impact of a pensions freeze and how will different groups of pensioners cope with this?" or "what impact will the introduction of student loans

have on decision-making processes for prospective university students?" As these studies were not intended as broad information-gathering activities, they required carefully constructed exercises that could deliver guidance on specific aspects of the reforms being designed. Some of the issues which arose in designing the methodology are highlighted below. In particular, these are related to defining the real value added of the qualitative work, refining the scope to ensure that the key policy questions are covered and framing the exercises to allow a policy-oriented analysis.

Maximising the Value Added

Design work for most of the research exercises was preceded by two important exercises, which strongly enhanced the value added of the research. A thorough *review of the policy arena* for the topics involved was critical in isolating the possible impacts of reforms that might be most important for poorer or more vulnerable groups. In some instances, this involved probing into the micro-detail of, for example, procedural reforms so that exercises could be designed to gather feedback on specific elements of those reforms in a concrete manner. This is not always as straightforward as it sounds; policy documents were often vaguely phrased, and frequently there were considerable departures between policy on paper (and the proposed reforms) and current implementation practice. Untangling the specifics of policy change involved many in-country interviews and discussion beyond the review of paperwork. This work was important in framing the methodology. For example, as the research work on access to *Ndihma Ekonomike* transfers was being developed, it became clear that the complex regulations already in existence to define eligibility were, in reality, applied with some considerable variation. This raised the question of whether the research should be based around changes in policy or on actual practice and led to the inclusion of comparable exercises in focus groups with beneficiaries, non-beneficiaries and officials asking participants to describe the flow of activities they either encountered during application/validation (for beneficiaries) or applied during these processes (for officials).

In addition, *quantitative analysis of household survey data* was extremely helpful in pinpointing the groups that should be included in the sample. Quantitative analysis of expenditure data for households with elderly heads in Serbia, for example, led the team to focus on rural pensioners with smaller landholdings as a priority because of their relative income poverty. Quantitative analysis of the recipients of disability-related cash transfers in Albania led the team to divide the sample to look at disability pensions and disability allowances separately. Modelling work using household survey data that analysed the exclusionary effects of existing criteria (see Chapter 16) for eligibility for social assistance in Albania was used to identify participants in the research on access to the *Ndihma Ekonomike* scheme. More broadly, the starting point of the qualitative work was generally located where nationally representative quantitative data was unable to probe further.

Narrowing the Scope

In every case, the team had more questions than could be addressed during a focus group discussion and was interested in capturing more population subgroups than could be accommodated within the budget.

Keeping focus groups to a 1.5- to 2-h limit confined the research to four or five discussion-led exercises, and the first challenge to the design team was to identify the priority four of five big questions that could be addressed in this format and that would work together to build a coherent, smooth-flowing discussion. As a rule, this was not a quick process. Following the predesign work (above), design would typically involve a brainstorming session with methodology and sector specialists, followed by a draft design, and a brainstorming involving the whole research team. The process continues with a revised design, piloting attended by the methodology specialists and sector specialist often through web streaming) a subsequent brainstorming and the finalisation of the design. Frequently at the piloting phase, the research tool would include a combination of exercises, some in which the team were fairly confident would deliver interesting results to the relevant questions and would be manageable from a facilitator's perspective and some of which had more question marks regarding their workability. Piloting was extremely important in dropping some exercises, merging other exercises and modifying other exercises. Piloting of a module on domestic violence in Serbia, for example, allowed the team to develop an abbreviated exercise which could be incorporated into other focus groups rather than needing to stand alone as a separate focus group.

The value of a focus group format is maximised when the exercises and discussion engages all participants; if only one participant can engage in a meaningful way with the topics and exercises, then the focus group format adds little over a straightforward, one-on-one interview. One of the objectives in the piloting process is to weed out issues that might be pertinent to the research, but which waste time in a packed focus group. These issues were flagged by research teams as issues to be followed up bilaterally with particular participants in a mini-case study format to avoid boring the other focus group participants who were not informed of/interested in that specific issue. All of the research exercises complemented the focus groups with in-depth interviews or case studies to provide additional detail on specific lines of enquiry without interfering with the efficiency of the focus group.

The design process inevitably involved narrowing the number of population subgroups that were covered, and a repeated challenge to the design team was balancing the breadth of different perspectives (suggesting the need for as many diverse subgroups as possible) and ensuring a depth of results that could be meaningful. In all cases, the research sample ended up having both rural and urban components and, in most instances, had an emphasis on poorer groups. In most exercises, Roma communities were identified as a group that required particular and separate attention. Some samples were established to provide a comparison between participants and nonparticipants of particular government programmes. All studies that were concerned with impacts of reforms on delivery of services included focus groups

with service providers, and comparisons between service user and service provider responses were often particularly useful, particular with respect to understanding, on the one hand, where users have most difficulty in ensuring access and, on the other hand, understanding the constraints that providers were facing at those same moments in processes of securing access.

Designing to Frame the Analysis

All of these research exercises were designed to bring evidence to policy development processes. Teams were particularly concerned that the analysis should go beyond descriptions and quotes to provide a capacity to benchmark across groups (possibly with an eye to benchmarking over time) and to provide indications of priority, scale and intensity. In all of these studies, the research methodology is framed around a number of exercises, each of which produces simple tables or charts that can either be aggregated or can be compared. Clearly the estimates produced have no statistical credibility because numbers are small and sampling is not random, but they do provide a focal point for the analysis and they do provoke easy questions of the kind "why this group scores problems in this way and that group ranks them differently".

As an example, one of the research exercises was intended to explore the impacts of energy sector reform on poor households. The reforms were likely to increase the price of electricity and, possibly, change approaches of electricity companies towards their management of payment defaults. The purpose of the research was to understand patterns of electricity use and expenditures (not necessarily aligned for poor households), understand how they cope with peaks in expenditures and gather their responses to a number of possible options for supporting them through the transition. There was a specific interest in understanding whether the programme to provide poor households with cash transfers would be an appropriate vehicle for providing support. The focus group was structured around three areas of enquiry: energy use patterns during the year, how households cope with energy expenditures and the usefulness of existing/new support mechanisms. Each of those areas of enquiry had an output that in some way assigned measures to the perceptions expressed during the discussion.

The first area of enquiry on energy consumption involved the group development of approximate graphs representing consumption of different fuels for different months of the year. This exercise generated a lot of discussion about how households decide on energy use and which months are most difficult in terms of meeting energy needs, but it also provided the research team with a relatively clear way to analyse patterns between different groups and between users of different energy sources and to assess where the areas of maximum stress occur for different groups. Figure 4.1 illustrates what these findings look like comparing urban and rural dwellers, but the team also presented comparisons for participants who were recipients of social assistance and for those who were non-recipients.

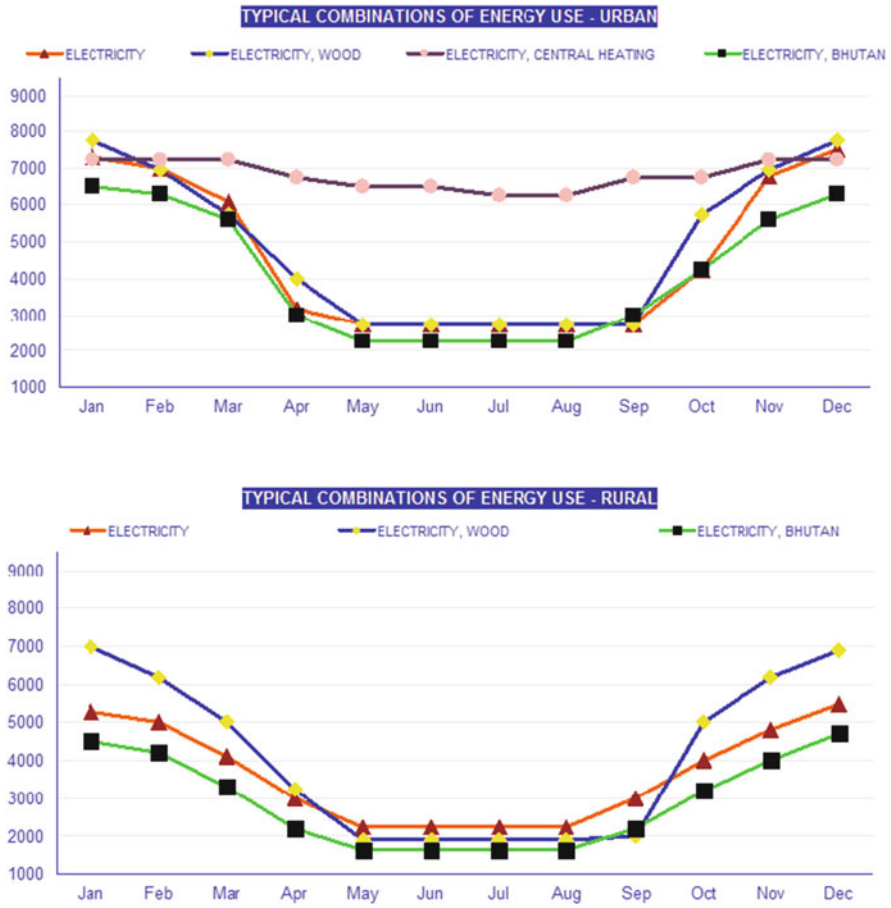

Fig. 4.1 Output from focus groups comparing energy consumption across groups in Serbia. *Source*: IPSOS (2011)

The second area of enquiry, on how vulnerable people manage energy payments, involved, as the discussion evolved, the construction of a table where participants listed the strategies they used to manage energy bills, performed a count to judge the frequency with which the strategy is used, ranked those strategies with respect to the efficiency of the strategy and listed the advantages and costs of those strategies. Consolidating these findings across groups in a table highlighted that urban households favour borrowing money as a way of paying unaffordable bills, while rural households would often, as a first resort, default on their payments.

The third area of enquiry explored the degree to which households were accessing social assistance mechanisms and why; and probed on whether certain mechanisms would provide suitable tools for supporting poor households as reforms in the energy sector increased their energy costs. The discussion delivered several structured outputs. The first was a table detailing the schemes that participants knew

Table 4.1 Focus group scores on possible scenarios for assistance mechanisms

	NS total	NI total	BG total	Rural	Urban	Recipients	Non-recipients	Total average
Option A: Supplementing monthly social payments								
Convenience	3.56	3.97	3.2	3.69	3.46	4.13	3.02	3.58
Effectiveness in improving family situation	3.9	3.78	3.4	3.72	3.67	4.61	2.77	3.69
Helping the poorest who need help most	4.59	2.97	3.74	3.84	3.69	4.29	3.25	3.77
Total average	4.02	3.57	3.45	3.75	3.61	4.34	3.01	3.68
Option B: One-off lump sum								
Convenience	3.47	2.9	2.85	2.88	3.27	2.32	3.83	3.07
Effectiveness in improving family situation	3.44	2.56	3.2	2.75	3.38	2.64	3.48	3.06
Helping the poorest who need help most	3.95	3.03	3.56	3.27	3.75	3.18	3.84	3.51
Total average	3.62	2.83	3.20	2.97	3.47	2.71	3.72	3.21
Option C: Energy efficiency subsidy								
Convenience	3.77	4.34	4.25	4.37	3.87	3.92	4.32	4.12
Effectiveness in improving family situation	3.62	4.24	4.03	4.11	3.81	3.87	4.05	3.96
Helping the poorest who need help most	4.37	3.77	4.14	4.05	4.12	4.14	4.03	4.08
Total average	3.92	4.12	4.14	4.18	3.93	3.98	4.13	4.05

Source: IPSOS (2011)

about that were supposed to deliver benefits for the poor, their perception of who actually received those benefits and their perceptions of the benefits and costs of these allowances. The findings varied considerably between the groups of poor who were beneficiaries of schemes and those who were not. The follow-on activity presented scenarios to the group, including a potential scenario under discussion within the government to ease hardship caused by rising energy tariffs by raising allowances under one of the social assistance programmes targeted towards the poor. Participants discussed and scored the options on three aspects of the proposal (convenience, effectiveness in improving the family situation and helping the poorest who need most help). Throughout the discussion, the facilitator prepared tables with the participants that summarised the scores, which permitted the tabulation and comparison of the perceptions of various groups. Notable is that poor recipients of the social assistance were in favour of the additional grant, but poor participants who were not recipients preferred to receive a subsidy to carry out energy efficiency improvements to their accommodation rather than support tied to transfer systems. This reflected their view that they would remain excluded from the social assistance schemes (Table 4.1).

The preparation of these tables and the possibility of comparing systematically the views of various groups present the research teams with helpful framing for their reports in a way that exercises based only around narrative would not. Much of the illuminating detail remains in the discussion transcripts and serves to explain, interpret and elaborate the tables.

Some Insights from the Findings of This Research

The studies have provided a considerable wealth of micro-detail on the experience and mechanics of social exclusion, especially in relation to different policy measures (social assistance of last resort, pensions, disability benefits) and to groups, such as the Roma, which are not always sufficiently covered or identifiable in existing household surveys. Looking across the studies and specific sectors and policies of interest, a number of themes seem to repeat, regardless of sector of enquiry. These relate in particular to the problems of access to specific programmes which are intended to reach the excluded, both because of errors in targeting and complex processes that fail to include some of the most excluded groups which they are meant to reach, and because of lack of information. To illustrate the importance of this research, and its potential to complement and strengthen other types of research, this section summarises briefly some of the main points that have arisen with respect to the existence of potentially exclusionary mechanism in relation to government programmes, particularly social assistance of last resort. It also compiles evidence on how those mechanisms might apply to one of the groups which appears to be extremely excluded in multiple dimensions, the Roma.

Shocks, Coping Among Poorer Households and Possible Exclusionary Mechanisms Linked to Social Assistance

Several of the studies discussed in this chapter examined differences in possible behavioural responses between households with access to formal social assistance of last resort and those without to analyse the possible impacts of different policy changes. This research has been structured around exercises that probe on household responses to various shocks, including those generated by the economic crisis, those arising from lumpy expenditures and those arising from a loss of real income (pension freeze). The relatively limited coverage of many of these programmes and particularly of social assistance of last resort (see also Chapter 13 of this book) allowed the comparison of focus group discussions of equally poor people, some benefiting from social assistance and some not.

Some common findings emerged throughout the various studies and provide useful examples of the insights that this type of analysis can contribute to the understanding of poverty and exclusion:

When discussing their coping strategies, respondents sometimes mentioned social assistance programmes, but often rather low down the list of responses. There were significant differences by programme though: in Serbia, in the middle of the economic crisis, participants were asked to describe the positive and negative changes over the last 12 months and how they coped with these changes. Two forms of formal assistance were mentioned—child allowance and agricultural pensions—but they were among the least frequently mentioned and scored low for efficiency in terms of helping them to overcome adversity. Two vulnerable groups, IDPs and Roma, put many other strategies ahead of seeking government assistance. Single mothers, however, were crucially dependent on child allowance in a period of unstable employment opportunities.

Coping mechanisms that might be interpreted as destructive, in the sense that they have the capacity to generate a second round of negative impacts, were very prevalent among respondents, whether they were enjoying some form of government assistance or not. Among these would be cutting food consumption, stopping medications, building up debts and engaging in nonlegal behaviours (e.g. theft of electricity or smuggling), all of which bear a strong resemblance to coping strategies deployed during the global economic crisis in much poorer countries (Heltberg, R et al. 2012). The prevalence of reducing consumption was particularly striking. Pensioners mentioned this as a way of coping with the coinciding shocks of frozen pensions, rising prices and rising medical bills. All vulnerable groups ranked this high as a coping strategy in response to the combined labour market and price shocks associated with the economic crisis. Both recipients and non-recipients of the material allowance mentioned that they reduced consumption of basic commodities (such as switching to inferior foods) as a response to rising electricity prices.

Local and official views often were in line with quantitative assessments of inadequate coverage of these programmes. For example, local officials working on the

Ndihma Ekonomike programme universally estimated that poverty rates were higher than coverage rates in the research communities.

Lack of information about sources of assistance for poor households prevents many vulnerable groups from claiming their entitlements in many situations. Applicants and recipients often receive scant and unsatisfactory information from the offices administering the benefits, and non-recipients cannot correctly define who is entitled to the different types of assistance.[1]

The operational rules of the programmes can often limit the role that social programmes can play in helping people cope with shocks. Applications require a full knowledge of the various steps, the right papers (having papers to start with, in fact) and facing the costs of providing the papers and visiting different offices.

There is a perception of randomness or unfairness in the system, compounded by the lack of transparency regarding eligibility criteria and calculations of benefits. Explanations regarding refusals are not always given, and grievance processes are not always efficient or trusted enough to use. The fact that many poor households are turned down for assistance while other households (judged by the non-recipients to be of similar levels of poverty) are considered eligible promotes distrust in the system. With some frequency, discussions about access to schemes turned to the value of connections, the possibility of bribes, the subjectivity of decision-making and, in some cases, interference by politicians.

Recipients found that the financial support offered by most schemes (including the Ndihma Ekonomike, disability payments in Albania, material allowance in Serbia, pensions in Serbia) was too small to live off or compared to economic shocks such as the loss of a job or the rise in cost of basic commodities. The erosion of the real value of the benefits overtime was an important aspect of this assessment. And for some particular programmes (such as energy benefits), many poor households who had not applied indicated they had not bothered to do so because the costs of application were too high relative to the rewards if they were successful.

Some perceived benefits of the programmes went beyond the transfer itself. For example, there was perceived value in being a known recipient in facilitating access to food on credit in local stores, since shop owners were more confident of eventual payment, although all but pensioners complained about delays and irregularities in payments. Some of this was countered by the loss of dignity associated with being dependent on welfare.[2]

The overall picture that emerges from these studies, therefore, is one where the role of these safety nets in helping poor households to handle shocks is relatively minor, at least in terms of poor people's own descriptions of the role it plays in the livelihoods.

[1] The research team visited ten offices administering Ndihma Ekonomike in Albania and found no publicly information about processes or costs of processing in any of the offices.

[2] In addition, some schemes gave access to supplementary benefits, such as energy subsidies and various one-off payments, but these were accessed sporadically, possibly because often they are financed by municipalities and therefore not available in all research sites.

Taken together these studies suggest that broader patterns of exclusion in Albania and Serbia may be reproduced to some extent in the patterns of access to social assistance (in the sense that processes of application and criteria for eligibility are, to a certain degree, exclusionary of particular vulnerable groups). This might not make a tremendous difference at a material level as the material value of social assistance of last resort had been so eroded over recent years that multiple additional strategies to cope with shocks were necessary for all poor people, both recipients and non-recipients. Yet these exclusionary elements of access to social assistance might, make more of a difference in driving certain groups in the future. For example, there are currently discussions of alleviating the impact of rising electricity prices by topping up existing social assistance schemes (e.g. Ruggeri Laderchi et al. 2012). These measures by making the benefits linked to social assistance more significant might increase take-up by eligible households, but—unsurprisingly—when this scenario for support was presented to poor households in Serbia, it was much more appealing to those who were successfully accessing social assistance already than to those who had tried to access support but had failed.

Possible Exclusionary Mechanisms Linked to Social Assistance and the Disadvantage of Being Roma

Most of the studies discussed in this chapter have included Roma groups in the sample, in part because information on Roma from quantitative surveys is scarce and in part because it was anticipated that Roma groups would experience particular impacts that might not be observed among other groups. In general, the studies found that Roma groups were worse off than other groups, suffered multiple deprivations and had limited access to protective mechanisms which were sometimes proposed as possible instruments to lessen the impact of reforms or other shocks. Respondents also mentioned discrimination in some instances.[3]

In most instances, the Roma communities included in the research were described as being poorer than others, including by the Roma themselves. In studies in Albania, Roma participants estimated that 90 % of their community might classify as poor, much higher estimates than the other communities included in the research. Research teams in Serbia described the Roma communities as being "*on the verge of existence*".

Information gathered on the impacts of the economic crisis in Serbia suggest that not only was their starting position more disadvantaged, but that they were also more vulnerable to economic shocks (particularly the contraction in availability of

[3] In Serbia, Roma groups described discrimination as "*always there"* and provided examples of how Roma children had been excluded from Christmas charity and faced insults at school (*"Our children should go to school. Children should eat regularly, get dressed, not to be any different from Serbian children, not to be called Gypsies or other insulting names. Our children should be together with all other children, and how can we provide it when we have no income". "Our children are insulted at school because they have nothing to wear and they have no textbooks".).*

Table 4.2 Changes in living conditions experienced in the last year, reported by Roma groups

Grades	Roma settlements, Belgrade, urban	Integrated Roma, rural, Jaša Tomić and Batočina	Cardboard settlement, urban, Kragujevac	Roma IDPs, integrated and collective centres, Bujanovac	Total
1—Much worse	2	22	8	16	48
2	13	2			15
3	1				1
4					
5—Much better					

Table 4.3 Changes in living conditions experienced in the last year, reported by single mothers

Grades	Belgrade Low class	Belgrade Middle class	Nis	Zrenjanin	Total
1	1				1
2	7			8	15
3		5	7		12
4		3			3
5			1		1

informal sector work and increases in prices of basic items). Participants in the research assigned scores to improvements or deteriorations in living conditions that they had experienced over the previous 12 months. Comparing the perceptions of Roma groups (Table 4.2) and another vulnerable group, single mothers (Table 4.3), the concentration of scores by Roma in the "much worse" category is quite striking. This was an important finding, since the expectation was that those on the margins of the organised, formal economy would not be among the worst hit.

Interactions with official systems and processes appeared to be more problematic for Roma groups than for other population groups. The lack of information about sources of assistance for poor households described above appeared to be a particularly pressing constraint for Roma, whether in respect to poverty-targeted social assistance, to energy subsidies or to disability allowances. So, for example, lack of information about energy subsidies associated with the *Ndihma Ekonomike* was not generally an important reason why many *Ndihma Ekonomike* recipients had not applied, but the research team found this was a particularly important reason why Roma respondents were not accessing benefits. Similarly, disabled Roma participants were far less aware of possible subsidies for prescription costs than were non-Roma recipients of disability allowances. In situations where some people are able to "work the system" better than others, Roma often seemed to be at the disadvantaged end of the spectrum.[4]

[4]In the words of one of the reports "while the substantial medical expenses for the treatment of some patients with chronic kidney failure in private hospitals are covered by the government (case in Rrashbull), other beneficiaries with the same condition have to 'settle' for the seemingly lower-quality treatment in public hospitals (case in the urban Roma community in Tirana)"

Problems with application procedures are more marked for Roma than for other groups. In addition to the length, multiple stages, costs of the application processes and the unhelpfulness of officials reported by other recipient of social assistance, Roma participants were particularly disadvantaged when it comes to the paperwork required in the processes. Where processes to claim entitlements are based on paperwork that Roma routinely do not have (those mentioned in various exercises included "personal documents", "unemployment documents", proof of tax payments and payment of electricity bills), then those processes will clearly exclude Roma people.

The lack of transparency on the functioning of many of these social assistance programmes leads to suspicions of discrimination. In some instances, Roma respondents reported to be almost self-excluding from sources of support in the belief that time and costs invested in application processes would be wasted because officials would discriminate against them. There were some differences of perspective on the existence of discrimination between officials and Roma participants. Problems attributed by some Roma respondents to discriminatory behaviours (e.g. lack of jobs provided through the National Employment Office, non-approvals of benefit payments) were attributed to other factors by officials (lack of skills undermining the suitability of Roma applicants for available jobs, lack of sufficient paperwork). In contrast, in Albania, Roma respondents reported receiving answers such as "you should find a job instead" when applying for Ndihma Ekonomike.

Conclusion

This chapter has sought to illustrate how qualitative research, and particularly structured focus group discussions, can play an important role in informing policy relevant analysis of poverty and inclusion. The discussion of both the methodological aspects of this research and of the findings related to exclusionary mechanisms embedded in the way social assistance programmes are run has been based on the experience of a number of studies that have been commissioned to assess the distributive impact of reforms or to inform large analytical studies. Beyond the specifics that have been presented, two key messages emerge from these findings.

- First the design of these types of activities, and the way respondents' answers are summarised and analysed, is key. It is easy to dismiss qualitative evidence as not sufficiently technical or rigorous if the studies have not been properly planned and designed to ensure that they capture appropriately the reality under consideration (in terms of sampling) and that results across research sites can be summarised and compared to tease out the specificities of the different situations.
- Second, the richness of this approach lies in the ability to delve into understanding dynamics and processes shaping people's choices and perceptions. For this work to be most useful, it is important that it is conducted based on a solid understanding of available evidence, particularly quantitative, so that the value added of its contribution can be maximised.

Appendix 1. Strategies for Coping with Economic Shocks

Coping strategy	Frequency (number of participants)	Efficiency (grades from 1 to 5)	Which groups use it?	Which groups cannot use it?
Consumption of groceries from own production	32	+++	All small rural households	
Day labour of all kinds (cutting bounds, collecting fruit, cutting cabbage, picking corn, etc.)	32	+++	All small rural households	
Rather female day jobs: cleaning houses, bringing and packing wood, ironing	15	+++	Female	Male
Rather male day jobs: working on a building site, cutting and chopping wood, slaughtering cattle, loading manure, digging, mowing, hay stacking, collecting wood from creeks, etc.	15	+++	Male	Female
Sale of agricultural products and animals (eggs, milk, cheese, pigs, lambs, brandy, apples, corn, wheat, potatoes)	20	+++		Households without machinery and animals
Change of production area (one female respondent started growing flowers)	1	++		Households without monetary means
Picking sloe berries, cornel berries and dog-rose berries in the woods	1	+++		
Extra care for animals and resale on the market	1	++		
Borrowing from neighbours, relatives	25	+++		
Buying “on tick” in shops	5	++		
Financial support and children’s allowance	2	+	Poor families with children	Without owned land
Prolonging payment or not paying bills for public utilities	12	+		
Reduction of consumption	25	++		
Agricultural pension	6	+		

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Chapter 5
Updating Poverty Maps Between Censuses: A Case Study of Albania

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Introduction

There is increasing interest among researchers and policy makers in obtaining credible "poverty maps"—estimates of poverty at the smallest possible disaggregated geographic level of a country. Currently, this information is not easy to obtain because detailed household surveys that would cover every subregion (or small area) of a country would be too costly and therefore never done, and most censuses which overcome the problem of coverage do not contain income information. However, a recent approach that has received considerable attention proposed a way to construct microlevel estimates of poverty and inequality. The small area estimation (SAE) technique developed by Elbers et al. (2003) exploits the availability of income data from typical household surveys such as a Living Standard Measurement Survey (LSMS) and universal coverage from the census. In a recent paper, Tarozzi and Deaton (2009) provide a simpler version of the SAE methodology but argue that the usefulness of their estimator and indeed that of the SAE to provide credible estimates of poverty at a small area rest on strong area homogeneity and conditional independence assumptions. They conclude that in general differ-

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ences in the returns to local labor, rental, and asset markets will lead to violations of these assumptions and therefore imprecise estimates of poverty for small areas.

But even in contexts where these assumptions are not violated (as in Elbers et al. 2008) and precise estimates can be obtained additional difficulties arise when updating poverty maps over time. The limited availability of census and household surveys collected at the same time limits the number of poverty maps that can readily be constructed: while censuses are typically implemented every decade, primarily due to the high cost of a population-wide survey, household sample surveys can be much more frequent, say, for instance, every year in Brazil and every 3 years in Albania. It is thus very difficult to update the poverty map constructed with matching census and household survey during the inter-census years. But finding ways to construct poverty maps between census years is of high interest to policy makers and international donors who want to understand time evolution of spatial poverty, investigate the correlation of poverty dynamics and other variables in time, or want to monitor country development strategies.

To our knowledge, only two methodologies have been proposed to update poverty maps. The first methodology has been proposed by Emwanu et al. (2006) combining a new survey, as part of a panel, with old census to update the poverty map in Uganda. The 1992 Uganda Household Integrated Survey (UHIS) and 1999 Uganda National Household Survey (UNHS) have 1,263 common households for which consumption information is available for both years. The authors combined 1999 UNHS data with the 1992 census (matching on the 1992 household characteristics) and used a reweighting scheme to obtain a poverty map for 1999. But panels are very rare, especially in developing countries, so an alternative proposal is to match the new household survey with an old census on only time-invariant covariates. This is the method followed by Lanjouw et al. (2011) and Van der Weide (2008) to update poverty maps for Vietnam and Indonesia and the Philippines, respectively. Even aside from the difficulties of finding panels or truly time-invariant characteristics, the challenges of the above-mentioned methodologies are not small: consumption and other variables must be comparable over time, migration must be well accounted for, and redistricting[1] can happen more often than not.

The contribution of this chapter relies on an alternative methodology, also based on a reweighting scheme. Specifically, our method, which is motivated by Lemieux (2002), constructs a counterfactual consumption distribution for the old household surveys in our case the Albania LSMS 2002, using the information contained in two later intercensal survey, Albania LSMS 2005 and 2008. The method projects what the consumption distribution for the 2002 LSMS (which was conducted about the time the census was done) would look like if the parameters (the coefficients of a consumption model) and distribution of the characteristics of the sample, and therefore population, were as reported in the 2005 and 2008 surveys. The derived counterfactual distributions together with the census are then used to obtain two updated poverty maps of the country for 2005 and 2008, respectively. As a

[1] Geographic subregions that are subdivided, merged, disappear, or are being created.

comparison and robustness check, we also present results for 2005 from the method proposed by Lanjouw et al. (2011), which uses time-invariant characteristics from the new survey matched to the census to derive welfare estimates.[2]

The results obtained for the Albania poverty estimates with our method are quite encouraging as they offer useful insights into poverty dynamics at a small geographic unit level. We find that poverty estimates aggregated from the municipality level match very closely the "true" estimates obtained at strata, urban/rural and national levels using survey data. Furthermore, even in strata where substantial poverty reduction has taken place, the method captures substantial local heterogeneity. In addition, when few time-invariant variables are common to the census and household survey data, we find that our proposed method performs better than using time-invariant characteristics in three crucial areas. First, its coverage probabilities—the 95% confidence band—are superior to the method utilizing only time-invariant variables. Second, while estimates of poverty from our proposed method, and those using only time-invariant variables are similar, our method's estimates are closer to the true estimates more often. Finally, we find that the explanatory power of our proposed method, as measured by the R^2, is often two to three times higher than the method using only time-invariant characteristics for all first-stage consumption and error models.

The rest of this chapter is organized as follows. In the first section we present the SAE methodology and present a discussion of the two alternative methods we use to update the poverty map in Albania. The following section provides a short description of the data used. We then describe the estimation strategy and in the following section present the results. The last two sections discuss the shortcomings of the method and conclude, respectively.

Methodology

The SAE or Poverty-Mapping Technique

The poverty-mapping methodology proposed by Elbers et al. (2003) typically involves a household survey and a population census as data sources. Let W be a welfare indicator (such as headcount poverty or inequality) based on the distribution of a household-level variable of interest, y, such as consumption or income. The consumption or income of a household, h, in cluster c, is modeled as

$$\ln(y_{ch}) = \beta' X_{ch} + v_{ch} = \beta' X_{ch} + \mu_c + \varepsilon_{ch} \tag{5.1}$$

where X_{ch} is observable covariates and the composite error term v_{ch} consists of two parts—a cluster fixed effects μ_c and an idiosyncratic (or household-specific) error

[2] Due to the limitation of the time-invariant characteristics common to both census and LSMS data, we did not reproduce the exercise with the 2008 LSMS.

term ε_{ch}. The Elbers, Lanjouw, and Lanjouw estimator (henceforth ELL) treats the idiosyncratic error term as heteroskedastic and the cluster fixed effects as i.i.d and homoskedastic.

The ELL estimator consists of several stages. First, survey data[3] is used to obtain an estimate of the parameter β in Equation (5.1) by restricting the explanatory variables to those that also occur at the household level in the population census (or some other large dataset) or in a tertiary dataset that can be linked to both the census and survey. A consistent estimation of the parameters in Equation (5.1) is not enough to estimate the statistics of interest (poverty headcount or inequality), because these outcomes are usually functions of y, not of its conditional distribution. Therefore, the ELL adds an error term to the conditional distribution. In particular, the estimator allows for an intra-cluster correlation in the disturbances. It accomplishes this by assigning to each household in a cluster, the mean value of the resulting residuals $\hat{v}_{ch}$ over all observations from the same cluster. Failing to take into account spatial correlation in the disturbances would result in underestimating standard errors in the final poverty estimates. Typically, different models are estimated for each region and the specifications include census mean variables and other aggregate-level variables in order to capture latent cluster-level effects as well. An estimate of the fixed component of the error term would lead to the estimate of the household-specific error terms, $\varepsilon_{ch} = \hat{v}_{ch} - \hat{\mu}_c$. Since the idiosyncratic error terms are assumed heteroskedastic, ELL proposes to normalize them. To do so, ELL fits a parametric heteroskedasticity model to the variance of the idiosyncratic error terms:

$$\sigma^2(X) = \frac{A\mathrm{e}^{z'_{ch}\gamma} + B}{1 + \mathrm{e}^{z'_{ch}\gamma}}, \tag{5.2}$$

where A and B are parameters to be estimated and z_{ch} is a subset of the covariates that influence the heteroskedasticity of the idiosyncratic error. Once the parameters in Equation (5.2) are obtained, household-specific error terms are computed as

$$\hat{\varepsilon}_{ch} = \frac{\varepsilon_{ch}}{\hat{\sigma}_{\varepsilon,ch}} - \frac{1}{N_h}\sum \frac{\varepsilon_{ij}}{\hat{\sigma}_{\varepsilon,ij}}. \tag{5.3}$$

All regressions in this "first stage" are estimated with household weights and with parsimonious specifications in order to avoid overfitting. To obtain the welfare statistics of interest, ELL carries the parameter estimates in Equations (5.1) and (5.2) and the empirical distribution of the fixed and idiosyncratic error terms as inputs into the second stage. The simulated (or "constructed") consumption data is arrived at in the following steps (see Elbers et al. 2003 and Tarozzi and Deaton 2009). First, a set of parameters from the consumption and idiosyncratic error models are drawn [see Eqs. (5.1) and (5.2)]. Second, an estimated value of the cluster fixed effect, $\hat{\mu}$, drawn from the empirical distribution of errors in Equation (5.1)

[3] These surveys are stratified at the region or state level, as well as for rural and urban areas. Within each region there are further levels of stratification, and also clustering. At the final level, a small number of households (a cluster) are randomly selected from a census enumeration area.

is assigned to each cluster in the census. Third, each observation in the census is assigned a normalized idiosyncratic error term, possibly from the empirical distribution of the residuals. Fourth, household-specific error terms are estimated using a heteroskedastic model [Equation (5.3)]. Finally, the simulated values of consumption are obtained as

$$\ln(y^r) = X'\hat{\beta}^r + \hat{\mu}_c^r + \hat{\varepsilon}_{ch}^r. \tag{5.4}$$

The predicted household level per capita consumption in the census is a function not only of the parameter estimates from the first-stage consumption models estimated in the survey but also of the precision of these estimates and of those parameters describing the error models. Therefore, instead of producing just one predicted consumption level per household in the census, the method simulates *r*-predicted expenditures for each household (typically around 100 simulations).

The full set of simulated household level per capita consumption in the census is then used to obtain welfare estimates, *W*, of each target population. Demombynes et al. (2007) describe a variety of simulation approaches that are available and note that all yield closely similar welfare estimates. Elbers et al. (2003) also study the precision of the resulting estimates of *W* and demonstrate that prediction errors will fall (or at least not rise) with the number of households in the target population and will also be affected by the properties of the first-stage models, in particular the precision of parameter estimates. A general rule of thumb is that welfare estimates obtained on this basis will be estimated fairly precisely as long as the target population comprises at least 1,000–5,000 households.

Updating Poverty Maps with Counterfactual Population Distributions (CM)

Suppose that there is only one census and two household surveys, a *new* and an *old* household survey. When the old household survey is conducted about the same time as the census, the SAE method described above can be applied and welfare estimates obtained for that year. The problem is how to update the poverty estimates for small areas when there is a new survey, but no new census, especially when the new survey may contain either very few observations or none at all in most of the small areas. In this case, we propose to construct a counterfactual consumption distribution of the old household survey, using information from both the old and new household survey following the methodology proposed by Lemieux (2002), and match the resulting counterfactual distribution with the old census data.

To construct the counterfactual wealth distribution, consider a consumption model using the *new* survey (for instance, the 2005 survey):

$$\ln(y_{05,i}) = \beta'_{05} X_{05,i} + \varepsilon_{05,i}, \tag{5.5}$$

where y_{05} denotes consumption in year 2005, i indexes the household, β_{05} is a parameter (that captures the "returns" to or "price" of covariates in 2005), X_{05} is a vector of covariates, and ε_{05} is unobserved component of consumption.

Note that using this *new* survey, without additional adjustments, and applying the ELL estimator, would be problematic because the returns to covariates and the parameter β may have changed between 2002 and 2005. In addition, the profile of the population—that is, covariates such as education levels, age composition, and so on—may also have changed. Finally, the returns to unobserved covariates may also have changed. To recreate a consumption distribution that resembles consumption in 2002, we would have to account for these changes. Therefore, our counterfactual consumption distribution has three steps.

The first step is to create the consumption distribution which would have prevailed in 2002 if the parameters were as in 2005. That is,

$$\ln(y^{p}_{02,i}) = \hat{\beta}_{05,i} X_{02,i}. \tag{5.6}$$

Equation (5.6) accounts for changes in the parameters of covariates, by using the estimated parameters from the *new* survey to estimate consumption distribution in the *old* survey. However, in addition to these parameters, the levels of covariates may have changed because perhaps the population is now more educated. When the covariates of interest are few, say only the education variable that takes only two values—primary and higher education—then a simple reweighting of each cell would be sufficient. But when changes in multiple covariates are of interest, as they are in our case, it is not feasible to do a cell-by-cell reweighting. Instead, we have to create a score that reduces the dimension of the data, by stacking the *new* and *old* surveys and then running a probit model

$$P_{it} = \Pr ob(survey = 2005 \mid Z_{it}, M_{it}) = \alpha'_{z} Z_{it} + \alpha'_{m} M_{it}. \tag{5.7}$$

In principle, we can include a large set of observable household-level characteristics, Z_{it}, and also the migration status of the household, M_{it}, or any suitable variables that capture the scale of migration, which is of crucial concern when trying to update poverty maps. Equation (5.7) allows us to obtain a propensity score—the predicted probability of being in period $t = \{2002, 2005\}$—conditional on the observable characteristics:

$$\psi_{it} = \frac{1 - P_{it}}{P_{it}} / \frac{P_{t}}{1 - P_{t}}, \tag{5.8}$$

where P_t is the unconditional probability that an observation belongs to period t or the share of year 2005 observations in total observations (i.e., both years). In this framework, accounting for changes in the distribution of observable characteristics is equivalent to reweighting the consumption distribution estimated in Equation (5.6) so that we have

$$\ln(y^{r}_{02,i}) = \ln(y^{p}_{02,i}) \times \psi_{02,i}. \tag{5.9}$$

The only step remaining is to add a measure of the unobserved component of consumption. If the dispersion in unobserved consumption is due to random events that are unrelated to systematic differences across households, then there would be nothing more to say about the error term. However, one reason to add a measure of the unobserved consumption is that the residual is unlikely to be just a random component of consumption. Instead, it may reflect systematic, albeit unexplained, differences between households. As an example, note that if income were determined only by human capital endowments (e.g., education), then the residual would capture the unmeasured component of human capital so that an increase in the returns to education would lead to an increase in the dispersion of the residual (the unmeasured component of income). Moreover, using the consumption in Equation (5.9) would be equivalent to using only an imputed and reweighed conditional mean consumption, which would have much smaller standard errors and less variability. Therefore, for these two reasons, we adjust the consumption in Equation (5.9) with counterfactual residuals.

We first estimate a consumption model for the 2002 data and rank all the households on the basis of the residual distribution for that year. Then we assign to each household in the year 2002 survey the value of the ranked residual from the empirical distribution of residuals in the year 2005 survey [Equation (5.5)] which corresponds to the year 2002 rank. We now have the counterfactual consumption, the consumption that would have been observed in 2002, if the parameters, the distribution of covariates, and the unmeasured determinants of consumption are as in 2005. From Equations (5.5) and (5.9), we can rewrite this counterfactual distribution as

$$\ln(y^{c}_{02,i}) = \psi_{02,i}(\ln(y^{p}_{02,i} + \varepsilon^{r}_{05,i}) = \psi_{02,i}(\hat{\beta}_{05}X_{02,i} + \varepsilon^{r}_{05}), \tag{5.10}$$

where $\varepsilon^{r}_{05,i}$ denote the value of the ranked residual in 2005 assigned to a household with the same residual rank in year 2002. Note that in practice, in addition to the reweighting factor, sampling weights, ω_{it}, can be easily introduced so that we end up with a modified weighting factor: $\psi_{02,i} \times \omega_{02,i}$.

To summarize, our proposal to update poverty maps during intercensal years with a new household survey is to (a) create the counterfactual consumption distribution—the distribution that would have prevailed in 2002 if the parameters of consumption and the distribution of observable and unobserved covariates were as they were in 2005—as in Equation (5.10), then (b) implementing the SAE methodology described in Equations (5.1) through (5.4), by setting $y_{ch} = y^{c}_{02,i}$ and $X_{ch} = X_{02,i}$.

Updating Poverty Maps with Time-Invariant Variables (TIM)

To compare the estimates using the CM methodology, we also construct a poverty map for 2005, using time-invariant characteristics. To obtain welfare estimates, this method matches the survey and census on the time-invariant characteristics of the population. That is, the consumption model in Equation (5.1) is estimated by using

only time-invariant characteristics, X_{ch}, that can be identified in the *new* household survey and the census in the first stage. Subsequently, the parameters from the estimates in the first stage are applied to the census data to obtain the welfare estimates. The main disadvantage of this method is that there are very few covariates that are time invariant, and so welfare outcomes become estimated on a very small selection of variables. Therefore, a major concern with this method is the likelihood that omitted variables will introduce substantial biases in estimation.

Data

The Republic of Albania is administratively divided into 12 prefectures, which are further organized into 36 districts, and each district may contain several communes and municipalities. Municipalities and communes are important in the decentralized governance structure because, in addition to receiving block grants from the central government, they raise their own revenues, have representative government, and elected mayors (in the case of municipalities). Since early 1990s, there have been 374 communes and municipalities. Therefore, for development purposes, this will be the most relevant lowest level of disaggregation to obtain poverty maps. For constructing an updated poverty map, we use four datasets: the Population and Housing Census of 2001 (PHC) and the Living Standard Measurement Study (LSMS) in 2002, 2005, and 2008 (henceforth LSMS02, LSMS05, and LSMS08, respectively).

Census: The census was conducted in April 2001 but used the 31 March 2001 as reference. The 2001 census also introduced the concept of an open population in order to assess the consequences of emigration and internal migration. For the purposes of the PHC, the cities and the villages were divided into 9,834 enumeration areas (EAs) throughout the country, consisting of about 80–120 dwellings. The fieldwork for the census was based on a four-part questionnaire with questions at four different levels: building questionnaire, to be completed only for the first or only dwelling in the building; dwelling questionnaire, to be completed for all the inhabited dwellings in the building; household questionnaire, to be completed for all the households (if more than one) in the dwelling; and individual questionnaire, to be completed for all the members of the household who were present or absent for less than 1 year (to be defined in the roster). At the end of March 2001, there were 726,895 households in Albania with 3,069,275 persons (1,347,281 in the labor force) living in 512,387 buildings.

The LSMS: The LSMS02 was carried out between April and June of 2002, with some field activities extending into August and September. The survey work was undertaken by the Living Standards unit of INSTAT (Albanian National Statistics Office), with the technical assistance of the World Bank. The PHC provided an updated sampling frame which of 9,834 enumeration areas. The final sample design for the LSMS02 included 450 primary sampling units (PSUs) and 8 households in

each PSU, for a total of 3,600 households. Four reserve units were selected in each sample PSU to act as replacement unit in nonresponse cases. In a few cases in which the rate of migration was particularly high and more than four of the originally selected households could not be found for the interview, additional households from the same PSU were randomly selected. The sampling frame was divided into four regions (strata): coastal area, central area, mountain area, and Tirana. These four strata represent the domains of estimation. They were further divided into major cities, other urban, and other rural. The EAs were allocated proportionately to the number of housing units in these areas.

Four survey instruments were used to collect information for the 2002 Albania LSMS: a household questionnaire with rich household level and individual information on 15 topics covering demographics, education, health, labor markets, migration, and so on; a diary for recording household food consumption; a community questionnaire; and a price questionnaire. The LSMS05 and LSMS08 are repeated cross sections of 3,840 and 3,600 households, respectively, patterned exactly after the LSMS02 in sampling, data collection, and core topics covered.

Estimation Strategy

A major concern with simulating welfare measures for small census areas is the possibility that spatial homogeneity—the idea that some aspects of the conditional distribution of income or consumption should be the same between the small areas and the larger survey area which provides the data for undertaking the imputation—is violated. This is in part because the local labor and land markets and other environmental factors will likely differ across local areas (Tarozzi and Deaton 2009). As a partial remedy, we estimate six separate models to construct the poverty estimates. We estimate a model for rural and urban areas separately for two levels of stratification: central and coastal areas. Tirana has no rural areas, and mountain urban samples are too small, so in all we estimate models for mountain areas, central urban, central rural, coastal urban, coastal rural, and Tirana. Although Albania's regional markets have become fairly well integrated since the 1990s, INSTAT stratified its LSMS on these four areas because they are widely accepted to belong to reasonably distinct agroecological and economic areas. In addition, estimating these six models allows us to stay with the precedent established for constructing the 2001 poverty map (Betti et al. 2003) and to compare our results to these early results.

Variable selection: To obtain the counterfactual consumption which we use as an input for the simulation in CM, we used a large set of variables exactly defined in LSMS02, LSMS05, and LSMS08 that can reasonably be considered to influence consumption. But once the counterfactual is created, we have to find variables that are common to LSMS and the PHC. The list for TIM—the time-invariant variables—is much harder to find, but we were able to identify 18 variables that meet the definition (surprisingly a much larger set than would normally be possible).

Results

First, we find that the proposed CM method predicts poverty rates with a good deal of accuracy.[4] Recall that the household surveys allowed one to be able to estimate poverty at stratum level and in each stratum, separately for rural and urban areas. Table 5.1 compares the "actual" poverty rates—taking the survey-based poverty rates as the true poverty rates—and the predicted poverty rates using the CM method and aggregated from the estimates at the commune level. The predicted poverty rates and the change in poverty from 2002 are strikingly similar for both methods and are very close to the actual rates. For instance, the estimated rural and urban rates in each stratum fall within the 95 confidence interval of the actual for 2005. The census-based predictions are quite consistent with those from 2008, with the only exception of the poverty rates for the central areas (Fig. 5.1).

Table 5.1 Results at the stratum level using CM method

Stratum	2002 (BETTI)	2005 (LSMS)	2008 (LSMS)	2005 (CM)	2008 (CM)
Coast rural	0.29	0.20	0.15	0.23 (0.01)	0.12 (0.01)
Coast urban		0.12	0.11	0.16 (0.01)	0.13 (0.01)
Central rural	0.28	0.26	0.11	0.24 (0.01)	0.17 (0.02)
Central urban		0.13	0.10	0.12 (0.02)	0.16 (0.02)
Mountains	0.41	0.26	0.27	0.30 (0.01)	0.36 (0.03)
Tirana	0.23	0.08	0.09	0.06 (0.01)	0.08 (0.05)
Albania	0.25	0.18	0.12	0.19	0.17 (0.10)

Note: Standard errors in parenthesis

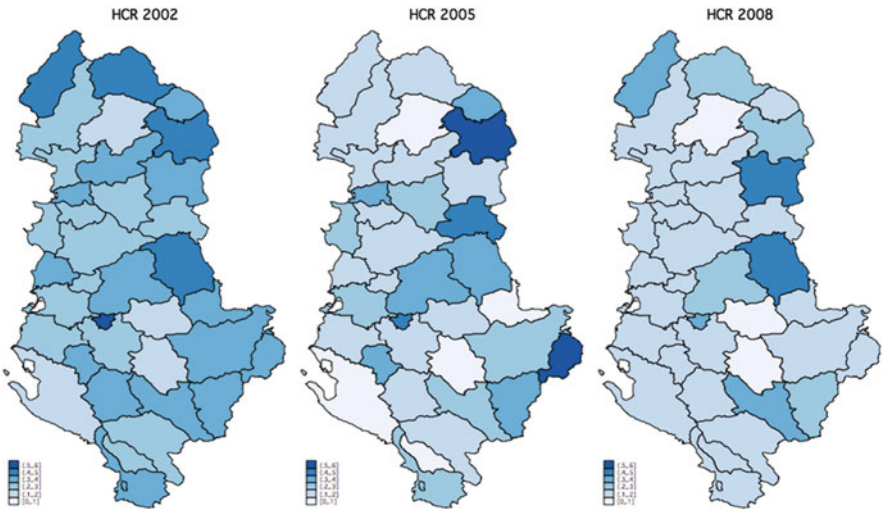

Fig. 5.1 Poverty rate estimates for 2002–2005–2008 at the district level

[4] All the separate strata level regression models and the poverty and inequality estimates at commune level are available from the authors upon request.

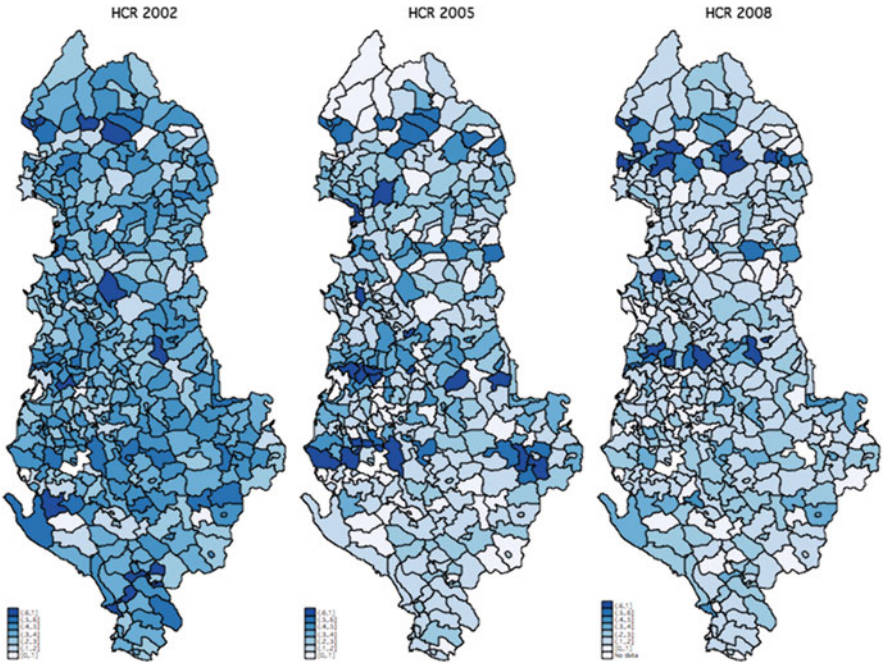

Fig. 5.2 Poverty rate estimates for 2002–2005–2008 at the commune level

Second, although the predicted poverty rates at the stratum, and also rural and urban areas, match the actual very well, there is still substantial heterogeneity at the commune levels, which is evident from Fig. 5.2. For instance, even in the mountain areas (mostly the northern part of the country), where the fastest declines in poverty are recorded, there are still very poor communes. Similarly, in parts of the country where poverty rates did not decrease more dramatically (such as the central areas), we find communes which witnessed sharp declines in poverty.

Third, we find that the differences in predicted poverty between the CM and TIM methods emerge more strongly as the prediction moves to the commune level (Tables 5.4 and 5.5). We note that our proposed method, CM, does much better at explaining poverty outcomes at the commune level. One reason for this claim is that the CM method does better at explaining variation in consumption and the residuals. Table 5.2 presents the size of variation explained by CM and TIM in each stage of the estimation. The R^2 for the β-model is the level of variation explained when we implement Equation (5.1), while the R^2 for the α-model is the level of variation explained in the residual model—the model to explain the household-level heteroskedastic error term. The R^2 for the β-model are very high, almost 60% and almost twice as high as what TIM explains. The R^2 for the α-model are generally lower for both TIM and CM, but the latter's are almost three times as high as the former. The observed low R^2 for the TIM models should not be surprising, as it may reflect in part the small number of covariates that can

Table 5.2 Poverty mapping intermediate results for 2005

Stratum	Methodology	R^2 β-model	Var(η)/MSE	R^2 α-model	HCR estimated
Coast rural	TIM	0.35	0.06	0.09	0.29
	CM	0.62	None	0.20	0.25
Coast urban	TIM	0.30	0.06	0.04	0.13
(w/o Tirana)	CM	0.60	None	0.18	0.12
Central rural	TIM	0.40	0.02	0.08	0.22
	CM	0.62	None	0.40	0.25
Central urban	TIM	0.35	None	0.07	0.05
	CM	0.39	None	0.34	0.15
Mountains	TIM	0.47	0.04	0.07	0.26
	CM	0.37	0.01	0.13	0.30
Tirana	TIM	0.38	0.03	0.05	0.07
	CM	0.62	0.01	0.15	0.06

meet the time-invariant test. However, the concern with this inability to explain significant variation in consumption is that the TIM method fails to account for substantial heterogeneity at the commune level. In fact, if we make the reasonable assumption that the commune-level trends in poverty rates should mimic the corresponding stratum-level poverty trends, we find that the TIM method substantially underperforms the CM model.

Discussion on Validity

As discussed above, one concern with the validity of small area estimates is heterogeneity—that is, local areas will be economically connected such that the conditions for estimating accurately the parameters do not exist (Tarozzi and Deaton 2009). As few censuses collect consumption and income data, it is very difficult to evaluate this requirement. However, two recent attempts come to different conclusion. Tarozzi and Deaton (2009) use Mexican census data and find that heterogeneity is a serious problem, although they also find that in many instances, the poverty maps contained useful information. By contrast, Elbers et al. (2008) use Brazilian census data and find that even with heterogeneity, the SAE estimates remain valid.

The local heterogeneity problems will be compounded if there is substantial migration, an issue that is of greatest concern when new surveys on one hand and old surveys and census on the other are separated by several years in time. Clearly with large migration, the population in the small area could be very different from the population at the time of the census so that at the very least, it is prudent to check the extent of migration. Therefore, we explicitly control for migration status of households between 2002, 2005, and 2008 in Equation (5.4) and find that the parameter is not statistically significant. Albania has had massive internal and international migration for most of 1990s and into the 2000s decade. Migration peaked in 1998, a year after a pyramid scheme led to many households' savings being wiped out. However, after years of rising, international migration started turning into a trickle by 2002, while internal migration had basically been exhausted long before.

Tarozzi and Deaton argue that if heterogeneity does not hold, poverty maps can be obtained by a simple two-stage process. In the first stage, a logit model of correlates of poverty is estimated. In the second stage, the parameters in the first stage are used to predict poverty and inequality for the populations in small areas in the census. But when we are updating poverty maps, there are two things to worry about; first, the characteristics of the population would have changed, again because perhaps they accumulate some determinants of income or consumption. But even if this were not true, the number of residents in each area may have changed, and both problems are exacerbated by massive migration.

Conclusion

In this chapter, we have estimated various measures of welfare for small administrative units in Albania, combining the 2001 Population and Housing Census with the 2002, 2005, and 2008 Living Standards Measurement Study survey data, in order to get updated poverty measures at a small geographic level. Tables 5.3, 5.4 and 5.5 present the findings. Our proposed estimation strategy produces precise poverty rates at the stratum, prefecture, and district levels. The precision of these estimates should be valuable to researchers and policy makers even at the commune level. Throughout the years, Albania's development outcomes have shown high spatial heterogeneity among prefectures and municipalities within districts to which they belong. This suggests that there is scope for policy in Albania to consider geographic targeting of some of the development programs, as explored for example in Chapter 16.

Table 5.3 Poverty estimates at the prefecture level (CM)

	2005			2008		
Prefecture	FGT[a] (0)	FGT (1)	FGT (2)	FGT (0)	FGT (1)	FGT (2)
Berat	0.10	0.04	0.02	0.16	0.03	0.01
Dibër	0.36	0.15	0.09	0.37	0.07	0.02
Durrës	0.26	0.09	0.05	0.15	0.03	0.0
Elbasan	0.31	0.09	0.04	0.19	0.03	0.01
Fier	0.17	0.05	0.02	0.12	0.02	0.01
Gjirokastër	0.13	0.05	0.03	0.11	0.02	0.01
Korçë	0.24	0.07	0.03	0.14	0.02	0.01
Kukës	0.29	0.09	0.04	0.33	0.05	0.01
Lezhë	0.33	0.15	0.09	0.17	0.03	0.01
Shkodër	0.10	0.03	0.01	0.19	0.04	0.01
Tiranë	0.11	0.03	0.01	0.12	0.02	0.00
Vlorë	0.09	0.03	0.01	0.11	0.02	0.01

[a]The Foster–Greer–Thorbecke (sometimes referred to as FGT) metric is a generalized measure of poverty within an economy. It combines information on the extent of poverty (as measured by the headcount ratio), the intensity of poverty (as measured by the total poverty gap), and the inequality among the poor (as measured by the Gini and the coefficient of variation for the poor)

Table 5.4 Poverty estimates at the prefecture level for 2005 (TIM)

	TIM		
Prefecture	FGT (0)	FGT (1)	FGT (2)
Berat	0.28	0.07	0.03
Dibër	0.32	0.08	0.03
Durrës	0.20	0.05	0.02
Elbasan	0.27	0.06	0.02
Fier	0.14	0.03	0.01
Gjirokastër	0.13	0.03	0.01
Korçë	0.27	0.07	0.03
Kukës	0.15	0.03	0.01
Lezhë	0.26	0.06	0.02
Shkodër	0.16	0.03	0.01
Tiranë	0.11	0.02	0.01
Vlorë	0.07	0.02	0.01

Table 5.5 Poverty estimates at the district level for 2005 (CM and TIM)

	FGT (0)		FGT (1)		FGT (2)	
District	CM	TIM	CM	TIM	CM	TIM
1. Berat	0.10	0.29	0.03	0.08	0.01	0.03
2. Bulcuizë	0.49	0.60	0.15	0.17	0.07	0.07
3. Delvinë	0.06	0.15	0.01	0.05	0.00	0.02
4. Devoll	0.45	0.16	0.12	0.03	0.05	0.01
5. Dibër	0.16	0.13	0.04	0.02	0.01	0.01
6. Durrës	0.21	0.19	0.05	0.05	0.02	0.02
7. Elbasan	0.29	0.27	0.06	0.06	0.02	0.02
8. Fier	0.12	0.12	0.03	0.03	0.01	0.01
9. Gramsh	0.35	0.32	0.10	0.08	0.04	0.03
10. Gjirokastër	0.13	0.04	0.05	0.01	0.02	0.00
11. Has	0.35	0.23	0.11	0.05	0.05	0.02
12. Kavajë	0.19	0.12	0.05	0.03	0.02	0.01
13. Kolonjë	0.11	0.08	0.03	0.01	0.02	0.00
14. Korçë	0.24	0.19	0.05	0.04	0.02	0.01
15. Krujë	0.39	0.22	0.14	0.05	0.08	0.01
16. Kuçovë	0.12	0.18	0.03	0.05	0.02	0.03
17. Kukës	0.27	0.14	0.08	0.03	0.03	0.01
18. Kurbin	0.19	0.22	0.05	0.05	0.02	0.02
19. Lezhë	0.54	0.23	0.27	0.06	0.18	0.02
20. Librazhd	0.34	0.35	0.10	0.08	0.05	0.03
21. Lushnjë	0.20	0.20	0.05	0.05	0.02	0.02
22. Malësi e Madhe	0.09	0.09	0.03	0.01	0.02	0.00
23. Mallkastër	0.30	0.05	0.08	0.01	0.03	0.00
24. Mat	0.54	0.40	0.29	0.10	0.17	0.04
25. Mirditë	0.14	0.35	0.05	0.09	0.03	0.03
26. Peqin	0.32	0.10	0.11	0.02	0.05	0.01

(continued)

Table 5.5 (continued)

	FGT (0)		FGT (1)		FGT (2)	
District	CM	TIM	CM	TIM	CM	TIM
27. Përmet	0.11	0.20	0.02	0.04	0.01	0.01
28. Pogradec	0.19	0.54	0.04	0.17	0.01	0.07
29. Pukë	0.12	0.20	0.03	0.04	0.01	0.01
30. Sarandë	0.09	0.13	0.03	0.03	0.01	0.01
31. Skrapar	0.12	0.33	0.07	0.07	0.06	0.02
32. Shkodër	0.10	0.16	0.02	0.04	0.01	0.01
33. Tepelenë	0.13	0.21	0.06	0.05	0.04	0.02
34. Tiranë	0.09	0.11	0.02	0.02	0.01	0.01
35. Tropojë	0.27	0.13	0.08	0.02	0.04	0.01
36. Vlorë	0.09	0.05	0.02	0.01	0.00	0.00

Table 5.6 Poverty estimates at the district level (CM)

	2005			2008		
District	FGT (0)	FGT (1)	FGT (2)	FGT (0)	FGT (1)	FGT (2)
1. Berat	0.10	0.03	0.01	0.16	0.03	0.01
2. Bulcuizë	0.49	0.15	0.07	0.34	0.05	0.01
3. Delvinë	0.06	0.01	0.00	0.07	0.01	0.00
4. Devoll	0.45	0.12	0.05	0.12	0.02	0.00
5. Dibër	0.16	0.04	0.01	0.50	0.10	0.03
6. Durrës	0.21	0.05	0.02	0.15	0.04	0.01
7. Elbasan	0.29	0.06	0.02	0.16	0.03	0.01
8. Fier	0.12	0.03	0.01	0.11	0.02	0.01
9. Gramsh	0.35	0.10	0.04	0.28	0.04	0.01
10. Gjirokastër	0.13	0.05	0.02	0.09	0.02	0.00
11. Has	0.35	0.11	0.05	0.45	0.08	0.02
12. Kavajë	0.19	0.05	0.02	0.13	0.03	0.01
13. Kolonjë	0.11	0.03	0.02	0.15	0.03	0.01
14. Korçë	0.24	0.05	0.02	0.13	0.02	0.01
15. Krujë	0.39	0.14	0.08	0.16	0.03	0.01
16. Kuçovë	0.12	0.03	0.02	0.11	0.02	0.01
17. Kukës	0.27	0.08	0.03	0.37	0.06	0.01
18. Kurbin	0.19	0.05	0.02	0.15	0.03	0.01
19. Lezhë	0.54	0.27	0.18	0.15	0.03	0.01
20. Librazhd	0.34	0.10	0.05	0.27	0.04	0.01
21. Lushnjë	0.20	0.05	0.02	0.12	0.02	0.01
22. Malësi e Madhe	0.09	0.03	0.02	0.16	0.03	0.01
23. Mallkastër	0.30	0.08	0.03	0.13	0.02	0.01
24. Mat	0.54	0.29	0.17	0.22	0.04	0.01
25. Mirditë	0.14	0.05	0.03	0.25	0.05	0.01
26. Peqin	0.32	0.11	0.05	0.19	0.03	0.01
27. Përmet	0.11	0.02	0.01	0.12	0.02	0.01
28. Pogradec	0.19	0.04	0.01	0.17	0.03	0.01

(continued)

Table 5.6 (continued)

	2005			2008		
District	FGT (0)	FGT (1)	FGT (2)	FGT (0)	FGT (1)	FGT (2)
29. Pukë	0.12	0.03	0.01	0.32	0.07	0.02
30. Sarandë	0.09	0.03	0.01	0.09	0.02	0.01
31. Skrapar	0.12	0.07	0.06	0.18	0.03	0.01
32. Shkodër	0.10	0.02	0.01	0.17	0.04	0.01
33. Tepelenë	0.13	0.06	0.04	0.13	0.02	0.01
34. Tiranë	0.09	0.02	0.01	0.12	0.02	0.00
35. Tropojë	0.27	0.08	0.04	0.18	0.02	0.01
36. Vlorë	0.09	0.02	0.00	0.12	0.03	0.01

Beyond the specific results presented for Albania, this chapter makes an important contribution to the literature on small area estimation, by presenting a comparison of two different methodologies for updating poverty maps in inter-census years. The method we propose shows that poverty maps which are very appealing and potentially very useful for policy making can be updated without a need for more frequent census updates or imposing strong restrictions on existing data (e.g., that they should be panel or contain large time-invariant characteristics). In our method, only repeated cross sections of surveys are sufficient to estimate poverty at very disaggregated levels.

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Chapter 6
Social Exclusion in Bosnia and Herzegovina

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Introduction

Measurement and social policy design in Bosnia Herzegovina (henceforth BiH), as in the other countries in the Western Balkans, is currently undergoing a transition towards the social inclusion framework adopted in the European Union. Different sets of indicators of exclusion have been developed over time, since the adoption of the Europe 2020 target for the risk of poverty and exclusion (Chap. 2), the key elements of this measuring framework are the risk of poverty, attachment to the labour market and material deprivation. While the official poverty rates computed by the BiH Agency for Statistics already use a relative poverty measure,[1] adopting these new indicators will still involve a change from measuring poverty from the space of consumption to income. The introduction of material deprivation is new to the poverty measurement discourse in BiH, and so is the measure of low work intensity.

This chapter takes advantage of specially collected data on social exclusion based on the module developed for the Extended Household Budget Survey 2011 (henceforth EHBS) following the recommendations of the Expert Group on "Measuring poverty and social exclusion in pre-accession and European neighbourhood

The findings, interpretations and conclusions expressed in this chapter are those of the authors and do not necessarily reflect the views of the International Bank for Reconstruction and Development/ The World Bank and its affiliated organizations, or those of the Executive Directors of The World Bank or the governments they represent. The World Bank does not guarantee the accuracy of the data included in this work.

[1]The World Bank typically measures poverty in BiH, as in all other countries of Eastern Europe, based on an absolute consumption poverty measure.

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countries" (Chap. 3).[2] It can therefore present for the first time for BIH estimates of the indicators of social exclusion that all European Union Member States are bound to monitor to report on their progress towards the Europe 2020 social inclusion target. These initial estimates give a flavour of the type of information that the EHBS will allow the State Agency for Statistics (henceforth BHAS) to report on in the future. It also allows us to contrast the more standard poverty analysis with the insights of these new indicators.

The chapter is structured as follows: the section "Data Description" provides a brief discussion of data and methodology underlying the analysis of social exclusion and material deprivation; the section "The Risk of Poverty and Social Exclusion Profile" provides a profile of social exclusion and material deprivation based on 2010 data, including comparisons between social exclusion indicators and consumption-based poverty measures; the section "Material Deprivation" provides some concluding remarks.

Data Description

This chapter uses data collected in the last quarter of 2010 by the LITS-SM survey. The survey was conducted as a follow-up interview of the sample that had been interviewed for the BiH 2010 wave of the Life in Transition Survey (LiTS)—a cross-country effort (including all transition economies and in 2010 several Western European countries) covering almost 39,000 households in 34 countries to assess public attitudes, well-being and the impacts of economic and political change in the region based on a nationally representative sample in each of the countries.[3]

The sample of the LiTS 2010 survey in BiH included 1,087 households. The supplemental modules, fielded 2 months after the original LiTS survey, were able to capture 842 households. While attrition is not random,[4] the differences between either the LiTS or the LiTS follow-up sample from the BiH population census

[2]Since the adoption of the *Europe 2020* strategy social inclusion, indicators have become very visible at the European level. It is therefore very important that BiH by supplementing the core HBS structure with social inclusion modules has adopted a practical solution that will allow us to start monitoring progress on these new indicators while ensuring continuity with the HBS series and the measurement of monetary poverty based on a consumption indicator as it has been done over the past decade.

[3]The LITS was collected jointly by the European Bank for Reconstruction and Development and the World Bank.

[4]A larger share of attrited households comes from Republika Srpska (RS), and a smaller share is from North FBIH and especially from Sarajevo. The attrited households also report lower levels of per capita consumption than the overall LiTS sample and similarly a lower incidence of important household assets such as a car, computer and mobile or fixed phones, indicating a lower overall welfare level relative to the full sample (see table 6.14 and 6.15 in Appendix 1).

distribution do not appear to be systematic.[5,6] As the result, the sample used in this chapter is treated as self-weighting.[7]

The supplemental modules were designed to provide information on the impact of the crisis (including labour market dimensions, remittances and reliance on social assistance programmes) and social exclusion indicators.[8] The module on social exclusion is based on the EHBS social exclusion module, which in turn collects the main variables of the EU-SILC survey to measure exclusion. In addition, the module includes some of the migration and remittances variables collected in other modules of the EHBS. Combining information from the LITS and the additional modules, the LITS-SM includes information on income, expenditures, social exclusion and labour market activities.

The expenditure-based measure of welfare which we use to compare the social exclusion indicators with measures of poverty used to date in BiH is derived from the consumption module in the LiTS survey, where households report monthly household expenditures for the following three categories: (1) food, beverages and tobacco; (2) utilities (electricity, gas, water, heating, fixed line telephone); and (3) transportation (public transportation and car fuel); and also expenditures over the past 12 months for the following expenditure categories: (4) education (including tuition, books, kindergarten expenses); (5) health (including medicines and health insurance); (6) clothing and footwear; and (7) durable goods. The consumption aggregate used in this chapter is based on the total household expenditures on all of the above categories, expressed in per adult equivalent terms. This consumption indicator is not comparable with the consumption indicator collected by the BHAS through the HBS surveys, and as such, it cannot be used to update either the national poverty estimates or those regularly published by the World Bank (World Bank 2009).

The Risk of Poverty and Social Exclusion Profile

As discussed in Chap. 2, the concept of social exclusion looks at deprivation as complex and multidimensional, and the three indicators which combined measure the risk of poverty and social exclusion overall poverty objective capture the main

[5]The differences are not systematic in the sense that there is no household-level variable that explains the difference between the population pyramid based on the LiTS-SM sample and the population pyramid given by census (see Fig. 6.4). If such a variable existed, it could have been used to reweigh the sample accordingly. Given that no such variable could be found, the LiTS-SM sample of households is regarded here as a self-weighting sample of all households in the country. The LiTS sample is a self-weighting sample of households by design.

[6]The estimates of the population by age groups are from the US Census Bureau international database (http://www.census.gov/ipc/www/idb/informationGateway.php).

[7]Note that in the LiTS survey, the households were sampled consistent with a self-weighting sample. The weights were then applied in order to back out the distribution of the adult (18+) population of BiH. Since we are more interested in population estimates of household characteristics and not with the opinion questions of the LiTS survey, re-weighting would not necessarily be appropriate.

[8]A special module on health was also collected to provide information on a separate research project.

dimensions of the concept. They include the *risk of poverty*, living conditions severely constrained by lack of resources (*material deprivation*), and exclusion from the labour market (*low work intensity*).

This section provides a broad profile of these three key social exclusion indicators both singularly taken and aggregated as in the Europe 2020 measure. It also provides some comparisons with other EU Member States, one of the advantages of having internationally comparable measures.

At-Risk-of-Poverty Profile

In the European Union, the at-risk-of-poverty indicator is defined as having an income level that is below 60% of the median income in the country, expressed in equivalent adult units based on the OECD scales.[9] This is the measure that we use in this chapter. This measure is different from the official poverty rate reported by the BHAS[10] and from the poverty rates calculated by the World Bank (World Bank 2009).[11] To calculate the risk of poverty, we use income data from the LiTS-SM.

According to 2010 data from LiTS-SM, the *at-risk-of-poverty population* is comprised roughly of 1.5 million people or 32% of the overall population of BiH. EUROSTAT estimates that in 2010, the at-risk-of-poverty ratio was 21% in Bulgaria, Croatia and Romania and 16% overall for the EU-27 group of countries (Table 6.1).

In BiH, the at-risk-of-poverty population is concentrated in rural areas, which account for 58% of the total, compared to total share of the rural population (51%). The higher risk of poverty in rural areas is consistent with patterns in new EU members, as well as in Southern European states (Portugal, Spain, Greece or Italy) where the risk of poverty is also higher in rural areas (European Commission 2011).[12]

Disaggregating by the sex of the household head, female-headed households are less represented in the at-risk-of-poverty group compared to their overall population share in rural areas, whereas in urban areas, the distribution is even across male- and female-headed households. In terms of the age group of the head of household, in urban areas, the at-risk-of-poverty population is concentrated in households where the household head is in the 65+ age group—27% of the at-risk-of-poverty group come from such households compared to their share of 19% of overall population. In rural areas, a higher than average share of those at risk of poverty is in households

[9] According to the OECD scale, the first adult household member gets a weight of 1, all subsequent adults a weight of 0.5 and all children under the age of 14 a weight of 0.3.

[10] The national poverty measure reported by the BiH Agency for Statistics is based on a relative poverty threshold set at 60% of median consumption per equivalent adult (based on HBS data). The latest national estimate of poverty headcount, based on this measure, was 18.2% according the HBS 2007 data.

[11] The World Bank computes poverty as is the 2001 LSMS-based poverty line set at KM 205 per capita per month in 2007 prices.

[12] In contrast, in northern European countries, the at-risk-of-poverty rate tends to be lower in rural areas.

Table 6.1 Age profile of the at-risk-of-poverty population (%)

	At risk of poverty	Overall	Incidence of poverty risk
0–17	21.7	17.7	40.1
18–24	11.3	11.3	32.8
25–34	12.9	17.6	23.9
35–44	15.7	13.8	37.2
45–54	17.0	16.1	34.6
55–64	10.9	12.4	28.9
65+	10.5	11.1	31.2
Total	100	100	32.8

Note: Authors' calculations based on LiTS 2010 and supplemental module data

where the household head falls into the 45–54 age group (33% of the at-risk-of-poverty population compared to the overall share of 29% of population in that group).

The overall age distribution of the adult population suggests a somewhat higher risk of poverty for those in the 35–44 age group, although this is primarily a rural phenomenon. The risk of poverty is also considerably higher for children (ages 0–17) both in urban and rural areas. The lowest poverty risk is recorded in the 25–34 age group. The situation is broadly similar in the EU, where the risk of poverty is considerably higher among children, whereas the at-risk-of-poverty rate among the elderly is in line with the average risk for the country.[13] The group of 18–24-year-olds which tends to be at higher poverty risk in EU Member States does not appear to be more affected than others in BiH.

Those residing in large households (five household members or more) are at a much higher risk of poverty in both urban and rural areas. For smaller households, in rural areas, the risk of poverty is similar for households of 1, 2 or 4 members and somewhat higher for three-member households. In urban areas, the risk of poverty is smallest in single-member households, increases slightly for two-member households and then much more markedly for three-member households. Larger household size is similarly associated with higher risk of poverty in the European Union.

As is commonly the case, the risk of poverty is strongly associated with education. While overall 31% of the population reside in households where the household head has primary education or less, in the at-risk-of-poverty group, this share is 49%. Similarly, while 44% of the population overall comes from households where the household head has completed upper secondary education or above, only 28% do so in the at-risk-of-poverty group. The overall risk of poverty is highest for those residing in households where the head of household has primary education (54%) and lowest for those in household where the head has a bachelor's degree (11%) (Table 6.2).

This association is mirrored by the distribution of own education levels and welfare. Among those in the 25+ age group, 31% reported having primary education or less in 2010, but these individuals account for 45% of the population in the at-risk-

[13] Although in a number of EU countries poverty risk is higher for the 65+ age group (e.g. Bulgaria, Denmark, UK).

Table 6.2 Welfare distribution by education level of household head, 2010 (%)

	At risk of poverty	Overall
No education/degree	11.6	8.5
Primary	37.1	22.3
Lower secondary	23.1	25.1
(Upper) secondary	22.4	30.3
Post-secondary non-technical	3.1	5.6
Bachelor's degree or higher	2.8	8.2
Total	100	100

Note: Authors' calculations based on LiTS 2010 and supplemental module data

Table 6.3 Education and risk of poverty (%)

	At risk of poverty	Overall	Incidence of poverty risk
No education/degree	14.9	10.3	44.4
Primary	29.6	20.8	43.6
Lower secondary	24.2	24.9	29.9
(Upper) secondary	25.0	30.8	24.9
Post-secondary non-technical	2.8	4.6	18.4
Bachelor's degree or higher	3.6	8.5	12.9
Total	100	100	30.7

Note: Authors' calculations based on LiTS 2010 and supplemental module data

of-poverty group. As in the case of the education of household head, individuals with low education levels (primary or lower) face a much higher than average poverty risk, and the reverse is true for those with post-secondary education (Table 6.3).

Another strong predictor of poverty risk is employment status. In the at-risk-of-poverty group, 70% of those in the age group 25–60 did not work during the past 12 months, compared to 51% overall. Based on the employment status of the household head, 40% of the adult population resided in households where the household head did not work during the past year, but in the at-risk-of-poverty group, the corresponding share was 60% (Table 6.4).

These two dimensions—education and labour market status—are themselves strongly related. In the 25–60 age group, 34% of those who did not work over the past 12 months had primary education or less, compared to only 11% of those who worked. Looking at it another way, 81% of those with no education did not work over the past year, compared to only 21% of those with a bachelor's degree or higher.

Labour market participation differed considerably between men and women—63% of men and 37% of women in the 25–60 age group reported having worked during the past 12 months. Participation rates increase for higher levels of education, and among those with a bachelor's degree or higher, the differences in labour market participation between men and women vanish.

In terms of the main livelihood source, wages are much less prevalent and reliance on sales of farming products more prevalent in the at-risk-of-poverty group as

Table 6.4 Employment status and education levels, 25–60 age group (%)

	Worked for income	Did not work for income	Worked for income	Did not work for income	
	Row percentages		Column percentages		Overall
No education/degree	19.0	81.0	1.8	7.2	4.5
Primary	25.2	74.8	9.1	26.0	17.7
Lower secondary	47.0	53.0	26.2	28.5	27.3
(Upper) secondary	54.9	45.1	39.6	31.4	35.4
Post-secondary non-technical	72.6	27.4	7.2	2.6	4.9
Bachelor's degree or higher	78.5	21.5	16.3	4.3	10.2
Total	49.1	50.9	100	100	100

Note: Authors' calculations based on LiTS 2010 and supplemental module data

compared with the general population. On the other hand, the prevalence of self-employment income and of pensions is roughly similar in these two groups.

Estimates from a multivariate profile of risk of poverty (see Table 6.16 in Appendix 2) confirm higher poverty risk for those residing in households where the head has a low level of education. The higher risk of poverty associated with low educational attainment is still present when the main livelihood source of the household is accounted for. In individual level regressions (not reported), having no education is associated with a higher risk of poverty, controlling for the education of the head of household.

The risk of poverty is also positively associated with the absence of the household head in the labour market, even controlling for education and the main livelihood source in the household. Individual level regression estimates confirm the strong negative correlation between employment of the household head and lower poverty risk, even if one's own employment status is accounted for. One's own unemployment is similarly associated with a higher risk of poverty, holding the employment status of the head of household constant.

The risk of poverty is higher for households where the main source of livelihood is self-employment income (relative to wages) and especially for households relying on sales of farming products. While the presence of remittances in the household is negatively associated with poverty risk, when help from family and friends is the main income source, the conditional poverty risk is higher than for households relying on wage income.

Characteristics such as the age and sex of the household head, as well as the size of the household, do not appear to be significant predictors of poverty risk conditional on other characteristics, whereas a higher share of adult women and of the elderly appears to be associated with a lower risk of poverty. Individual level regression estimates confirm that poverty risk decreases with age, and is lower among women, conditional on other personal and household characteristics.

Note, finally, that while unconditionally risk of poverty is higher in rural areas, this appears to be driven by the underlying characteristics of the urban/rural populations. Once characteristics such as education, labour market participation and household composition are held constant, rural areas are no longer associated with a higher probability of poverty risk at conventional confidence levels.

Material Deprivation

In the European Union, the material deprivation indicator is based on a list of nine variables[14] (data for which is collected in the EU-SILC survey) recording whether people can afford the following: (1) pay their rent or utility bills; (2) keep their house adequately warm; (3) face unexpected expenses; (4) eat meat, fish or a protein

[14] Atkinson and Marlier (2010).

equivalent every second day; (5) a week of holiday away from home once a year; (6) a car; (7) a washing machine; (8) a colour TV; and (9) a telephone. The main focus is on the material deprivation rate, defined as the enforced inability to pay for at least four of the above-mentioned nine items. This indicator aims to capture the extent to which individuals might be unable to achieve the living conditions considered typical in the European Union due to lack of financial resources.

The information collected in the LITS-SM focuses on a slightly different set of variables, identified during the design phase of the EHBS as better responding to the reality in BiH, therefore making this indicator only broadly comparable with those collected in EU Member States.[15] In particular, we do not have data on the affordability (as separate from possession) of cars, washing machines, TVs or telephones (variables 6–9 in the list above). Variables 1–5 are the same as in EU-SILC, the unexpected expenses being defined at the level of 60% of median consumption per adult equivalent in 2007. Based on these data and to keep a focus on the enforced lack of a given item, the definition of material deprivation adopted in this chapter is defined as the enforced inability to pay for at least three of the following five items: (1) pay their rent or utility bills; (2) keep their house adequately warm; (3) face unexpected expenses; (4) eat meat, fish or a protein equivalent every second day; and (5) a week of holiday away from home once a year.

The above definition differs from the EU definition and is based on data availability. Note that while the EU definition focuses only on the aggregate indicator of material deprivation, as this is the first time that detailed material deprivation indicators are available for the country, we also look at them individually trying to understand what they add to our understanding of exclusion in BiH.

An Aside: The Individual Variable Capturing Material Deprivation

Variables capturing material deprivation when individually taken can be highly controversial, and indeed, they are not intended to be in themselves alone poverty measures. It is the accumulation of a number of these material deprivations that is likely to make the living conditions that a household can afford so different from a society's norm as to make that household stand out as marginalized.[16] Since the beginning of this type of research (Townsend 1979), however, the selection of indicators, and their perceived ad hoc nature, has generated a huge amount of

[15]The variables collected in the LiTS-SM match the variables collected by the EHBS.

[16]This concept which has developed in a sociological intellectual tradition that is very different from the welfarist framework typically used by economists has a clear resonance with how deprived groups often describe their situation and their interactions with others. As an example among the many that qualitative analysis can provide, consider the response of a Roma woman when asked about her children schooling "Our children are insulted at school because they have nothing to wear and they have no textbooks" (IPSOS 2009).

Table 6.5 Share of households unable to afford (%), by urban/rural

	Urban	Rural	Overall
Pay rent or utility bills	16	21	18
Keep house adequately warm	26	25	25
Unexpected expenses of KM 386	74	68	71
A meal of meat, fish or vegetable protein	28	27	27
Holiday away from home	60	73	66

Note: Authors' estimates based on data from LiTS supplemental modules, 2010

debate. Criticisms included the impression that the variables were focused on one particular lifestyle or that they included a number of items which would be "nice to have" but whose enforced absence did not necessarily capture deprivation.

To address these concerns, at the European level, the choice of items collected by the SILC (of which those collected in BiH are a subset) has been validated by a Eurobarometer survey in 2007, which verified that almost all items included were considered necessities by at least 50% of the population. More recently, in 2009, a long material deprivation module was run with the SILC to explore a variety of new indicators that can be used to refine the current list of necessities and possibly finding ways of adapting it to national circumstances. The process of analysing those data at the EU level is ongoing and will feed into a revision of the Europe 2020 at risk of poverty and exclusion target planned for 2014 (European Commission 2011).

As this is the first time that this type of indicators, and particularly the indicators that are going to be collected by the EHBS, is analysed for BiH, it is worth looking at them more closely, to understand what they capture and possibly start a reflection on whether in the future they might be further adapted to capture the essential features of living in BiH.

Of the five variables collected in the LiTS-SM that capture the inability to afford necessities (i.e. the inability to pay rent or utility bills; to keep the house adequately warm; to face unexpected expenses; to eat meat, fish or a protein equivalent every second day; and to take a week of holiday away from home once a year), the most salient one is the inability to afford unexpected expenses worth 386 KM (Euro 195)—more than 70% of households appear to be unable to afford an unexpected expense of this magnitude through their own resources. Two thirds of households appear to be unable to afford a week's annual holiday away from home. The distribution of these indicators appears to be broadly similar across urban and rural areas (Table 6.5). An econometric analysis of the profile of households deprived in each of the indicators discussed is presented in Table 6.17 of Appendix 2 and the notes attached.

As expected, these deprivations are correlated. For instance, in households that could not afford proper nutrition, 98% also could not afford unexpected expenses (compared to 61% among those who could afford proper nutrition). Among households that could not afford to pay rent or pay utility bills, 37% could not afford to keep the house adequately warm, whereas among households that had no issues with rent/utility bills payments, 23% could not afford to keep the house adequately warm.

Table 6.6 Material deprivation and ability to make ends meet (%)

	Pay rent or utility bills	Keep house adequately warm	Unexpected expenses of KM 386	A meal of meat, fish or vegetable protein	Holiday away from home
With great difficulty	45	47	97	68	96
With difficulty	28	33	94	53	91
With some difficulty	14	24	74	15	72
Fairly easily	7	16	46	7	32
Easily	5	3	15	0	5
Total	18	25	71	27	66

Note: Authors' estimates based on data from LiTS supplemental modules, 2010

But are these indicators capturing real necessities? This is not a question that we can answer directly with reference to how the inhabitants of BiH define necessities, as it has been done for EU Member States. Comparing the incidence of these indicators across quintiles or for households at risk of poverty or not is not very telling. While on the one hand it confirms that these deprivations are higher among those at the bottom, it also shows that the incidence of these deprivations is relatively high also for the non-poor. For example, 82% of those at risk of poverty could not afford to meet unexpected expenses with own resources, and 83% could not afford a vacation away from home compared with 71% and 66%, respectively, for the non-poor. High rates reported by richer groups are hard to interpret as it is not possible to disentangle the impact of the crisis that affect their levels of material deprivation, from the problems related to the choice of the indicators.

The data provide however other pointers that the material deprivation variables collected in BiH broadly represent necessities. We would expect that if something is a necessity, for example, those who report to have no problems making ends meet should be able to afford it. As Table 6.6 shows, this is indeed the case. Future research might however investigate whether a lower threshold might have to be adopted for the unexpected expenses indicators, as many as 15% of the heads of households who felt their families had no problems making ends meet reported that they could not mobilize that amount. One holiday away from home, which is likely to generate more concerns as a variable capturing deprivation, appears however to be something that the households in BiH who can make ends meet can generally afford and therefore less of a concern.

Further confirmation of the association between these variables and the household standard of living is offered by their distribution across categories of households as identified by the head educational status and employment status, two variables that are associated with higher incomes and expenditure levels. As Fig. 6.1 shows the inability to afford these different items exhibits a reassuring pattern across categories, though even households that we would expect to be better off cannot necessarily afford the 1 week holiday and can mobilize the 386 KM.

Overall therefore, while there seems to be scope to explore more extensively and validate further the variables included in our survey and in the EHBS to measure material deprivation, they seem to be broadly in line with the intention for which they were included.

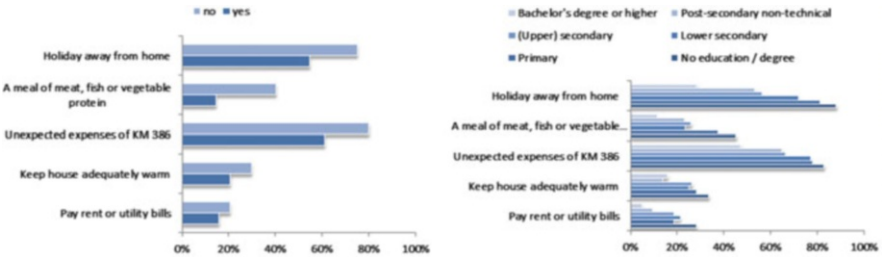

Fig. 6.1 Material deprivation rates by level of education and employment status of HH head (%). *Note*: Authors' estimates based on data from LiTS supplemental modules, 2010

Material Deprivation Profile

Overall, the material deprivation rate based on deprivation in three out of five areas is 37% in BiH—equivalent to roughly 1.7 million people. This MD rate, while measured slightly differently, is similar to the ones observed in new EU members (40% in Bulgaria, 32% in Romania, 22% in Latvia), while at the level of EU-27, only 8% of the population face exclusion on the MD dimension (European Commission 2011).

The materially deprived population is somewhat more evenly distributed across urban and rural areas than the at-risk-of-poverty population—rural areas accounted for 53% of the materially deprived (51% of population resides in rural areas).

Recall that poverty risk in BiH was found to be higher among children and among those in the 35–44 age group. The age profile of material deprivation differs from that of poverty risk. The material deprivation rate is higher than average for those in the 55–64 age group, and especially for the 65+ population, but not among children. In the 35–44 age group, the MD rate is also somewhat below average. The higher MD rate among the elderly is observed both in rural and urban areas, whereas the lower level of material deprivation in the 35–44 age group is primarily associated with urban areas of BiH (Table 6.7).

The higher material deprivation associated with the elderly population is confirmed by the MD profile based on the age of the head of the household—a higher share of the MD population resides in households where the HH head is in the 55+ age group. Female-headed households are overrepresented in the materially deprived population, a pattern driven by the higher MD of FHHs in urban areas. This is in contrast with the profile of the at-risk-of-poverty population where female-headed households had below average poverty risk.

An interesting difference between the profile of the households which are in material deprivation as opposed to those classified as at risk of poverty is that while on average the risk of poverty is higher for larger households (5+), this is not the case with those that are materially deprived. In fact, the material deprivation rate is highest for single-member households in both rural and urban areas, whereas households composed of three members appear to be deprived the least.

Table 6.7 Age profile of the materially deprived population (%)

	MD population	Overall	MD rate
0–17	17.9	17.7	37.3
18–24	10.5	11.3	34.3
25–34	14.0	17.6	29.4
35–44	12.3	13.8	32.9
45–54	16.3	16.1	37.4
55–64	13.9	12.4	41.5
65+	15.0	11.1	49.8
Total	100	100	36.9

Note: Authors' calculations based on LiTS 2010 and supplemental module data

Table 6.8 Material deprivation by category of main household income (%)

	MD population	Overall population	MD rate
Salary, wages	45.2	54.9	30.4
Self-employment income	10.1	11.3	33.0
Sales of farm products	8.1	7.5	39.7
Pensions and state benefits	32.2	22.7	52.3
Help from relatives/friends	4.5	3.6	45.9
Total	100	100	36.9

Note: Authors' estimates based on data from LiTS supplemental modules, 2010

Also in the case of material deprivation, as it was the case with the risk of poverty, labour market attachments and educational level of the head of the households are important correlates. In households where the HH head worked during the past 12 months, the material deprivation rate was 27%, whereas it was 50% in household where the head did not work during the past year. Likewise, the material deprivation rate exceeded 50% in households where the head had no formal education, and only 8% of the population in households where the head had tertiary education were similarly deprived.

Looking across main income sources, households who rely on salaries/wages and or income from self-employment as their main livelihood source as compared to households that rely on proceeds from the sale of farmed products, from pensions or from help of relatives or friends have much lower incidence of material deprivation[17] (Table 6.8).

Low Work Intensity Households

The third component of EU's at-risk-of-poverty or social exclusion (AROPE) indicator is living in a household with very low work intensity. The work intensity of a household is the ratio of the total number of months that all working-age household

[17]Only seven households in our sample report benefits from the state as their main livelihood source.

members have worked during the income reference year and the total number of months the same household members theoretically could have worked in the same period, and the low intensity threshold is set at 20%.

In this chapter, we define low work intensity as one where the number of months worked by working-age household members over the past 12 months is less than 20% of the theoretically possible amount. This is in line with the EU's definition even the definition had to be adapted due to data limitation. The LiTS-SM only records whether someone was employed (and similarly if someone was a student) over the past 12 months or not. This implies, for instance, that a person of working age is assigned a theoretical work load of 12 months over the past year and an actual work load of 12 months if that person reported being employed and 0 months if that person was not employed. Likewise, an individual in the 18–24 age group who did not work but was a student over the past 12 months is assigned a theoretical and actual work loads of 0 months.[18]

Roughly a quarter of households fall into the low work intensity category in 2010.[19] These households are home to about 1.2 million people or 26% of the BiH population. This is higher than in the EU-27 as a whole, where only 9% of the population lives in low work intensity households. Even in countries like Bulgaria and Romania, the share of population residing in low work intensity households was under 10% (15% in Croatia).

This group is somewhat skewed towards rural areas, which account for 52% of total (relative to 45% in households that are not excluded from the labour market). The higher prevalence of labour market exclusion in rural areas is similar to the patterns in new European states, whereas in the EU-15, it is densely populated areas that have a higher share of population residing in low work intensity households.

Not surprisingly, the risk of poverty is positively associated with low work intensity. For instance, 55% of the population residing in low work intensity households were at risk of poverty, compared to only 25% in households that were not excluded from the labour market. More than 40% of the population in the at-risk-of-poverty group were residing in low work intensity households, whereas in households that were above the risk-of-poverty threshold, this ratio was only 17%. Similar patterns are observed in the EU. For the group of EU-27 countries, the at-risk-of-poverty rate exceeded 50% in low work intensity households, and the risk of poverty decreases considerably once work intensity exceeds 50%. However, the evidence from the EU suggests that work intensity has to be quite high (above 60%) or even very high (above 80%) in order to reduce significantly the risk of poverty (European Commission 2011).

[18]Following EU definitions, households composed entirely of individuals in the 60+ age group, students or combinations of these groups are excluded from the calculations of the low work intensity rate.

[19]The ratio is 30% if households composed entirely of the elderly and/or students are excluded.

Table 6.9 Material deprivation is more acute in low work intensity HH (%)

	At least 1 employed HH member	Low work intensity HH	Total
Pay rent or utility bills	17.0	22.6	18.4
Keep house adequately warm	23.7	30.8	25.4
Unexpected expenses of KM 386	66.4	84.6	70.9
A meal of meat, fish or vegetable protein	23.3	39.4	27.3
Holiday away from home	60.9	81.3	65.9
Total number of deprivations (0–5)	1.9	2.6	2.1

Note: Authors' estimates based on data from LiTS supplemental modules, 2010

Low work intensity households are similarly associated with more acute material deprivation. For instance, 85% of low work intensity households are unable to afford unexpected expenditures, whereas this is the case for 66% of non-low work intensity households. Low work intensity households are also less likely to be able to afford proper nutrition or vacations, to keep current on utilities/rent or to keep their household adequately warm (Table 6.9). Notably, the deprivation of low work intensity households appears to be particularly acute when it comes to meeting unexpected expenses or being able to afford appropriate nutrition, highlighting the vulnerability of these households to income shocks.

The Relationship Between Poverty Risk, Material Deprivation and Low Work Intensity

The relations between risk of poverty, material deprivation and labour market exclusion can be seen in Table 6.10 and Fig. 6.2. Overall, 2.7 million people or 58% of BiH population reside in households that are either at risk of poverty, excluded from the labour market or report at least three material deprivations; just under 440,000 people (or 9.5% of the population) suffer from exclusion in all three areas. Among those at risk of poverty, 43% also come from low work intensity households, while in the latter group, 55% are also at risk of poverty. More than half of the population in the at-risk-of-poverty group also report three or more material deprivations.

Two things stand out in Fig. 6.2, particularly when comparing it to the pattern for EU Member States and for selected countries (shown in Fig. 2.3).

First, the incidence of the three deprivations is relatively similar with material deprivation the largest deprivation only 11 percentage points higher than the smallest—workless households. This is quite different from the examples presented in Fig. 6.4, where one of the three components of the measure clearly dominates. Note that the prevalence of MD is also less extensive than in the case of

Table 6.10 How do various dimensions of social exclusion relate? (individuals)

Category	Population
1. Residing in low work intensity HH	1,189,468
2. At risk of poverty	1,514,576
3. At least 3 material deprivations (out of 5)	1,705,358
Intersection of (1) and (2)	650,216
Intersection of (1) and (3)	673,578
Intersection of (2) and (3)	813,744
Intersection of (1), (2) and (3)	439,967
Union of (1), (2) and (3)	2,711,831

Note: Authors' estimates based on data from LiTS supplemental modules, 2010

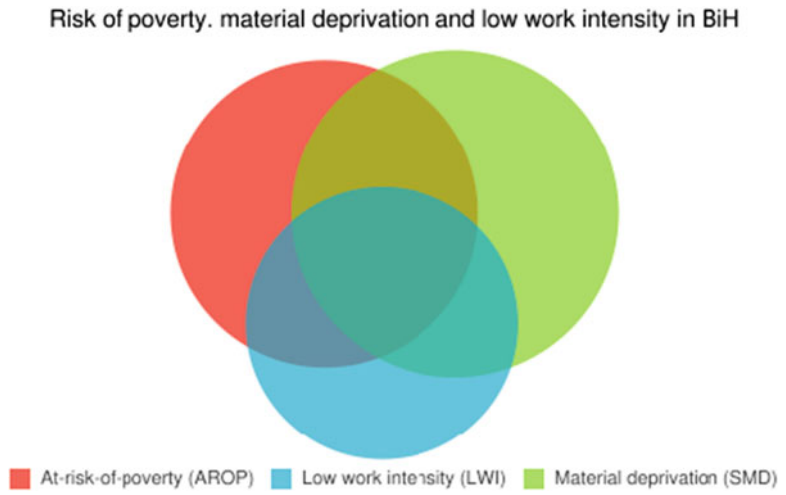

Fig. 6.2 Overlapping domains of poverty, material deprivation and low work intensity. *Note*: Authors' estimates based on data from LiTS supplemental modules, 2010. Size of bubbles and their overall corresponds to the relative size of the three categories

Bulgaria, one of the new MS with which BiH could have more in common given their relatively low income levels. The smaller number of items included in the material deprivation indicator in BiH might have contributed to this finding.

Secondly, there is clear overlap between the three areas of social exclusion (Fig. 6.2),[20] even if a relatively small share is deprived across the three dimensions (16% of those who either were at risk of poverty, residing in a low work intensity household or had three or more deprivations, only 9.5% of the total population).

[20]This is also confirmed by a principal component analysis of the three domains (risk of poverty, low work intensity and the material deprivation indicator that identifies households with at least three deprivations out of five). According to the PCA estimates, only the first principal component has an eigenvalue exceeding 1 (the commonly used *Kaiser criterion*, according to which an additional principle component is retained when it extracts at least as much variance as the equivalent of one original variable), and this principal component explains close to 50% of the variation in the three social exclusion domains.

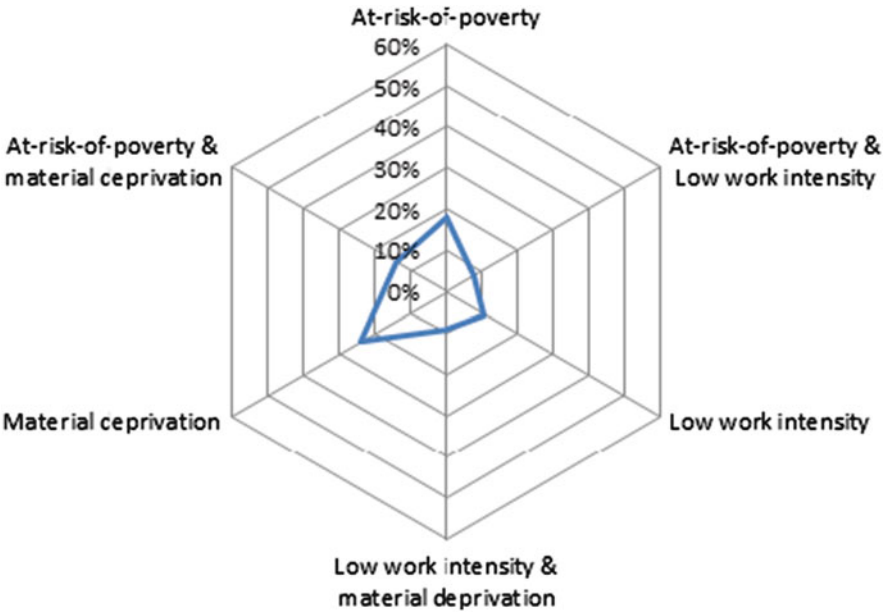

Fig. 6.3 Overlap between risk of poverty, material deprivation and low work intensity(% of the union of three categories). *Note*: Authors' estimates based on data from LiTS supplemental modules, 2010. Nonoverlapping categories. Intersection of AROP, LWI and MD omitted

As discussed when analysing the profiles of the different indicators which are part of AROPE, there are important links between these different deprivations. Labour market participation, in particular, is an important correlate of both the risk of poverty and material deprivation. Emphasizing the importance of the labour markets for the social agenda is one of the major policy contributions of the EU approach to measuring poverty and exclusion (Chap. 2), and this indeed seems to apply also for BiH.

Another tool to explore these differences is the spider chart presented in Fig. 6.3 which describes the incidence of the three different deprivations and their combination as a share of the union of these three categories. Figure 6.4 reproduces the latest charts for different groups of EU countries (European Commission 2011) for comparison purposes.[21] Again, the profile of the risk of poverty and social exclusion in BiH outside the overlapping region is considerably higher than for the EU states. Moreover, the at-risk-of-poverty-and-social-exclusion population is more evenly distributed across the three dimensions of deprivation, unlike in Bulgaria or Romania, where material deprivation dominates, or Western European countries like Luxembourg or Sweden, where risk of poverty dominates.

[21] Note that in all these charts, following European Commission (2011) the categories are nonoverlapping, and the intersection of the three indicators is omitted.

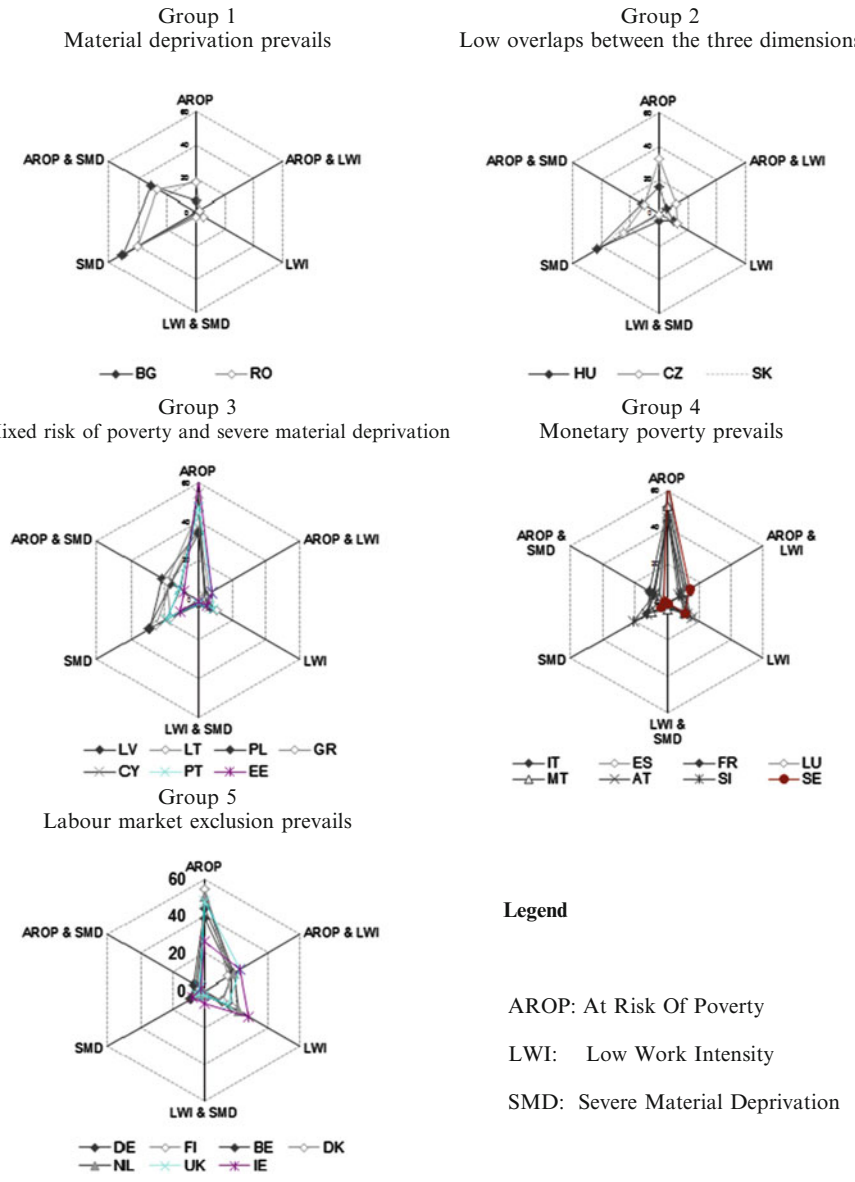

Fig. 6.4 Overlap between poverty risk, material deprivation and low work intensity in the European Union. *Source*: European Commission (2011), Chart 3, page 118

Are there notable differences in the main characteristics of the populations found at the intersections of the different domains of social exclusion? Estimates in Table 6.11 reveal that low work intensity HH with at least three deprivations is less likely to be rural. They also have a better education profile and are more reliant on pensions as their main livelihood source and less reliant on income from self-employment.

Table 6.11 Profiles of populations at the intersections of exclusion domains (% of total)

	At risk of poverty and 3+ deprivations	At risk of poverty and low work intensity HH	Low work intensity HH and 3+ deprivations	At risk of poverty and low work intensity HH and 3+ deprivations	Overall
Type of settlement					
Urban	41.6	41.0	48.3	45.6	49.4
Rural	58.4	59.0	51.7	54.4	50.6
Entity/district					
FBiH	73.1	69.8	77.5	76.5	67.0
RS	26.9	30.2	22.5	23.5	33.0
Age cohort					
0–17	22.8	22.8	20.2	23.9	17.5
18–24	10.6	8.1	9.0	8.4	11.3
25–34	13.2	15.9	12.7	13.7	17.7
35–44	15.9	17.7	17.1	20.4	13.9
45–54	15.9	15.9	16.2	14.6	16.1
55–64	10.8	12.6	17.3	11.5	12.4
65+	10.8	7.2	7.5	7.5	11.1
Sex					
Male	48.6	49.4	48.8	48.7	48.1
Female	51.4	50.6	51.2	51.3	51.9
Education					
No degree/no education	13.6	11.5	10.5	9.0	9.1
Primary education	31.5	35.1	33.7	33.9	22.4
Lower secondary education	24.5	21.0	21.1	22.0	23.5
(Upper) secondary education	27.3	28.6	30.5	31.6	33.4
Post-secondary non tertiary education	1.5	1.9	1.8	1.7	3.9
Bachelor's degree or more	1.5	1.9	2.5	1.7	7.7
Main income source in HH					
Salary or wages in cash or in kind	43.5	33.5	36.4	39.8	55.0
Income from self-employment	10.1	10.8	5.5	7.1	11.2
Sales or bartering of farm products	13.7	16.2	11.8	16.4	7.5
Pensions	23.3	28.1	37.3	26.1	21.8
Benefits from the state	3.1	5.7	4.3	5.8	0.9
Help from relatives or friends	6.3	5.7	4.6	4.9	3.5
Total	100.0	100.0	100.0	100.0	100.0

Note: Authors' estimates based on data from LiTS supplemental modules, 2010

Relative to overall population of BiH, the population at the intersection of all three domains of exclusion (risk of poverty, material deprivation and low work intensity) is more heavily concentrated in rural areas and is more skewed towards the bottom of the educational attainment distribution. It is also much more reliant on farm income and on benefits from the state and, respectively, much less reliant on wage income or income from self-employment.

The Relation Between the at Risk of Poverty and Exclusion Indicator and a Consumption-Based Poverty Measure

The consumption module included in the LiTS survey does not provide sufficient detail to provide poverty trends consistent with the 2007 poverty estimates.[22] To explore the relation between the new indicator of risk of poverty and social exclusion and the consumption-based poverty measures calculated so far for BiH, we defined a consumption-based poverty measure which identifies as poor the e bottom quintile of the LiTS consumption aggregate. While this cut-off is arbitrary, the size of the population below this threshold is broadly consistent with the 2007 poverty estimate from BHAS and also with the at-risk-of-poverty measures for Eastern European Member States of the European Union.[23]

Table 6.12 reports the distribution of the at-risk-of-poverty group and of other indicators of social exclusion by consumption quintile. It also includes the quintile distribution of the union and intersection measures described above.

Of those in the at-risk-of-poverty group, only 35% were also in the bottom consumption quintile. This is partly due to the fact that the consumption threshold is set at 20% of the population, whereas 32% of the population fall into the at-risk-of-poverty group (in other words, the poverty line is set too low to capture all those at risk of poverty). Nevertheless, even if we look at the bottom two consumption quintiles, they still only account for just over half of the at-risk-of-poverty group. Similarly, 43% of the population in the bottom consumption quintile in BiH are not at risk of poverty by the EU definition. In spite of the discrepancy between the bottom quintile group and the at-risk-of-poverty group, a similar share of both groups (just over 50%) is also deprived in at least three dimensions of material deprivation, and a similar share (just over 40%) comes from low labour intensity households (Table 6.13).

The estimates are broadly similar for other social exclusion indicators. Only 30% of the population with material deprivation in at least three out of five dimensions

[22] As the survey included only a summary consumption module, it cannot be used to measure precisely how much a household spends but rather to order households in terms of their spending relative to each other.

[23] According to 2008 EU-SILC data, the at-risk-of-poverty rate was 20% in Estonia and Lithuania, 21% in Bulgaria, 23% in Romania and 26% in Latvia (Eurostat 2010).

Table 6.12 At risk of poverty or exclusion indicator and its components, by consumption quintile

Consumption quintile	At risk of poverty	Material deprivation	Low work intensity	Union (poverty, MD or LWI)	Intersection (poverty risk, MD and LWI)
1	34.8	29.8	32.1	**27.9**	42.9
2	18.4	25.3	22.9	**22.7**	21.2
3	19.8	20.1	14.7	**19.9**	18.6
4	13.5	13.8	16.4	**16.4**	7.5
5	13.5	11.0	13.9	**13.2**	9.7
Total	100	100	100	**100**	100
Share of bottom quintile in:	57.0	54.9	41.3	**81.7**	42.9

Note: Authors' estimates based on data from LiTS supplemental modules, 2010. Values in bold are those of the union of the first 3 columns, i.e. the AROPE indicator

(or of the population residing in low work intensity households) is located in the bottom consumption quintile, and the bottom two consumption quintiles capture just over half of each of these two groups.

More than two thirds of the group identified as poor by AROPE are found outside of the bottom consumption quintile. However, 82% of the population in the bottom consumption quintile is identified by the union indicator, such that it captures rather well the types of deprivation that can be captured by a consumption-based indicator of poverty.

Comparing the profiles of deprivation based on consumption with the one based on the EU's main (union) indicator shows that the consumption poverty measure is more prevalent in rural areas and in the RS compared to the risk of poverty or exclusion indicator. There are no notable differences between the two definitions in terms of the distribution of the respective groups by sex, age or employment status. At the same time, the group identified by the bottom consumption quintile has a worse education profile—only 25% have upper secondary education or higher, compared to 35% based on the union indicator.

Conclusions

The purpose of this chapter was to present for the first time estimates of the indicators of social exclusion that all European Union Member States are bound to monitor to report on their progress towards the *Europe 2020* social inclusion targets. As part of this exercise, we have also explored what is captured by individual indicators of material deprivation, and we have contrasted the results of more standard poverty analysis with the insights offered by this new approach. Without repeating the specific findings, some general considerations are in order on what can be learnt from this exercise.

Table 6.13 At risk of poverty or social exclusion indicator (AROPE) and consumption poverty profiles (%)

	AROPE	Bottom quintile	Overall
Type of settlement			
Urban	45.4	36.7	49.4
Rural	54.6	63.3	50.6
Entity/district			
FBiH	67.0	62.0	67.0
RS	33.0	38.0	33.0
Age cohort			
0–17	18.6	20.7	17.5
18–24	10.4	13.1	11.3
25–34	14.2	11.6	17.7
35–44	13.2	14.3	13.9
45–54	16.9	14.8	16.1
55–64	13.9	12.7	12.4
65+	12.7	12.9	11.1
Sex			
Male	47.8	49.8	48.1
Female	52.2	50.2	51.9
Education			
No degree/no education	12.2	15.6	9.1
Primary education	27.9	30.2	22.4
Lower secondary education	24.8	29.2	23.5
(Upper) secondary education	28.5	20.7	33.4
Post-secondary non tertiary education	3.1	2.7	3.9
Bachelor's degree or more	3.5	1.6	7.7
Employment status over past 12 months			
Employed	22.7	23.3	35.6
Not employed	77.3	76.7	64.4
Main income source in HH			
Salary or wages in cash or in kind	43.1	43.9	55.0
Income from self-employment	11.2	7.4	11.2
Sales or bartering of farm products	10.7	13.5	7.5
Pensions	28.9	30.2	21.8
Benefits from the state	1.6	1.3	0.9
Help from relatives or friends	4.5	3.8	3.5
Total	100.0	100.0	100.0

Note: Authors' estimates based on data from LiTS supplemental modules, 2010

First, this approach is explicitly multidimensional, and as such, surveys that aim to measure being at risk of poverty and social exclusion need to include a new and larger set of variables than those traditionally monitored in a Household Budget Survey. BiH has chosen to integrate these new variables in the existing HBS and therefore allow both continuity and innovation in measurement. As this chapter

demonstrates, such approach allows the gathering of some extremely useful variables (such as those related to housing, long term unemployment and also the material deprivation indicators) which provide a much richer texture to the description of living conditions in the country.

Second, this approach, and particularly the focus on the aggregate of the three different indicators, will bring a new set of estimates of deprivation and possibly also a different distribution of those deprived across geographical areas. It will be important to keep monitoring the measures that have been used so far and to communicate clearly what the new numbers might capture not to confuse the public. Note, for example, that in our findings, a consumption-based measure would find that poverty is more concentrated in rural areas, in the RS and among the worst educated than the risk of poverty and social exclusion measure would.

Finally, the adoption of this approach allows the possibility of benchmarking the BiH experience with other countries which are EU Member States (and with candidate and potential candidate countries that are starting to collect SILC data). This opens up the door for mutual learning both on measurement and analytical issues and on policy. On the measurement side, as at the European level there is an ongoing effort to redesign the SILC survey, it will be important to continue testing and refining the indicators currently included in the EHBS, keeping them in line with the new SILC and possibly addressing some of the concerns that we have started exploring in this note. On the policy side, EU Member States, for example, use these data to look at the effectiveness of their social protection system and identify how it could be strengthened (this is something that our limited sample size did not allow us to do). Similarly, based on this analysis, strengthening the functioning of labour markets in light of the European Agenda for new skills and jobs remains a central key question in Europe. These are all examples and experiences from which BiH will be able to learn in the future to improve the design and the effectiveness of its own policies.

Appendix 1. Characteristics of the Sample

Table 6.14 Geographic distribution of original LiTS and supplemental modules samples (% of total)

	Attrited HH	Resample	Original sample
Cazin FBIH	8.6	5.1	5.9
East RS	22.9	13.7	15.7
Hercegovina	6.1	11.1	9.9
North FBIH	18.0	26.1	24.3
Sarajevo	2.5	15.0	12.1
West FBIH	8.2	8.1	8.1
West RS	33.9	21.0	23.9
Total	100	100	100

Source: LiTS 2010 data. None of the differences between the resample and the original LiTS sample are statistically significant at the 5% level

Table 6.15 Selected characteristics of original LiTS and supplemental modules samples

	Attrited HH	Resample	Original sample
HH size	2.82	2.82	2.82
Urban	0.56	0.53	0.54
Annual per capita consumption	7,290	8,386	8,139
Car	0.32	0.44	0.41
Computer	0.47	0.59	0.56
Mobile	0.17	0.25	0.23
Phone	0.24	0.26	0.26
TV	0.04	0.04	0.04

Source: LiTS 2010 data. None of the differences between the resample and the original LiTS sample with the exception of HH consumption are statistically significant at the 5% level

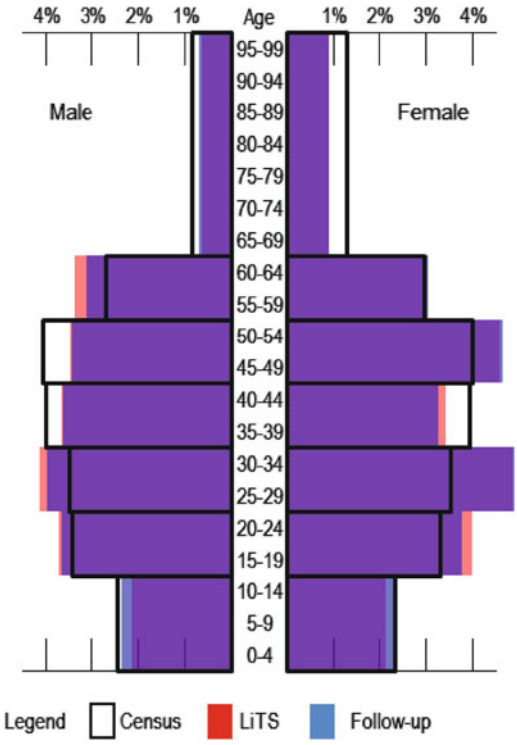

Fig. A.1 Correspondence between age-gender distributions in BiH Census, LiTS survey and the LiTS follow-up survey

Appendix 2. Detailed Multivariate Results

Table 6.16 Multivariate profile of at risk of poverty (household)

	At risk of poverty (1/0)	At risk of poverty (1/0)
Age	0.001	0.001
	(0.002)	(0.002)
Female HH head	–0.028	–0.041
	(0.041)	(0.040)
HH size	0.024	0.020
	(0.018)	(0.017)
HH composition		
Children share	0.028	0.067
	(0.130)	(0.127)
Youth share	–0.045	–0.048
	(0.092)	(0.087)
Adult female share	–0.247**	–0.177*
	(0.110)	(0.102)
Elderly share	–0.284***	–0.196**
	(0.098)	(0.093)
Not worked last year (HH head)	0.148***	0.157***
	(0.042)	(0.036)
Education of HH head		
No education	0.162**	0.111*
	(0.074)	(0.062)
Primary education	0.223***	0.193***
	(0.060)	(0.052)
Lower secondary education	0.015	0.015
	(0.034)	(0.033)
Post-secondary/university	–0.057	–0.042
	(0.041)	(0.045)
Rural	0.057	0.053
	(0.046)	(0.041)
Republika Srpska	0.046	0.014
	(0.049)	(0.045)
Remittances in HH (1/0)	–0.132**	–0.138**
	(0.057)	(0.059)
Main income source in HH		
Income from self-employment		0.104**
		(0.047)
Sales of farm products		0.338***
		(0.074)
Pensions		–0.022
		(0.038)
Help from relatives/friends		0.253***
		(0.080)
Pseudo R^2	0.121	0.158
Obs	808	808

Notes: Average marginal effects for probit regression reported. Estimates account for sampling weights. Robust standard errors in parentheses, clustered at PSU level in parentheses. Omitted categories: HH composition—share of adult males; education—upper secondary; work status—worked last year; area—urban; entity—FBiH. Significance levels: *$p<0.1$, **$p<0.05$, ***$p<0.01$
Source: LiTS 2010 and supplemental survey data

Table 6.17 Material deprivations profile

	Rent-utilities	Keeping the house warm	Unexpected expenses	Proper nutrition	Holiday away from home
Age	0.003*	0.000	−0.004**	0.002	0.000
	(0.002)	(0.002)	(0.002)	(0.002)	(0.002)
FHH	0.077	0.047	−0.011	0.035	0.051
	(0.047)	(0.047)	(0.044)	(0.040)	(0.049)
HH size	0.002	0.001	−0.010	−0.043**	0.067***
	(0.014)	(0.018)	(0.021)	(0.020)	(0.019)
Household composition					
Children share	−0.019	0.035	0.045	0.166	−0.293*
	(0.107)	(0.134)	(0.130)	(0.136)	(0.156)
Youth share	−0.152	−0.005	0.105	0.134	−0.061
	(0.097)	(0.101)	(0.100)	(0.106)	(0.104)
Adult female share	−0.138	0.007	−0.032	0.008	0.031
	(0.090)	(0.088)	(0.081)	(0.077)	(0.095)
Elderly share	−0.122**	0.000	0.182*	0.052	0.122
	(0.059)	(0.098)	(0.103)	(0.086)	(0.107)
Not worked last year (HH head)	−0.003	0.072*	0.098**	0.173***	0.077
	(0.040)	(0.043)	(0.045)	(0.043)	(0.048)
Education of HH head					
No education	0.006	0.080	0.139*	0.055	0.175**
	(0.073)	(0.083)	(0.079)	(0.083)	(0.085)
Primary	−0.055	−0.001	0.087*	0.034	0.132**
	(0.043)	(0.046)	(0.052)	(0.054)	(0.060)
Lower secondary	0.018	0.000	0.126***	−0.021	0.106*
	(0.034)	(0.051)	(0.049)	(0.050)	(0.055)
Post-secondary/ university	−0.133***	−0.114***	−0.119**	−0.096*	−0.163***
	(0.031)	(0.036)	(0.058)	(0.052)	(0.043)

Rural	0.040	−0.019	−0.094	−0.014	0.050
	(0.041)	(0.067)	(0.058)	(0.059)	(0.056)
Republika Srpska	−0.017	0.050	−0.017	0.019	0.101
	(0.045)	(0.083)	(0.055)	(0.068)	(0.062)
Any remittances in HH (1/0)	−0.075	−0.257***	−0.063	−0.147**	−0.007
	(0.058)	(0.069)	(0.054)	(0.060)	(0.076)
Main livelihood source of HH					
Income from self-employment	−0.051	0.048	−0.118*	0.040	0.072
	(0.045)	(0.068)	(0.071)	(0.060)	(0.056)
Sales of farm products	0.099	−0.193***	0.030	0.019	0.066
	(0.081)	(0.061)	(0.078)	(0.067)	(0.069)
Pensions	−0.009	−0.026	0.104**	0.025	0.082
	(0.047)	(0.057)	(0.047)	(0.046)	(0.064)
Help from relatives/ friends	0.144*	0.002	0.121	0.049	0.058
	(0.085)	(0.082)	(0.090)	(0.085)	(0.077)
Pseudo R^2	0.063	0.047	0.091	0.104	0.135
Obs	808	808	808	808	808

Notes: Average marginal effects for probit regression reported. Estimates account for sampling weights. Robust standard errors in parentheses, clustered at PSU level in parentheses. Omitted categories: HH composition—share of adult males; education—primary; work status—worked last year; area—urban; entity—FbiH. Significance levels: *$p<0.1$, **$p<0.05$, ***$p<0.01$

Source: LiTS 2010 and supplemental survey data

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Chapter 7
On Measuring Social Exclusion: A New Approach with an Application to FYR Macedonia

Joseph Deutsch, Jacques Silber, and Paolo Verme

> *By necessaries I understand not only the commodities which are indispensably necessary for the support of life, but what ever the custom of the country renders it indecent for creditable people, even the lowest order, to be without....Custom has rendered leather shoes a necessary of life in England. The poorest creditable person of either sex would be ashamed to appear in public without them.*
>
> Adam Smith, The Wealth of Nations (1776/1996*)*

Introduction

The term "social exclusion" is generally attributed to René Lenoir who for a while was "secrétaire d'Etat à l'action sociale" of the French government and published in 1974 a book entitled *Les exclus: Un Français sur dix*. Béland (2007) stresses, however, that as early as 1965, a social commentator named Jean Klanfer published in French a book entitled *Social exclusion: The study of marginality in Western societies* in which "the term 'social exclusion' refers to people who cannot enjoy the positive consequences of economic progress due to irresponsible behaviour" (Béland 2007). Klanfer's book was in fact also mentioned by Paugam (2005) as well as by

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Omtzigt (2009). Both authors mention the fact that the French economist Pierre Massé, who had been head of the French Planification Authority, had already used this term in a report he wrote on "The dividends of progress" (Massé 1964).

What did these various authors refer to when they used the term "social exclusion"? For René Lenoir, the "socially excluded" who, he argued, represented one-tenth of the French population were the " mentally and physically handicapped, suicidal people, aged invalids, abused children, substance abusers, delinquents, single parents, multi-problem households, marginal, asocial persons, and other social 'misfits'" (cited by Sen 2000).

The view taken by the British government is somehow different. It stresses the intergenerational dimension and the need for prevention in early years. "Social exclusion is about more than income poverty. Social exclusion happens when people or places suffer from a series of problems such as unemployment, discrimination, poor skills, low incomes, poor housing, high crime, ill health and family breakdown. When such problems combine they can create a vicious cycle. Social exclusion can happen as a result of problems that face one person in their life. But it can also start from birth. Being born into poverty or to parents with low skills still has a major influence on future life chances" (cited in Australian Government 2009).

The government of Sweden takes a much wider approach to the topic. "Social exclusion means that people or groups are excluded from various parts of society or have their access to them impeded. Social exclusion occurs in part through people not gaining access to key parts of social life such as the labor market (and culture, leisure activities, social relations politics and housing) and in part through a process in which people are gradually (attached) as a result of a social problem to several other subsequent problems. It is thus a social phenomenon which is more complex and dynamic than that covered by the term social problem, which often involves one problem at a time…" (cited in Australian Government 2009).

The concept of social exclusion and more generally social policy has also gained a key role in the EU political debate during the past 10 years or so. A list of primary and secondary indicators of social exclusion has been proposed (for more details, see, e.g., Atkinson et al. 2004; Verma et al. 2006; Marlier et al. 2007; Maquet, Chap. 2 of this book). But it seems that the list of indicators put forth by the Indicators Subgroup of the Social Protection Committee of the EU (Social Protection Committee, 2001) misses one of the important aspects of social exclusion. As stressed by Sen (2000), "the helpfulness of the social exclusion approach does not lie… in its conceptual newness, but in its practical influence in forcefully emphasizing—and focusing attention on—the role of relational features in deprivation." Sen (2000) recommends in fact making a distinction between the two ways in which social exclusion can lead to capability deprivation. "Being excluded can sometimes be in itself a deprivation, and this can be of intrinsic importance on its own. For example, not being able to relate to others and to take part in the life of the community can directly impoverish a person's life. It is a loss on its own, in addition to whatever further deprivation it may indirectly generate. This is a case of constitutive relevance of social exclusion. In contrast, there are relational depri-

vations that are not in themselves terrible, but which can lead to very bad results. For example, not using the credit market need not be seen by all to be intrinsically distasteful. Some do, of course, enjoy borrowing or lending, while others do not feel this to be a matter of inherent importance… But not to have access to the credit market can, through causal linkages, lead to other deprivations, such as income poverty, or the inability to take up interesting opportunities that might have been both fulfilling and enriching but which may require an initial investment and use of credit. Causally significant exclusions of this kind can have great instrumental importance: they may not be impoverishing in themselves, but they can lead to impoverishment of human life through their causal consequences (such as the denial of social and economic opportunities that would be helpful for the persons involved). Landlessness is similarly an instrumental deprivation…."

This is why, in trying to measure social exclusion in FYR Macedonia and its determinants, which is the goal of this chapter, we made sure to include also indicators that would take into account what Sen (2000) called "the role of relational features in deprivation" and which will appear in the empirical analysis under the more general heading of "social capital indicators."

For the purpose of this paper, in light of the way the concept has been debated in the literature and the data available, we identify five broad domains of social exclusion: employment, assets, living conditions, subjective well-being and social capital. How individuals fare in each of these domains defines their social exclusion status.

This chapter is organized as follows. In the first section we present succinctly some general features of the economic and social situation in FYR Macedonia and the data sources that have been used. In the following section we describe the methodological approach that has been adopted to analyze social exclusion. More precisely, we explain that in a first stage, we used a multivariate technique called correspondence analysis that allowed us to aggregate in one factor, separately for each domain of social exclusion, the variables that were available to characterize this domain. Then, in a second stage, we used an approach commonly used in productivity analysis which is called "efficiency analysis." The technique selected was that of stochastic production frontier, and it allowed us to derive a latent vector assumed to represent the level of overall social exclusion of each of the individuals in the survey. In the next section we tried to identify the determinants of social exclusion by regressing the latent variable assumed to describe social exclusion on a certain number of explanatory variables such as the level of education, the marital status, and the age.

The Case of FYR Macedonia

This chapter analyzes social exclusion in the Former Yugoslav Republic of Macedonia. The data we use are part of a set of surveys carried out by UNDP and UNICEF in November and December 2009. The purpose of the surveys was to study social exclusion in transitional economies, and the study covered six countries including Serbia, FYR Macedonia, Moldova, Ukraine, Kazakhstan, and Tajikistan. The surveys were

based on nationally representative samples and covered different domains including employment, access to assets, housing, standard of living and income sources, opportunities, health, education and social services, social capital and relations, participation in cultural and political life. The Macedonian survey covered 2,700 individuals and was a multistage sample survey representative at the national and regional level and based on the EU-NUTS 3 regional classification.[1]

FYR Macedonia should be an interesting case for studying social exclusion. When it was still part of the former Yugoslavia, FYR Macedonia was mostly a rural economy, the poorest of the republics, and the one with the highest unemployment rate. After the breakdown of Yugoslavia in 1991, FYR Macedonia was only marginally affected by conflict. Despite its isolation and poverty, growth in FYR Macedonia resumed already in 1996.

As for most other Balkan republics, the new millennium brought about some prosperity for FYR Macedonia with sustained growth rates only recently interrupted by the global financial crisis. This period has also been characterized by structural reforms in various domains although poverty and unemployment largely persisted. FYR Macedonia today is home of a Macedonian Slav majority which accounts for less than two-thirds of the population and of a large Albanian minority accounting for over a quarter of the population. The country avoided ethnic conflicts mostly through peaceful agreements between the two dominant groups. But the ethnic question remains to these days a heated topic in FYR Macedonia, and it is likely to have important implications for social exclusion.

The Methodological Approach

The First Stage: Correspondence Analysis

Correspondence analysis was introduced by Benzécri (1980) and his French school. It is an exploratory data analytic technique aiming at analyzing simple two-way (or multiway) tables where some measure of correspondence is assumed to exist between the rows and columns. Correspondence analysis is extremely useful to transform a set of complex data into simple descriptions of almost all the implicit information provided by the data.

A very useful characteristic of correspondence analysis is that it allows one to obtain a graphical display of row and column points in biplots, which helps discovering some structural relationships that may exist between the variables and the observations.[2]

Although correspondence analysis (CA) may be defined as a special case of principal components analysis (PCA) of the rows and columns of a table, one should

[1] More information on the surveys is available in the technical report prepared for the UNDP-UNICEF study and available at http://europeandcis.undp.org/poverty/show/F2C6CE22-F203-1EE9-B1766979C32D5CEA.

[2] See Appendix 2 for more details on this technique.

stress that CA and PCA have each specific uses. Principal components analysis is a useful tool when the variables are continuous, whereas correspondence analysis is typically applied to the case of contingency tables.

While the chi-square test is the usual procedure adopted for analyzing, in a cross-tabulation, the degree of association between rows and columns, this test does not identify which are the important individual associations between a specific pair of row and column. Correspondence analysis on the contrary indicates how the variables are related and not simply whether there is such a link.

Assume a contingency table that has I rows and J columns. The plot given by a correspondence analysis gives then a set of $(I+J)$ points, I points corresponding to the rows and J points to the columns. If two row points are close, one can then conclude that their conditional distributions across the columns are similar. Given the symmetry of the role played by lines and columns in correspondence analysis, we can also conclude that if two column points are close on the biplot provided by the correspondence analysis, it implies that their conditional distributions across the rows are similar. Like principal components analysis, correspondence analysis provides the researcher with principal components which are orthogonal. Each component is a linear combination of the variables on one hand, the observations on the other. The coefficients of these variables (observations) for the first two components give us in fact the coordinates that allow us to plot these variables (observations) in the graph previously mentioned.

In this application of CA to the analysis of social exclusion, we analyzed several indicators for each of the domains of exclusion: employment, assets, living standards, subjective well-being and social capital (Appendix 1 gives a list of the variables in included in each domain). The first factor in each domain was assumed to summarize the features of social exclusion in that domain and used in the second stage of the analysis.

The Second Stage of the Analysis: Using the Stochastic Production Frontier Approach to Determine the Individual Degree of Social Exclusion

On the basis of the "inputs" (first factor) derived by correspondence analysis in each domain of social exclusion, an efficiency analysis was then implemented and an "output" score (degree of social exclusion) attributed to each individual. The (first) factors derived separately from correspondence analysis for each domain were considered as the inputs in the production of a latent variable reflecting the overall degree of social exclusion of the individual. Such a latent variable is evidently not observed, and to implement a stochastic production frontier analysis, we used a technique originally proposed by Lovell et al. (1994) and later adopted by Deutsch and Silber (1999), Deutsch et al. (2003), and Ramos and Silber (2005).

Let $x = (x_1, \ldots, x_k)$ denote the vector of the k aggregated "inputs" (first factors) derived from correspondence analysis for each of the k domains. Lovell et al.'s

approach (see Appendix 3 for more details) amounts to estimating a translog input distance function expressed as

$$\ln(1/x_M) = a_0 + \sum_{j \neq M}^{k} a_j \ln x_j + (1/2) \sum_{j \neq M}^{k} \sum_{h \neq M}^{k} a_{jh} \ln x_j \ln x_h + \varepsilon$$

where the subindex M refers to one of the domains of social exclusion previously defined (see Lovell et al. 1994 for more details on the procedure).

Note that the value of the (first) factors derived from correspondence analysis for the various domains was negative for some of the individuals. In order to be able to use a translog production function, we transformed these inputs as follows:

$$x'_{ji} = \frac{[x_j - Min\{x_{j1}, \ldots, x_{jI}\}]}{[Max\{x_{j1}, \ldots, x_{jI}\} - Min\{x_{j1}, \ldots, x_{jI}\}]}$$

where x_{ji} is the value of input $j(j = 1 \text{to} k)$ for individual $i(i = 1 \text{to} I)$ and x'_{ji} is the value of the "transformed input."

The technique of corrected ordinary least squares (COLS) is then used to obtain estimates of the various coefficients (see Appendix 3 for more details on the COLS technique). The modified residuals which are then derived provide input distance functions for each individual by means of the transformation

$$d_i = e^{[(\text{max}imum\ negative\ residual) - (residual\ \ for\ individual\ i)]}$$

This distance will by definition be greater than one so that all individual input vectors lie on or beyond the isoquant (frontier).

This input distance function will in fact measure the extent of social exclusion for individual i. More precisely, the further outside the isoquant the point corresponding to the degree of social exclusion of individual i in the various domains is, the more it must be radially contracted in order to reach the isoquant.

Explaining Social Exclusion

As illustrated above we considered social exclusion as a latent factor quantified by means of a multistep process that involved correspondence and efficiency analyses. The process that led to the quantification of our social exclusion variable used a set of variables that we judged to be proxies of the latent concept of social exclusion and finally delivered a social exclusion variable that we can now use as dependent variable in a regression.

Given the individual degree d_i of social exclusion, we can then estimate the following OLS regression:

$$d_i = \alpha + z_i \beta + u_i$$

where z_i is a vector of determinants of individual social exclusion and u_i is the normally distributed error term.[3] We aim at identifying explanatory factors among those variables that have not been used in the correspondence and efficiency analyses. Evidently, this particular methodology relies on both normative and positive criteria and restricts the possible predictors of social exclusion. As a result, the final sample and the range of variables used in the regression were reduced vis-à-vis the original sample and range of variables. The final set of variables includes personal characteristics (marital status, age, and education), ethnic group (Slavic, Albanian, and others), characteristics of the settlement (population size and type of settlement), characteristics of the dwelling (house size and type of property), type of settlement (small town, regional economic center, and capital), and regional fixed effects.

Results are presented in Table 7.1. The explanatory power of the regression is not very high with an R^2 of 0.14. However, we found 13 out 19 predictors to be significant and some interesting insights in what social exclusion in FYR Macedonia is about.

In terms of personal characteristics, it appears that being married reduces the likelihood of social exclusion. This relation is significant at the 10% level only but seems consistent, for example, with the happiness literature that shows married people to be happier on average. Several factors explain higher happiness in married people (Stutzer and Frey 2006), but marriage typically expands the network of social relations, and social relations are known in the happiness literature to be a major ingredient of subjective well-being. In FYR Macedonia, which is a very conservative society as compared with other Balkan countries, this may be particularly true, and marriage may be a relevant step toward better social integration.

In terms of ethnic minorities, we analyzed separately the Albanian from the Turkish, Roma, and Egyptian minorities and used the Slavic populations (mostly Macedonians) as base category.[4] We found that the Albanian minority is not socially excluded when compared to the Slavic population. The Albanian minority in FYR Macedonia has made substantial gains in social terms in recent years, and social exclusion does not measure wealth or income but the degree of integration in the local community. Also, the Albanian community in FYR Macedonia is typically concentrated in a few cities and regions and the regression controls for type of settlement and for regions.

Instead, the Turkish, Roma, and Egyptian minorities together appear to be the most socially excluded groups, and this relation is significant at the 1% level. This is expected, given that these groups tend to live in urban peripheries and in poorer areas and given

[3] Note that our dependent variable varies between zero and one and could not be conveniently transformed into logs. However, the distribution of the dependent variable fits a normal shape and the prerequisites for OLS estimations. This also simplifies the interpretation of the coefficients.

[4] Note that the Turkish, Roma, and Egyptian minorities were bundled together simply for a question of sample size.

Table 7.1 Regression results with dependent variable: social exclusion

Var.	Coef.	Std. err.	*t*-value
Married	–0.00905**	0.0038519	–2.35
Female	–0.00282	0.0029533	–0.96
Age	0.000832	0.0007967	1.04
Age^2	–9.92E-06	9.20E-06	–1.08
Low education (≤12years)	0.00561*	0.0031323	1.79
Albanians	0.00371	0.0050066	0.74
Turkish, Roma, or Egyptians	0.0419***	1.05E-02	3.99
Size of accommodation	–4.25E-07	1.50E-06	–0.28
Property is barrack or slum	0.0409***	0.0102268	4
Population ≤30,000 inhabitants	–0.0104***	0.004022	–2.58
Small town (1)	–0.0264***	0.004731	–5.58
Regional/economic center (1)	–0.0368***	0.0054856	–6.71
Capital (1)	–0.0450***	0.006768	–6.65
Pelagonia (2)	–0.0244***	0.0071889	–3.39
Southeast (2)	–0.00710	0.006814	–1.04
Southwest (2)	–0.0308***	0.0075702	–4.07
Polog (2)	–0.0177**	0.0075885	–2.33
East (2)	–0.0236***	0.0071644	–3.29
Vardar (2)	–0.0271***	0.007297	–3.72
Northeast (2)	–0.00210	0.0078395	–0.27
Constant	0.224***	0.0168194	13.29

Number of observations: 1,092; R^2: 0.14; Base categories: (1) Village; (2) Skopje
Significance levels: *$p<0.1$, **$p<0.05$, ***$p<0.01$

that their small numbers make them minorities also in small territorial areas such as small cities and villages. This is not the case for the Albanian minority, which is a minority at the national level but a majority in several urban and rural centers.

The type of property (barrack or slum as opposed to better types of properties) is an important factor associated with social exclusion. This factor may signal poverty and may also proxy various other elements associated with poverty such as low income and low access to services. Perhaps the appearance of the property stigmatizes their inhabitants, and this contributes to social exclusion. This may be particularly true for minorities such as Roma people, which are sizeable in FYR Macedonia and may live in temporary shelters.

Interestingly, in FYR Macedonia, people living in small places with less than 30,000 inhabitants suffer less from social exclusion. As compared to rural villages, we observe that people living in small towns, in regional or economic centers, or in the capital city are less socially excluded. We can also observe substantial differences across regions in terms of social exclusion, and it seems that all regions do better than the capital. In substance, small and medium urban centers are the better places to live in FYR Macedonia in terms of social exclusion. This is a very interesting result and one that confirms that social exclusion is not just about GDP per capita but is about interaction with others, access to services, and social networks.

What these results also show is that social exclusion is a relative concept and one that is affected by the degree of homogeneity of communities. It is natural to find

that social exclusion is larger in large and urban centers where more social strata and ethnic groups live together and where the probability of between-groups exclusion increases. The drawback of this finding—in a country like FYR Macedonia where the Slavic and non-Slavic communities tend to live apart geographically—is that the gains in *within* community cohesion may be achieved at the expenses of *between* community cohesion. This is an important consideration for social stability at the national level. By encouraging different communities to mix at the local level, the social planner may sacrifice short-term social cohesion at the local level but may also build long-term social cohesion at the national level. This seems an important trade-off for a country like FYR Macedonia and points to the fact that social exclusion must be considered in the specific context in which is measured.

Appendix 1. List of Variables Used

1. Various domains of social exclusion which have been distinguished and to which correspondence analysis was applied (list of variables used in each domain and number of the question in the original UNDP questionnaire):
   First domain: Employment
   First variable:

- During the last month, have you worked for payment (in cash or in kind) or for any other income at least for 1 day? (question 4)
- If you do not work, what is the main reason why you did not look for work:
  - Have a temporary/occasional work
  - Got tired of searching, thought no work available
  - Unable to work due to long-term illness or disability (question 8)

  Second variable:

- During the last month, have you worked for payment (in cash or in kind) or for any other income at least for 1 day? (question 4)
- If "no job," are you registered with the employment services in any capacity?
  - Yes, as a person looking for work
  - Yes, in another capacity
  - No (question 5)
- If "no job," have you made any efforts within the past 4 weeks to find work or established a business or enterprise? Yes or no. (question 7)

  Second domain: Assets

- *First variable*: Do you have a bank account (including a credit card and saving deposit) registered under your own name? (question 33)
- *Second variable*: Does your household own land? (question 37)

- *Third variable*: Does your accommodation in which you live have running water? (question 43)
- *Fourth variable*: Does your accommodation in which you live have flushing indoor toilet? (question 43)
- *Fifth variable*: Does your accommodation in which you live have central heating or a local heating system? (question 43)
- *Sixth variable*: Does your accommodation in which you live have electricity supply? (question 43)
- *Seventh variable*: Does your accommodation in which you live have sewage system? (question 43)
- *Eighth variable*: Does your accommodation in which you live have central gas supply? (question 43)

Third Domain: Living Standards

1. *Eleven following variables*: There are some things that many people cannot afford. For each of the following items on the card, can I just check how often your household could afford it in the past 12 months? The possible answers are never, seldom, sometimes, often. (question 46)

   - Buying food for three meals a day
   - Paying regularly the bills
   - Keeping your home adequately warm
   - Buying new clothes and shoes that you or your household needed
   - Buying medication that you or your household needed
   - Regular dental checks for every child in your household
   - Buying school materials/books for every child in your household
   - Having friends or family for a drink or meal at least once a month
   - Paying for a week's annual holiday away from home/abroad
   - Traveling to family celebrations/for family events
   - Buying books, cinema or theater tickets

2. *Twenty following variables*: Could you tell me whether your household has it, your household does not have it because you cannot afford it, or your household does not have it because you do not need it? (question 47)

   - Television
   - Computer
   - Internet
   - Cellular phone
   - Satellite/cable TV
   - Car (not motorcycle)
   - Washing machine
   - Freezer/refrigerator
   - Landline telephone
   - Radio receiver
   - Gas oven
   - Electric oven

- Generator
- Electric iron
- Outdoor metal stove

- Electric sewing/knitting machine
- Electric room heater
- Kerosene lamp

- Microwave oven
- Bed for each household member
- Living room furniture
- Vacuum cleaner

Fourth domain: Subjective well-being

1. *Thirteen following variables*: There are many situations that could negatively affect you or your household. Please tell me how worried you are about each of the following situations, assessing each type from 1 to 5 ("1" not worried at all and "5" very worried) (question 62)

   - Lack of sufficient incomes
   - Hunger
   - Denied access to health-care practitioners

     - Lack of housing (eviction)
     - Poor sanitation-related diseases
     - Street crime

   - Denied opportunity to practice your religion
   - Organized crime (e.g., racketeering you business)
   - Local religious conflicts (conflicts between different religious groups)
   - Local interethnic conflicts (conflicts between different ethnic groups)

     - Corruption of officials
     - Pollution

   - Global warming

   Fifth domain: Social capital

   - *First variable*: In your country, parents and children usually help each other. How is it in your family? Parents rather support the children or everyone takes care of themselves or children rather support the parents (question 87)
   - *Second variable*: Can you tell me about your close friends? These are people whom you trust, can talk to about private matters, or call on for help. With respect to close friendship, would you say that you do have close friends or you do not have any close friends, only acquaintances? (question 91)
   - *Third variable*: How often (never, seldom, a few times each month, a few times a week, almost every day) do you spend your free time with

     - Family/relatives

  - Neighbors
  - Your friends (question 93)

- *Fourth variable:* Generally speaking, do you think most people can be trusted? (question 95)
- *Fifth variable*: Have you attended any cultural event (theater, museums, concert, etc.) in the last 3 months? (question 98)

2. List of explanatory variables used as explanatory variables in regression analysis where the dependent variable is the individual degree of social exclusion obtained after applying the stochastic production frontier technique

Variable	Question
Level of education	Question 77
Ethnic group	Question 104
Type of settlement (village, small town, regional/economic center, capital)	Question 128
Age	General questions about household
Square of age	General questions about household
Region of residence	General questions about household
Marital status (married or not)	General questions about household
Gender	General questions about household
Size of accommodation	General questions about household
Property is barrack or slum	General questions about household

Appendix 2. On Correspondence Analysis

Correspondence analysis (CA) was originally introduced by Benzécri and Benzécri (1980). It is strongly related to principal components analysis (PCA), but while PCA assumes that the variables are quantitative, CA has been designed to deal with categorical variables. More precisely, CA offers a multidimensional representation of the association between the row and column categories of a two-way contingency table. In short, the goal of CA is to find scores for both the row and column categories on a small number of dimensions (axes) that will account for the greatest proportion of the χ^2 measuring the association between the row and column categories. There is thus a clear parallelism between CA and PCA, the main difference being that PCA[5] accounts for the maximum *variance*. A clear presentation of CA is given in Asselin and Vu Tuan Anh (2008) and Chap. 5 in Kakwani and Silber (2008).

Let us first recall what the main features of PCA. It is in fact a data reduction technique that consists of building a sequence of orthogonal and normalized linear combinations of the K primary indicators that will exhaust the variability of the set

[5] For an illustration of the use of PCA, see, for example, Berrebi and Silber (1981).

primary indicators. These orthogonal linear combinations are evidently latent variables and usually called "components." In PCA, the first component has the greatest variance, and all subsequent components have decreasing variances.

Let N be the size of the population, K the number of indicators I_k. The first component F^1 may be expressed for observation i as

$$F_i^1 = \sum_{k=1}^{K} \omega_k^1 I_i^{*k}$$

where I^{*k} refers to the standardized primary indicator I^k. Note that ω_k^1 is the (first) factor score coefficient for indicator k. It turns out that the scores ω_k^1 are in fact the multiple regression coefficients between the component F^1 and the standardized primary indicators I^{*k}. It is very important to understand that PCA has some limitations, of which the most important is probably the fact that PCA has been developed for *quantitative* variables.

It is therefore better not to use PCA when some of the variables are of a qualitative nature. Multiple correspondence analysis (MCA) is in fact the data reduction technique that should be used in the presence of categorical variables.

Let us therefore assume now that the K primary indicators are categorical ordinal and that the indicator I^k has J^k categories. Note that if some of the variables of interest are quantitative, it is always possible to transform them into a finite number of categories. To each primary indicator I^k, we therefore associate the set of J^k binary variables that can only take the value 0 or 1.

Let us now call $X(N,J)$ the matrix corresponding to the N observations on the K indicators which are now decomposed into J^k variables. Note that $J = \sum_{k=1}^{K} J^k$ represents now the total number of categories. Call N_j the absolute frequency of category j. Clearly N_j is equal to the sum of column j of the matrix X. Let $N_{..}$ refer to the sum of all the $(N \text{ by } K)$ elements of the matrix X. Let also f_j be the relative frequency $(N_j / N_{..})$, f^i be the sum of the ith line of matrix X, f_{ij} be the value of cell (i, j), and f_j^i be equal to the ratio (f_{ij} / f^i). Finally, call $\{f_j^i\}$ the set of all f_j^i's for a given observation i (j=1 to J). This set will be called the profile of observation i.

As stressed previously, CA is a PCA process applied to the matrix X but with the χ^2-metric on row/column profiles, instead of the usual Euclidean metric. This χ^2-metric is in fact a special case of the Mahalanobis distance developed in the 1930s. This metric defines the distance $d^2(f_j^i, f_j^{i'})$ between two profiles i and i' as

$$d^2(f_j^i, f_j^{i'}) = \sum_{j=1}^{J} (1 / f_j)(f_j^i - f_j^{i'})^2$$

Note that the only difference with the Euclidean metric lies in the term $(1 / f_j)$. This term indicates that categories which have a low frequency will receive a higher

weight in the computation of distance. As a consequence, CA will be overweighting the smaller categories within each primary indicator. It can be shown that

$$\omega_j^{1,k} = \frac{1}{(N_j^k / N)} Cov(F^{1*}, I_j^k)$$

where $\omega_j^{1,k}$ is the score of category j_k on the first (non-normalized) factorial axis, I_j^k is a binary variable taking the value 1 when the population unit belongs to the category j_k, F^{1*} is the normalized score on the first axis, and N_j^k is the frequency of the category j_k of indicator k.

It is also very interesting to note that CA offers a unique duality property since it can be shown that

$$F_1^i = \frac{\sum_{k=1}^{K} \sum_{j=1}^{J_k} \frac{w_j^{1,k}}{\lambda_1} I_{i,j}^k}{K}$$

where K is the number of categorical indicators, J_k is the number of categories for indicator k, $w_j^{1,k}$ is the score of category j_k on the first (non-normalized) factorial axis, $I_{i,j}^k$ is a binary variable taking the value 1 when unit i belongs to category j_k, and F_1^i is the (non-normalized) score of observation i on the first factorial axis.[6]

Reciprocally it can be shown that

$$\omega_j^{1,k} = \frac{\sum_{i=1}^{N} \frac{F_1^i}{\lambda_1}}{N_j^k}$$

This duality relationship implies thus that the score of a population unit on the first factor is equal to the average of the standardized factorial weights of the K categories to which it belongs. Conversely the weight of a given category is equal to the average of the standardized scores of the population units belonging to the corresponding category.

[6] Very similar results can be derived for the other factorial axes.

Appendix 3. On Frontier Efficiency Measurement

Duality and the Concept of Input Distance Function in Production Theory

Let $x_i = (x_{1i},\ldots,x_{ji},\ldots,x_{ki})$ denote the vector of levels of social exclusion in the various k domains of social exclusion for individual i and let y_i denote the overall level of social exclusion for individual i. An individual's performance, as far as social exclusion is concerned, may hence be represented by the pair (x_i, y_i), $i = 1, \ldots I$.

A theoretical social exclusion index SE can then be estimated using a Malmquist input quantity index:

$$SE(y, x^s, x^t) = D_{input}(y, x^s) / D_{input}(y, x^t)$$

where x^s and x^t are two different "social exclusion input" vectors and D_{input} is an input distance function. The idea behind the Malmquist index is to provide a reference set against which to judge the relative magnitudes of the two vectors of "social exclusion inputs." That reference set is the isoquant $L(y)$ and the radially farther x_i is from $L(y)$, the higher the overall level of social exclusion of individual i is, for x_i must be shrunk more to move back onto the reference set $L(y)$.

There is, however, a difficulty because the Malmquist index depends generally on y. One could use an approximation of this index such as the Tornqvist index, but such an index requires price vectors as well as behavioral assumptions.[7] Since we do not have prices for the "social exclusion inputs," we have to adopt an alternative strategy. The idea is to get rid of y by treating all individuals equally and assume that each individual has the same overall level of social exclusion: one unit for each "social exclusion input." Let e represent such a vector of "social exclusion inputs"—a k-dimensional vector of ones. Thus, the reference set becomes $L(e)$ and bounds the vectors of "social exclusion inputs" from below. Individuals with "social exclusion vectors" onto $L(e)$ share in fact the lowest level of "overall social exclusion," with an index value of unity, whereas individuals with large vectors of "social exclusion inputs" will then have higher overall level of social exclusions, with index values above unity.

To estimate the distance function, let $\lambda = (1 / x_k)$ and define a $(k-1)$-dimensional vector z as $z = \{z_j\} = (x_j / x_k)$ with $j = 1,\ldots,k-1$. Then $D_{input}(z, e) = (1 / x_k) D_{input}(x, e)$, and since $D_{\text{input}}(x, e) \leq 1$, we have

$$(1 / x_k) \leq D_{input}(z, e)$$

[7] This is also the case of other indices that are usually used to approximate the Malmquist index such as the Paasche index, the Laspeyres index, or the Fisher index.

This implies that we may also write

$$(1/x_k) = D_{input}(z,e)\exp(\varepsilon), \quad \varepsilon \leq 0$$

By assuming that $D_{input}(z,e)$ has a translog functional form, we have

$$\ln(1/x_k) = \alpha_0 + \sum_{j=1}^{k-1}\alpha_j \ln z_j + (1/2)\sum_{j=1}^{k-1}\sum_{h=1}^{k-1}\alpha_{jh}\ln z_j \ln z_h + \varepsilon$$

Estimates of the coefficients α_j and α_{jh} may be obtained using corrected ordinary least squares (COLS) or maximum-likelihood methods (see below) while the input distance function $D_{input}(z_i,e)$ for each individual i is provided by the transformation

$$D_{input}(z_i,e) = \exp\{\max(\varepsilon_i) - \varepsilon_i\}.$$

This distance will, by definition, be greater than or equal to one (since its logarithm will be positive) and will hence indicate by how much an individual "social exclusion input vector" must be scaled back in order to reach the "social exclusion inputs" frontier. This procedure guarantees therefore that all "social exclusion input vectors" lie on or above the resource frontier $L(e)$. The overall level of social exclusion for individual *i* will then be obtained by dividing $D_{input}(z_i,e)$ by the minimum observed distance value—which by definition equals 1.

Estimation Procedures: The Stochastic Production Frontier Approach

Let us take as a simple illustration the case of a Cobb–Douglas production function. Let $\ln y_i$ be the logarithm of the output of firm $i(i = 1\text{to}N)$ and x_i a $(k+1)$ row vector, whose first element is equal to one and the others are the logarithms of the k inputs used by the firm. We may then write that

$$\ln(y_i) = x_i\beta - u_i \quad i = 1\text{to}N$$

where β is a $(k+1)$ column vector of parameters to be estimated and u_i a nonnegative random variable, representing the technical inefficiency in production of firm i.

The ratio of the observed output of firm i to its potential output will then give a measure of its technical efficiency TE_i so that

$$\text{TE}_i = y_i / \exp(x_i\beta) = \exp(x_i\beta - u_i)/\exp(x_i\beta) = \exp(-u_i)$$

One of the methods allowing the estimation of this output-oriented Farrell measure of technical efficiency TE_i (see Farrell 1957) is to use an algorithm proposed by Richmond (1974) which has become known as corrected ordinary least squares (COLS). This method starts by using ordinary least squares to derive the (unbiased) estimators of the slope parameters. Then in a second stage, the (negatively biased) OLS estimator of the intercept parameter β_0 is adjusted up by the value of the greatest negative residual so that the new residuals have all become nonnegative. Naturally the mean of the observations does not lie any more on the estimated function: the latter has become in fact an upward bound to the observations.

One of the main criticisms of the COLS method is that it ignores the possible influence of measurement errors and other sources of noise. All the deviations from the frontier have been assumed to be a consequence of technical inefficiency. Aigner et al. (1977) and Meeusen and van den Broeck (1977) independently suggested an alternative approach called the stochastic production frontier method in which an additional random error v_i is added to the nonnegative random variable u_i. We therefore write

$$\ln(y_i) = x_i\beta + v_i - u_i$$

The random error v_i is supposed to take into account factors such as the weather and the luck, and it is assumed that the v_i's are i.i.d. normal random variables with mean zero and constant variance σ_v^2. These v_i's are also assumed to be independent of the u_i's, the latter being taken generally to be i.i.d. exponential or half-normal random variables. For more details on this maximum-likelihood estimation procedure, see Battese and Corra (1977) and Coelli et al. (1998), as well as programs such as FRONTIER (Coelli 1992) or LIMDEP (Green 1992). The same methods (COLS and maximum likelihood) may naturally be also applied when estimating distance functions.

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Chapter 8
Subjective Well-Being, Activation Policies, and the Inclusion Agenda

Marina Petrovic

Introduction

There are several philosophical approaches to determining and individual's quality of life. For example, normative ideals drawn from religious or philosophical systems (Diener and Suh 1997) can determine the characteristics of a good life. The approach dominant in economic thinking is based on utility and satisfaction of preferences. A different approach, rooted in behavioral science, defines quality of life in terms of people's experience of their subjective well-being (SWB). One of the major rationales for studying SWB is the belief that it has important implications both for people's lives and for public policy.

SWB refers to people's assessments of their lives and includes measures of both cognition and affect. Perceptions of well-being appear to be more complex than what is captured by objective indicators identified in relation to a societal context (Diener and Suh 1997). For example, forced unemployment can be seen as negative for society, and labor market indicators will capture its extent in a given context. In contrast, from a subjective well-being perspective, it would be important to know whether and how individuals' life satisfaction is affected by unemployment.

There is a considerable amount of work on the topic of subjective well-being in psychology and economic science (see Diener 1984; Diener et al. 1997; Frey and Stutzer 1999, 2002; Layard 2006; Van Praag and Ferrer 2004; Veenhoven 1991, 2000, 2004). Yet, despite an extensive literature on poor people's perceptions of poverty, particularly in low-income countries (e.g., the comprehensive Voices of the Poor study by Narayan et al. (2000)), the subjective well-being of the poor and socially excluded has been largely absent in debates over poverty and social exclusion in the European context.

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This study starts bridging this gap by focusing on the perceptions of able-bodied working-age social assistance beneficiaries about the effects of their public work engagement. In Serbia, public work employment has officially been defined as an active labor market measure with the aim of increasing the level of employability and chances for employment of "hard-to-employ" categories of people registered by the employment agency. By default, social assistance recipients belong to the "hard-to-employ" population.

The evidence in our study is complementary to a broader survey of social assistance recipients, conducted in Serbia as a baseline against which to judge the impact of a new law on social assistance (Petrovic 2011). In addition, the analysis of the SWB impacts of public work participation for social assistance recipients contributes to an understanding of the links between the welfare system and the labor market in Serbia. Those are of broader interest given the centrality of the activation agenda (the set of measures aimed at supporting the transition to from inactivity to work, particularly for social assistance recipients) in European thinking on inclusion as exemplified by the "workless households" indicator in the Europe 2020 target (see Chapter 2).

The findings of this study indicate that work experience is beneficial for the participants even if it does not lead to their immediate employment. Our evidence suggests that engagement in the public works program increases the participants' employability as indicated by the level of "qualifications and skills" and "chances for employment." It also reduces the mental cost of being unemployed and increases the participants' "self-confidence" and their "social contacts." Together, these findings are important for understanding the role of activation in the social inclusion agenda.

This chapter is structured as follows. We first place the overall discussion in the context of work engagement of social assistance recipients through public works program in Serbia. In the next section, we discuss different approaches to measuring subjective well-being of the unemployed poor. We further analyze SWB outcomes relating to public work activation in order to understand specific conditions that impact on recipients' better integration in the labor market and society in general. This is covered in the sections discussing the linkages between SWB, employability, and social inclusion. Finally, we offer the summary presentation of findings on overall subjective well-being of social assistance recipients who took part in public works.

Public Works in Serbia

The public works program is a rather new government-run program targeted at "hard-to-employ" categories of the unemployed and aimed at increasing their employability and employment. The program was introduced in 2006. Since then it has provided temporary employment and low pay to around 5,000 individuals yearly. Participants are the neediest unemployed and primarily unskilled workers. The program is mostly self-targeted, but it has a categorical component aimed at poor representatives of the Roma minority to facilitate their social inclusion. The

pay rate was set at the level of the minimum wage.[1] The program also entailed a learning component in the form of off- and on-the-job training. The training and work components combined lasted between 6 and 12 months.

In addition to providing employment, public works programs have additional objectives. These include increasing participants' competitiveness in the labor market, gaining additional knowledge and skills, and mitigating negative consequences of participants' socioeconomic status. The objectives which are officially adopted by the government aim to increase the "employability" of beneficiaries.

In 2008, the year to which this analysis refers, 263 projects were approved by the government, providing employment for 5,315 individuals (Vlada Republike Srbije 2009). Project activities covered three broad areas: social, humanitarian, and cultural activities; public infrastructure; and environmental protection. A total of 650 million dinars or 0.02% of GDP was allocated by the government for these activities. The overall expenditure on active labor market programs, of which public works were only a small part, comprised only 0.1% of GDP.

Public works are targeted to various disadvantaged groups, such as the Roma, refugees, the youth, the disabled, women, persons older than 50, the long-term unemployed, and social assistance beneficiaries.[2] The employment related benefits of this program appear to be limited. A study analyzing the impact of this program estimated that only 1.4% of all the participants were employed 6 months after the termination of the program (Arandarenko and Krstić 2008).

This analysis focuses on social assistance beneficiaries given their perceived limited prospects in the labor market. While there is a new policy shift toward labor activation for this group (Matkovic 2009), efforts in this direction are still limited. Other challenges that this group faces–such as the need to find employment for three months a year as benefit receipt is limited to nine months–contribute to make the analysis of this group very policy relevant.[3]

Measuring Subjective Well-Being of Deprived Groups

The literature presents two broad approaches to the analysis of subjective well-being. One focuses on summary measures of well-being, generally captured by single-item or multiple-item questions in surveys. Single-item questions on life satisfaction or happiness are usually framed as the following: "Taking things all together, how

[1] The wage was 15% higher for those with completed high school and 30% and 45% higher for college and university degree holders, respectively.

[2] In this study, social assistance benefit refers to the financial social assistance—"materijalno obezbedjenje" or "novcana socijalna pomoc" (term used since April 2011)—run by the government of Serbia. The financial social assistance is the main guaranteed minimum income program in the country, and it is aimed at individuals and households with an income below the minimum social welfare threshold. As such, social assistance fills the gap between the household's income and the established threshold.

[3] In 2008, the public works program was the only official program involving the activation of social assistance beneficiaries (see Petrovic 2009).

satisfied/happy are you with your life these days?" Individual satisfaction may also be captured by multiple-item questions. Box 8.1 shows examples of questions used in both types of approaches. Usually, respondents are asked to grade the level of their satisfaction/happiness on a scale, for example, from 1 to 5 or 1 to 7 (Diener et al. 1997; Bonin and Rinne 2006).

As an alternative, different domains over which SWB is defined are identified and are analyzed separately. Cummins (1996) surveyed theoretical and empirical literature on the quality of life to identify the relevant domains for an analysis of the general population.[4] The seven domains identified include material well-being, health, productivity, intimacy/friendship, emotional well-being, safety, and community. In his approach, questions relating to subjective well-being would usually ask how satisfied one person is with a "*domain*."

In this chapter, we follow this approach as it appears to be the most useful in providing policy relevant information on the performance of a specific program, though we tailor it to a specific group of respondents. The literature offers limited examples of SWB analysis for subgroups of the population. A notable exception is a study by Bonin and Rinne (2006), focusing on SWB of disadvantaged groups. They evaluated the effects of a specific active labor market program based on their impact on measures of subjective well-being of the beneficiaries.[5] Building on the Frey and Stutzer's (2002) discussion of items of personal happiness and the psychic and social cost associated with unemployment, Bonin and Rinne (2006) developed a set of domain measures for assessing subjective well-being outcomes including family income situation, health status, personal qualifications and skills, desire to find a job, chances to find a regular job, social contacts, and self-confidence. The responses in the Bonin and Rinne's (2006) study were captured in a survey.

The analysis presented in this study uses a variant of Bonin and Rinne's (2006) approach which has already been applied in Serbia. However, we implement it through qualitative tools, specifically in-depth interviews, rather than surveys.

While survey analysis is the most frequent method of measuring SWB in this case as there were no survey data available and it was not possible to carry out an ad hoc survey due to budget and time constraints. Instead, the respondents' judgments were captured in face-to-face interviews. We wanted to distinguish individual perceptions about changes in their lives. For this reason, we opted for in-depth interviews rather than focus groups. As stated in Chapter 4, the focus group format would add little over face-to-face interviews if not all the participants would actively

[4] Cummins identified 1,500 articles relating to "quality of life" and subsequently developed five criteria for the inclusion of the data on quality of life for the study. The selected 32 studies yielded 173 names of "domains" for the indicators of "quality of life." Finally, each of the named domains was classified into one of his seven domain categories for the general population.

[5] The program under evaluation was Beautiful Serbia program—an ad hoc operation supported by the government of Serbia and donors which provided training and temporary employment to disadvantaged population.

Box 8.1 Examples of questions related to life satisfaction or happiness

The University of Michigan's Survey Research Center (SRC) and the National Opinion Research Center (NORC):
Taken all together, how would you say things are these days—would you say that you are very happy, pretty happy, or not too happy?
The World Values Survey:
Taken all together, how happy would you say you are: very happy, quite happy, not very happy, not at all happy?
Eurobarometer Survey:
On the whole are you very satisfied, fairly satisfied, not very satisfied, or not at all satisfied with the life you lead?
Satisfaction with Life Scale (introduced by Ed Diener et al. (1997); answers rated on a scale 1–7 from "strongly agree" to "strongly disagree"):

1. *In most ways my life is close to ideal.*
2. *The conditions of my life are excellent.*
3. *I am satisfied with my life.*
4. *So far I have gotten the important things I want in life.*
5. *If I could live my life over, I would change almost nothing.*

Bonin and Rinne's (2006) assessment of the Beautiful Serbia program—survey respondents were requested to provide a self-assessment of changes concerning:

1. *Self-confidence*
2. *The desire to find a job*
3. *Social contacts*
4. *Health status*
5. *The family income situation*
6. *Personal qualifications and skills*
7. *The chances to find a regular job*

Answers were rated on a scale: *strongly improved, somewhat improved, stayed more or less the same, somewhat deteriorated, and strongly deteriorated.*

engage in the discussion. We found that social assistance recipients would not feel comfortable talking openly in a group about their family or income situations, nor they would be free to express their feelings in a group setting.

Data and Method

Data for this study come from qualitative analysis of semi-structured in-depth interviews with social assistance recipients and other disadvantaged people who participated in two separate public work projects in 2008. In total, 26 interviews were

conducted. This analysis is part of a broader qualitative study on the experiences of social assistance recipients with work engagement through public works.[6]

In order to focus and streamline the data-gathering process, the study drew on prestructured qualitative data collection and analysis. The research questions were specified prior to the field work. The case outline, including the conceptual framework and a defined set of specific questions with regard to subjective well-being dimensions, had been developed and included in the in-depth interview guide before any data were collected. A purposive sample was applied in the selection process. In line with Berg's (1989) reasoning, this strategy required special knowledge and expertise about a certain group under investigation. Since time for the data collection was limited, advanced planning for respondents' selection and within-case sampling was necessary. Access to public work program participants was ensured through the official government registry.

To ensure territorial diversity but also diversity in types of public work activities performed, the interviews were carried out in two towns: Ada (Vojvodina province) and Kragujevac (Central Serbia). In both towns, public work activities were planned and implemented in close cooperation with local authorities, public firms, and non-governmental organizations. The public work activities in Ada included mainly infrastructure and environment protection projects. The activities in Kragujevac focused more on provision of social services, namely, the types of care provision that could be performed in the homes of service beneficiaries—the so-called home care assistance services.

In total, 26 in-depth interviews were conducted—20 with social assistance recipients and 6 with non-recipient participants. There were 15 women and 11 men among the respondents from different backgrounds: urban, semi-urban, rural, and independent Roma settlements. The age ranged from 18 to 60 years. Most of the interviewees (16) completed only primary education while two young non-recipients had a university degree. An additional requirement of the approach was to ensure the right balance between people receiving social assistance for longer periods of time and those who were newer recipients.

The interviews were conducted face to face during February 2009. This meant that for some respondents, they took place shortly after the completion of the work engagement in public works. In all the cases, the timing of the interview corresponded to the period of 1–6 months from the completion of their work. Interviews took place in the offices of the public work implementation agency and lasted 50 minutes on average. All the interview participants were provided with detailed information about the study and the type of interview they were participating in. The interviews were recorded and confidentiality was guaranteed.

Information processing also followed a structured process. Raw field notes were coded without being previously transcribed. Notes were subsequently transformed into write-ups. The missing information, unclear data, and quotes were added by using the transcribed text. The data were entered directly in the earlier designed concept note by using the word processor and writing accompanying analytic text.

[6] See Petrovic (2009).

The conclusions drawn from the data were compared with those of Bonin and Rinne (2006) in which the same dimensions of subjective well-being were explored using the survey data.

The questions in the interviews were aimed at gaining insights in the participants' overall experiences with public works and covered three broad categories: beneficiaries' experiences with different types of assistance and support received, the experience of direct participation in public works, and experience with social services in general. While this qualitative approach entailed a broader set of questions related to overall experiences with public works, the analysis in this chapter focuses only on findings with respect to the impact of work engagement on social assistance beneficiaries and their subjective well-being outcomes.

The primary interest of our study was to obtain responses to the questions concerning particular dimensions of life that provide insights into how the respondents' personal situations had changed over time. The respondents were asked to compare their situation at the time of the interview with that before the public works program came into effect. The interviews entailed a self-assessment of changes concerning family income situation, health status, personal qualifications and skills, desire to find a job, chances to find a regular job, social contacts, and self-confidence. These items have already been identified in the literature as determinants of personal happiness (Frey and Stutzer 2002; Bonin and Rinne 2006). The analysis in this chapter summarizes positive and negative assessments in each area.

Before drawing conclusions, the study examined the extent to which each of the domains is related to subjective well-being. At variance with Bonin and Rinne (2006), we omitted a discussion on the link between personal health ratings and happiness as the close correlation between these dimensions made it impossible to attribute causality in our data. In addition, the analysis of changes in income takes into account adaptation trends which might result in a temporary impact only (Bonin and Rinne 2006; Layard 2006).[7]

Findings

As discussed above, the data collected through in-depth interviews provide us with an opportunity to analyze the impacts of formal work engagement on different dimensions of quality of life, including social assistance recipients' own assessment of their well-being. Studying this rather narrow definition of SWB relating to work activation helps us gain a greater understanding of specific conditions that might support recipients' better integration in the labor market and social inclusion in general. Social inclusion is usually defined as the process that prevents people from becoming excluded and provides them with the opportunities for greater participation in society. For social assistance recipients who are capable to work, this can be done by

[7] According to adaptation theory, people first react strongly to new circumstances, but they return to their original position over time (Diener et al. 1997).

improving their income situation through increased social transfers but also, and more important, by providing adequate employment opportunities and participation in different aspects of social and civic life.

The Livelihoods of Social Assistance Respondents and Public Work Participation

To put in context the respondents perceptions of their well-being and the extent to which public work participation affected it, we first consider their livelihood strategies and the role that different programs, from which they benefited, played.

Respondents were asked to describe the kinds of support they were benefiting from, with the aim of learning about their own and their families' conditions and coping mechanisms.

For social assistance recipients, the main survival strategies revolve around a combination of income sources (Matkovic et al. 2010). Respondents generally expressed disappointment with their survival strategies with a great deal of Social assistance was usually described as an important but minimal benefit covering only basic needs (bread, basic groceries, and, very often, utility payments). The child allowance was considered an important and stable source of income for families with children. For social assistance recipients, "stability of resources" mattered a lot as the assistance and support of extended family was almost non-existent, the role of nongovernmental sector was limited to a few cases, and informal jobs were infrequent. However, practically all the participants interviewed admitted that they worked in the informal economy, including agricultural and construction works, garden maintenance, cleaning jobs, and singing.

In contrast to the description of their usual livelihood strategies, the respondents were very enthusiastic in describing their work experience and income earned with the public works. They saw the income earned as a matter of pride and happiness relative to official support. Prompted to compare the overall feelings associated with the receipt of social assistance with that of earning money through formal employment, the respondents often provided arguments in favor of official work engagement:

> I feel as if, if this work continues, I am useful in this society. Why do I feel useful in the society? Because I also pay social contributions. Am I expressing myself well?…It means—I am useful! So, it means that I am providing assistance for someone else. Let the social assistance exist, but it should be given to those who really need assistance, who are not able to work. I think that's what the Government should do. But, we the young, we should work. Okay, not all the people are well educated, but I think, for example, we all have our own qualification. Why wouldn't I be able to clean the streets? Why wouldn't I clean the street—it's a respectful job and I can earn decently?!?
>
> (male, 32 years)

At the time of interviews, most of the respondents were registered as unemployed. Only three interview participants, including one social assistance recipient, retained employment status after the completion of the public work project. In terms of labor market achievements, this outcome could be described as rather disappointing. This is particularly true for the group of social assistance recipients since only one

Box 8.2 Social assistance recipients' impressions about work engagement

"Oh, it was the first official stamp in my worker's booklet!!! After so many years…I felt very well…This work gave me a lot...."

"When I received the first salary, I think…it was for me as if I was flying… Look at it from this side: not a single sick leave day, nothing, it was an incentive to get up and go to the work place…You work…You have a job...."

"When I receive social assistance, I feel very useless. In general…Personally…I don't feel comfortable, because the assistance should be receiving those who can't work. Those are the disabled and the elderly. They should receive social assistance. And we? We are young and we should work. So that even for the others…The others should also benefit and we should benefit. It's mutual… If we work for a firm, the employer…He should also benefit, and we should be fine. So, we get the money and they get the job done…I feel very bad when I have to wait to receive 4,000-5000…when I work, I get 15,000 and I could plan. Both my husband and I used to work. I feel more confident, important, and useful...."

participant out of the twenty interviewed managed to find a formal job following the public work engagement. One third of former welfare beneficiaries had already reapplied to the social assistance program; the other third claimed unemployment benefits, while the rest found themselves in some kind of limbo awaiting the decision on "the beginning of a new public work."

For a great majority of recipients, employment through public works was the first official employment after years of "waiting" or searching for a job. One respondent was offered employment through public works after being registered as unemployed for more than 22 years. Most had waited between 10 and 20 years. The overall satisfaction levels associated with employment were exceedingly positive. Some of them are presented in Box 8.2.

At the individual level, the experience of work engagement was significant in terms of mental stability, personal satisfaction, and pride. At the family level, besides financial security, the experience of formal work had an impact in terms of improved mood, mental health, and "peace at home" as presented in Box 8.3.

Except for the non-recipients with university degrees, earnings from the public works appeared to be a significant work incentive and a source of satisfaction for all the respondents. The minimum wage, received by majority of them, was described as a financial resource "paid on time" which allows them to "plan the financing of their needs." "Stability and security" of earnings are usually described as the most important factors influencing their decision to opt for formal employment with a minimum wage rather than informal activity that could possibly yield higher income. The older respondents also stressed the importance of paying social contributions and meeting the requirements for pension.[8]

[8] Public pension system in Serbia functions as a pay-as-you-go scheme.

Box 8.3 Perceptions about the impact of work activity on mental health

"When there was the public work, the atmosphere at home was very nice… Otherwise…We are all sick, nervous...."

"First of all, the family mood is at a higher level. Why? When I don't work, it has a negative mental effect, on all of us, you understand…When, for example, I have monthly earnings, my spouse as well, we get the money and schedule how we are going to spend it. The overall atmosphere in the family is better immediately."

"…My daughter had been sad all day long. I didn't know what to say. I told her that I got fired. I felt uncomfortable and very very useless and sad, both because of her and because our family. And, because of the society in general...."

Subjective Well-Being and Employability

The employment probability for social assistance recipients is generally very low. Despite the fact that public works provide only temporary employment, they are expected to raise the participants' competitiveness in the labor market, thus increasing their chances for employment. However, only one public work participant among those formerly receiving social assistance was employed 3 months after the completion of the public work project. According to the latest findings (Petrovic 2011), the share of social assistance recipients who found employment after public work participation is 6.8%, which is higher than the employment rate found for all public work participants—1.4% in 2007 (Arandarenko and Krstić 2008). Despite this relatively positive outcome labor market outcomes remain generally unfavourable. In this light, it is interesting to examine the impact of the program on employability, a key element of the activation agenda.

Some authors argue that improvement of subjective employability, other than increasing the chances of employment, decreases the mental cost of being unemployed, thereby directly influencing individual subjective well-being (Frey and Stutzer 2002; Bonin and Rinne 2006). With regard to employability, the discussion in our analysis centered on respondents' perceptions about qualifications and skills acquired, as well as on the chances of finding new employment.

Public works appeared to have a strong positive effect on the "qualifications and skills" of social assistance recipients, signaling that the training component of public works programs had a rather positive impact: "*I believe that I acquired some knowledge. Both as a brick layer and other stuff…We did all sorts of things there*." Prompted to assess the change, participants almost unanimously singled out the acquired qualifications and skills as the biggest positive achievement from public works: "*Really, it increased, my knowledge has increased. You learn when you work with people and you learn how to work with them…I don't want to lie. There were things that I didn't know how to do and I learned*."

For a significant number of respondents, training activities were provided as part of their public work engagement. The duration of training varied from few

Box 8.4 Perceived changes with regard to chances for employment

"I don't know, son…It all depends…it depends on other people as well…Is there anyone ready to give me some job and pay for my contributions…I just want the same…It's all the same, the chances are not that big, but still it all depends...."

"I've been looking for a job since December 'til now. I haven't found, I mean, I've found but…I was at one place. They had been looking for a worker. I went there. Took a seat. We talked this and that…And, then, they said…up to 30 years of age. And, I am 32. We talked for half an hour. The man said: 'Well, you are too old for this.' I was supposed to work in storage. What shall I say? I couldn't say anything. I spent half an hour there, we talked, I thought there will be something out of this since we had been talking for half an hour. But, he said up to 30 years of age. What can I say? I didn't want to believe in what I had just heard."

"The first thing they asked me was: 'How old are you?' and 'How many kids do you have?'"

"I think that the chances to find a new employment are bigger. I have some work experience now and I have a stamp in the worker's booklet. It should be easier…I hope...."

"My chances should be bigger now, but you never know…Still, I hope…I hope and expect some better days. I already told you about that certificate.... I know a bit more now then before…should help...."

days of on-the-job training to month-long certified training programs in specialized institutions. This could partially explain why many of them would like to perform the same activity in the future. For most of them, the training and qualifications represented their first experience of formal skill development. The quantitative analysis showed that only 8% of social assistance recipients had ever participated in a training program. The data further confirmed that for one third of social assistance recipients who participated in public works, the qualifications and skills acquired in the public works helped them find new employment (Petrovic 2011).

With regard to the "chances for employment," opinions were more diverse. Participants older than 50, but sometimes also the younger ones, expressed significant doubts over their chances of finding a new job. This was very often supported by anecdotal evidence about potential employers, who were seen as more interested in younger workforce as depicted in Box 8.4.

Some respondents however made rather short but very optimistic statements over their chances for future employment. This was particularly evident among participants for whom employment in public works was the first involvement in the formal labor market. Moreover, for many of them, the inclusion in the labor market was perceived as a first step toward greater inclusion in society.

Box 8.5 Perceived changes with regard to the level of social contacts

"Yes, I am in contact with people and I better understand them."

"I know more people now and I am in better contact with people because of the public work. In the past, even if they were looking for a worker, they didn't know who to contact. Now, if she decides to do something with the garden, she knows that you work that and that you are free after work. She gives me a call: « Would you please come? I have one tree that needs to be pulled out.» Or any other job around the house…It means, I know more people and they offer me jobs. And, in general, I have more contacts with people."

"My social contacts are much better. I've met more people, which opens the door…."

"Oh, yes, definitely. The circle is bigger…Both friends and others…And nice communication and better words…everything...."

Subjective Well-Being and Social Inclusion

As discussed above, social inclusion is not only about labor market integration. It also involves social exchange at a qualitatively new level, as well as participation in different aspects of social and civic life. Our interviews allowed us to explore the level of social contacts and social exchange that are part of this broader notion of inclusion.

In our study, personal contacts established at the workplace represented one of the core reasons for the very high level of contacts reported. In addition, higher reported levels of self-confidence enabled participants to broaden their social interactions. The level of self-confidence showed a marked increase, particularly among the former social assistance beneficiaries. This was usually coupled with an increased willingness to look for a new job. However, that in the absence of formal employment opportunities, the able-bodied social assistance recipients often reported undertaking activities in the informal economy and rarely make a distinction between formal and informal jobs. It is in this light that their reported willingness or readiness to look for a job and accept an offer should be interpreted. Even if their new jobs are found in the informal sector this does not detract from the general social integration effect of their labour market activation, as shown in Box 8.5.

Summing up, social assistance beneficiaries feel more and better heard after their work experience in the public works. They report a higher number of contacts and a higher position in society. Their work is valued. They feel accepted and more integrated:

> I felt nice and free, and I felt that they accepted me in the society. That's the fact. Here, in our municipality, they accepted me very well. All of them, without exception: the president, manager, to start with the highest positions…and all the others. They respected me and there was no discrimination. Somehow, it felt like a second family to me.
>
> (female, 35 years)

Participation in Public Works: An Overall Assessment

As noted earlier, respondents' assessment of their participation in public works included descriptions of whether their personal situation had changed following the completion of the project. In our analysis, we focused on individual' responses related to willingness to search for a job, changes in their family income, personal qualifications and skills, prospects new employment, and levels of self-confidence and social contacts.

The public work employment has positively affected the subjective well-being of social assistance recipients across these domains. The strongest positive effect concerned the qualifications and skills acquired in public works, possibly due to the training components which were well designed and well implemented. The frequency and quality of social contacts improved with increased integration in other areas including the, labor market. Positive effects reported in these areas were larger than the objective prospect of being employed, as perceived by program participants. Clearly, factors other than employment affect their well-being. This finding is in line with Bonin and Rinne's (2006) study.

Public works are generally not seen as very effective in terms of labor market impacts. In the case of Serbia, this finding is supported by Arandarenko and Krstić's (2008) analysis of active labor market policies. In our study, we explored a number of broader dimensions of impact. This results suggest that public works have important positive impacts on subjective well-being and social inclusion of social assistance recipients. This is particularly the case for older groups of recipients, as confirmed later in the study of Petrovic (2011).

An interesting observation related to subjective well-being outcomes also emerges. Across the board, social assistance beneficiaries grade their experiences very high on the subjective well-being measurements even when their basic needs remain unmet. This is in line with context theories which claim that the factors influencing SWB vary across individuals and time (Diener et al. 1997). How good or bad people judge life events will reflect the circumstances in which they live and the events they experience. For the group of social assistance recipients included in this qualitative analysis, the rather harsh initial life circumstances meant that any improvement on SWB dimensions was graded relatively high.

Finally, the findings suggesting a significant impact of work engagement on certain aspects of life. This is particularly related to acquiring qualifications and skills, broadening social contacts, and building self-confidence for greater social exchange. Such observations help to increase our understanding of subjective well-being of the poor. They also set the stage for greater policy actions leading to increased activation and social inclusion of welfare recipients. The effects identified might have serious policy implications, especially when considered alongside conventional economic performance indicators. Both kinds of measures are needed to understand well-being and to make informed decisions.

Conclusion

The subjective well-being impact of a given program is relevant both from the perspective of participants and of the decision makers concerned to improve individual welfare. By drawing attention to this aspect, this chapter did not aim to undermine the role of conventional economic indicators but to present a highly complementary set of measures for evaluation.

In this chapter, we focused the analysis on social assistance recipients. We wanted to contribute to a better understanding of subjective well-being of the poor who got a chance to work. Based on our qualitative analysis, we concluded that the positive effects of work engagement on subjective well-being of social assistance recipients were very strong. The evidence is strongest in relation to their perceptions about the level of attained qualifications and skills and social contacts. In addition, the program impacted on individual welfare by strengthening the desire to be active in the labor market and on self-confidence. The program has supported the overall integration of social assistance beneficiaries into society. All of this evidence makes the case for further work activation of social assistance beneficiaries.

Some of the findings presented in this chapter have been supported by a quantitative analysis of financial social assistance recipients in Serbia (Petrovic 2011). The results of this analysis confirmed the positive impact of qualifications and skills acquired in public works on finding a new job. They also revealed relatively higher willingness of social assistance recipients compared to other public work participants to be involved in employment.

On balance, subjective well-being measures enrich the assessment of public works program. There is scope for more use of subjective well-being measures to explore areas that may be neglected in traditional economic analyses. While it is important to triangulate these measures with other measures, they appear to be good candidates for inclusion in inclusion in an extended list of indicators to monitor deprivation and social exclusion.

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Chapter 9
Does Formal Work Pay in Serbia? The Role of Labor Taxes and Social Benefit Design in Providing Disincentives for Formal Work

Johannes Koettl

Introduction

This chapter is motivated by two particular features of the Serbian labor market, namely, the high levels of inactivity and informal employment among the Serbian working-age population. Both of these characteristics lead to the question if it is "worthwhile" for the working-age population to engage in income-generating activities in Serbia. And if so, what incentives do employers, the self-employed, and workers actually have to register these activities and pay taxes and contributions on the income that is generated?

There are a number of reasons employers, the self-employed, and workers might decide not to register their activities. First, regulations in the product and labor market—like product licensing, employment protection legislation, and minimum wages—might be too stringent, so in order to circumvent these regulations, people might decide to operate outside the formal economy. Second, certain administrative

Michael Weber contributed to the empirical analysis focusing on integrating income data from the household budget survey with data from the labor force survey. Background papers have been provided by Nikica Mojsoska-Blazevski, Victor Macias, Sasa Randjelovic, Bojan Ristic, and Jelena Zarkovic Rakic. This chapter greatly benefited from a close cooperation with Tatiana Gordine, Herwig Immervoll, and Dominique Partout at the Social Policy Division of the Organisation for Economic Co-operation and Development (OECD). Generous financial support has been provided by the governments of Austria, Germany, Korea, and Norway through the Multi-donor Trust Fund on Labor Markets, Job Creation, and Economic Growth.

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procedures related to paying taxes, accounting, completing statistical questionnaires, and so on might deter people from operating in the formal sector. Third, people and firms might want to avoid paying taxes on revenues, income, profit, or property and social security contributions. Fourth, formal income might lead to withdrawal of social benefits—like social assistance or unemployment benefits—so that people might prefer informal or no work over formal work. Fifth, enforcement of existing legislation on regulations and taxation might be weak, so the risks of circumventing regulations and avoiding taxes might be low.

This chapter focuses on the role of labor taxation and social benefit design, how it relates to informal employment and inactivity, and what disincentives for formal work might be provided to people in working age so they choose to "exit" into informality or inactivity. Bearing in mind that labor taxation and social benefit design are but two pieces in the puzzle to explain high levels of informality and inactivity, the analysis presented below highlights how, for lower wage earners, the value of formal social security entitlements that come with formal employment would have to be enormously high to offset the opportunity costs. This leads to the conclusion that formal (part-time) jobs at low-wage levels—so-called mini-jobs and midi-jobs—are not economically viable for low-wage earners. This lack of economic viability effectively excludes a substantial part of the Serbian working-age population from formal employment and social security coverage. In this latter sense, informality and inactivity might not only be a deliberate choice of exit but are also a matter of "exclusion."

The analysis starts from the question of what incentives or disincentives the inactive and the informally employed face when considering formal work. For the inactive, starting to work formally or not will be based on considerations of how any potential formal net wage and social security entitlements compare to the alternative of not working. Not working, though, might imply being eligible to income-tested benefits like social assistance, which recipients could (partially) lose when working formally, increasing the opportunity costs of formal employment.

For both workers and firms operating in the informal sector, switching to formality will have a number of implications. First, workers and their employers will become contributors to social security. This means that both the employer and the worker have to contribute to the pension fund, the health fund, and the unemployment insurance fund. The decision on formalization will therefore be importantly influenced by the value that informal workers attach to being covered by social security. Second, workers will have to pay personal income tax on their formal gross wages. This decision will be influenced by the value informal workers put on public services and social norms about paying taxes. Paying social security contributions and income tax combined will decrease workers' take-home pay when compared to their informal wage. Third, just like the inactive, informal workers after formalizing might not be eligible any more to a number of benefits that are income tested. When having no formal income on record, workers might be eligible to income-tested benefits like social assistance or family benefits. Once informal workers are formalizing, though, they might lose all or parts of these benefits, reducing their formal income further and

increasing the opportunity costs of formal work. Finally, firms which are formalizing informal workers, will generate additional formal revenues by switching informal revenues to formal revenues. This implies paying additional taxes in the product market, like sales or value-added taxes.

The chapter proceeds as follows: the next section describes the characteristics of the informal employed and the inactive. Next, the opportunity costs of formal employment, created by labor taxation and benefit design, are analyzed. This is followed by an investigation of some of the consequences of informality on Serbia's society, with a focus on fiscal implications in terms of lost revenues for the state. The final section outlines some policy options to address informality and inactivity in Serbia.

Informal Employment and Inactivity in Serbia

The International Labour Organization (ILO) defines informal employment as (1) employers and own-account workers who work in their own non-registered enterprises; (2) contributing family workers; (3) members of informal producers' cooperatives; (4) employees whose employment relationship is not subject to national labor legislation, income taxation, social protection, or entitlement to certain employment benefits; and (5) own-account workers engaged in the production of goods exclusively for own final use by their household (Hussmanns, 2003).

The Serbian Labour Force Survey (LFS) is well designed to measure this concept of informality. It contains questions on most dimensions of the above-mentioned definition. Specifically, for the analysis presented below, informality is defined as (1) all employers, self-employed, and own-account workers of non-registered enterprises; (2) unpaid family workers; and (3) all employees without written labor contracts. Note that since the ILO definition of informal employment includes unpaid family workers and self-employed with unregistered enterprises, it includes a large part of the agricultural sector—that is, farmers and their contributing family members. In Serbia, about 60% of the informally employed fall into this category (see below).

According to the October 2008 LFS, about 650,000 people worked informally as indicated in Table 9.1. That means that about 10% of the Serbian working-age population—aged 15 or older—were working informally. To put this into perspective, 2.2 million people were formally employed (34% of working-age population) while 3.1 million were inactive (49%) and 460,000 were unemployed (7%). It also means that 23%—almost a quarter—of all employed people in Serbia work informally.

Informal employment is concentrated in the private sector, especially in non-registered firms. Informal employment in the public sector is almost nonexistent as seen in Table 9.2 while in the private sector, 32% of all employed are informal. In private registered firms, about 16% of the employed are informal, while almost all

Table 9.1 The Serbian population aged 15 or older by employment status and age group (2008)

	Employed					
Age group	All employed	Formally employed	Informally employed	Unemployed	Inactive	Total
15–24	191,298	119,318	71,981	114,382	598,176	903,857
25–39	911,309	765,254	146,055	181,797	247,867	1,340,972
40–64	1,543,615	1,217,363	326,252	161,025	1,011,050	2,715,690
65+	159,085	57,436	101,649	0	1,230,724	1,389,809
Total	2,805,307	2,159,371	645,937	457,205	3,087,816	6,350,328

Source: Serbian Labour Force Survey (LFS, October 2008)

workers in non-registered firms are informal. Among all those informally employed, about 40% work in registered firms and 60% in non-registered firms. So, working in a non-registered firm is a strong indication of being informally employed, but a significant share of the informally employed also works in registered firms.

The majority of informal workers are aged 40–64. About 330,000 of the total 650,000 fall in this age group (see Table 9.1). Yet, when looking at informality rate by age group, the highest shares of informal workers are among the young (38% of the 15- to 24-year-old workers) and the old (64% of those workers aged 65 or older, see Table 9.3). So although most informal workers are aged 40–64, it is actually those who are at the margin of the labor market who are most likely to be informal, namely, those who just entered (the young) and those who are about to leave the labor market (the old).

For the most part, informal workers are employed in the agricultural sector, but there is also a sizeable informal labor force in the nonagricultural sector. About 68% of all informal workers are employed in the agricultural sector, mainly as individual farmers or as unpaid family workers as shown in Table 9.4. In the nonagricultural sector, employees are the main group of informal workers. Typical jobs of informal workers in the nonagricultural sector are in the retail and catering industry. The second largest informal group in the nonagricultural sector is the liberal professions and own-account workers. In fact, when compared to formal workers in this group, the data suggest that almost 70% of all workers in this group are informal.

In terms of educational attainment, informal workers display significantly lower education levels than formal workers. About 25% of informal workers have no or only primary education, while only 3% of all formal workers fall in the same group as shown in Table 9.5. Especially workers aged 40 and older with no or only primary education seem to be concentrated in the informal work force. Almost 70% of all workers who fall in this group are working informally.

The informal sector does not seem to act as a cushion during times of crisis. Contrary to common belief, informal employment was affected more severely than formal employment in the course of 2009. Comparing the shares of the working-age population that are formally or informally employed, unemployed, or inactive between April 2008 and October 2009 shows that the informally employed population decreased by more than 20% while the formally employed population decreased

Table 9.2 Share of formal and informal workers by ownership type of production unit (percent of all employed, 2008)

Ownership type	Formal (%)	Informal (%)	Total (%)
Private sector	67.9	32.1	100.0
Private—registered	84.0	16.0	100.0
Private—non-registered	2.3	97.7	100.0
Public sector	99.9	0.1	100.0
State	99.9	0.1	100.0
Socially owned	100.0	0.0	100.0
Other	93.2	6.8	100.0
Total	77.0	23.0	100.0

Source: Serbian LFS (October 2008)

by only 5% as indicated in Table 9.6. At the same time, the unemployed population increased by 18% and the inactive population increased by 5%.

The data suggest a certain segmentation of the Serbian labor market between formal and informal employment. Informal employment seems to be more sensitive to changes in economic growth, at least during the crisis year of 2009. One potential explanation could be that firms use informal workers for extensive adjustments of their staff, while formal workers are used for intensive adjustments. That is, firms adjust informal employment through layoffs during an economic downturn, while formal employment is adjusted by reducing working hours. This could potentially be due to employment protection legislation, which increases firing costs for the formally employed. Also other labor market policies that aim to support formal employment—like, for example, short work schedules or wage subsidies—might contribute to increasing the opportunity costs of firing formal worker vis-à-vis informal workers. A definite answer, though, cannot be provided without further analysis and might be different from what is observed in other countries.[1]

With regard to inactivity, Serbian labor force participation is low at only 51% (October 2008), and during the financial crisis last year, labor force participation dropped even further and is now at only 49% (October 2009, see Table 9.6). This compares unfavorably with other European countries. Even when correcting for GDP per capita, Serbia is below the trend when compared to other European countries (in Figure 9.1). In terms of educational attainment, the inactive population is less educated than the formally employed population, suggesting that their earnings potential on the labor market is lower, just like the informally employed.

The high inactivity rate means an untapped potential for the Serbian economy. This is the reason why the European Union's (EU) Lisbon strategy—now replaced

[1] The literature acknowledges that the share of informal employment might be pro-cyclical or countercyclical, although in most countries, it appears to be countercyclical. For a literature overview on this topic, see Perry et al. (2007).

Table 9.3 Key labor market indicators for the Serbian population aged 15 or older by age group (percent, 2008)

Age group	Activity rate (labor force as share of population) (%)	Employment rate (employed as share of population) (%)	Informality rate (informal as share of employed) (%)	Unemployment rate (unemployed as share of labor force) (%)
15–24	33.8	21.2	37.6	37.4
25–39	81.5	68.0	16.0	16.6
40–64	62.8	56.8	21.1	9.4
65+	11.4	11.4	63.9	0.0
Total	51.4	44.2	23.0	14.0

Source: Serbian LFS (October 2008)

Table 9.4 Informal workers by sector and professional status (share of total informal employment, 2008)

Professional status	Nonagricultural (%)	Agricultural (%)	Total (%)
Owner/co-owner of an enterprise	0.3	0.2	0.5
Owner/co-owner of a shop	1.0	0.2	1.2
Liberal profession and own-account worker	10.9	1.4	12.3
Individual farmer	0.0	25.4	25.4
Employee	17.1	6.2	23.3
Unpaid family worker	3.0	34.4	37.3
Total	32.2	67.8	100.0

Source: Serbian LFS (October 2008)

Table 9.5 Informal workers by formality status, age group, and educational attainment (share of total informal or formal employment, 2008)

Highest educational attainment	15–24 (%)	25–39 (%)	40–64 (%)	65+ (%)	Total (%)
Informal					
No education	0.0	0.1	1.1	2.4	3.5
Primary	0.8	1.3	10.2	9.0	21.3
Secondary	10.3	20.4	37.8	3.8	72.4
Tertiary	0.0	0.8	1.5	0.5	2.8
Total informal	11.1	22.6	50.5	15.7	100.0
Formal					
No education	0.0	0.0	0.1	0.2	0.3
Primary	0.0	0.2	1.4	1.5	3.1
Secondary	5.1	27.1	40.7	0.8	73.6
Tertiary	0.4	8.1	14.2	0.3	23.0
Total formal	5.5	35.4	56.4	2.7	100.0

Note: Shaded cells indicate a considerably higher share of that group among informal workers when compared to the same group among formal workers
Source: Serbian LFS (October 2008)

by the 2020 strategy—sets a target of 75% labor force participation of the population aged 20–64. For Serbia, as an aspiring EU country, it will be important to consider policies on how to increase the activity rate and unleash the untapped potential of the inactive labor force. This is discussed in further detail below.

In conclusion, it seems that a large share of the Serbian population is either not participating in the labor market at all or employed informally. While the crisis has diminished informal employment recently, 23% of all employed were working informally in 2008. Since there is almost no informal employment in the public sector, this corresponds to an informality rate of 32% of all employed in the private sector. Inactivity, on the other hand, increased during the crisis.

Table 9.6 Employment status of the Serbian population aged 15 or older over time (as share of working-age population)

	April 2008 (%)	October 2008 (%)	April 2009 (%)	October 2009 (%)	Percent change (%)
Employed	44.7	44.2	41.6	40.8	−8.7
Formally employed	34.2	34.0	32.4	32.4	−5.1
Informally employed	10.5	10.2	9.2	8.4	−20.3
Unemployed	6.9	7.2	7.7	8.1	18.4
Inactive	48.4	48.6	50.7	51.1	5.4

Source: Serbian LFS (April 2008 to October 2009)

Most of the informal work occurs in the agricultural sector, either as individual farmers or as unpaid family workers, although there is also a sizable informal labor force in the nonagricultural sector, in particular among employees and own-account workers. In addition, informality is concentrated among those with low educational attainment and above the age of 40 and to some extent among the young. In other words, informality is high among those that have just joined the labor force (the young) or those that are about to leave it (the elderly, in particular above the age of 65). Just like the informally employed, also the inactive display low educational attainment. This suggests that for both groups, earnings potential in the labor market is likely to be concentrated at the lower wage end.

The financial crisis could represent an opportunity to permanently reduce informal employment. The economic downturn of 2009 has considerably diminished informal employment, but the risk is that it will rebound strongly during the economic recovery. At the same time, inactivity has increased during the crisis and—given Serbia's aging population—should decrease in the future. Reforms to prevent a resurgence of informal employment during the recovery and decrease inactivity might also address labor taxation and social benefit design, which is the topic of the next section.

Labor Taxation and Social Benefit Design

This section presents a closer investigation of the Serbian tax and benefit system and focuses on the incentives and disincentives they provide to formal employment. For low-wage earners opportunity costs of formal employment are extremely high. This is due to the cost of the minimum social security contributions but also due to the design of social assistance and family benefits. Taken together, informal workers at low wages have to give up a considerable amount of their informal wage in order to formalize, and it is unlikely that the value of social security entitlement (and other benefits like formal employment protection legislation) that they get in return for formalization exceeds these implicit costs. The same holds for the inactive when

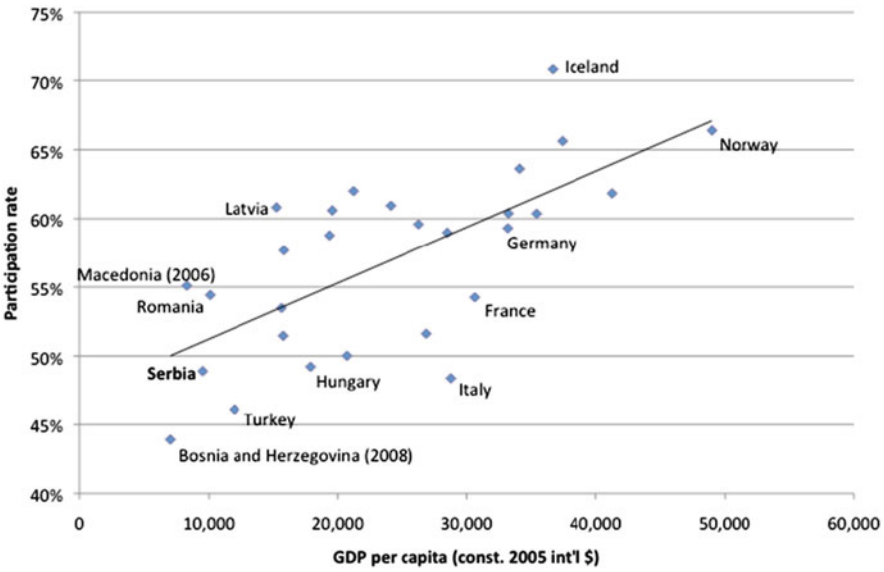

Fig. 9.1 Scatter plot of participation rate (labor force as share of population aged 15 or older, 2009) versus GDP per capita (constant 2005 international $, 2007) for select countries. *Source*: Author's calculation, based on Eurostat (2010), Serbia LFS (October 2008), and World Bank (2010)

considering formal work at low-wage levels. In other words, so-called mini-jobs and midi-jobs—that is, part-time jobs that pay less than the full-time minimum wage—are hardly economically viable in Serbia. Hence, workers with low educational attainment—like the informally employed and the inactive—might be, by and large, excluded from formal work in Serbia.

One indication, that taxation in general affects significantly income-generating activities in Serbia comes from enterprise surveys. A World Bank survey among Serbian enterprises reveals that 54% of firms cite tax rates as a one of the major obstacle—together with corruption and access to finance—for doing business in 2008 as shown in Figure 9.2. The question refers to all types of taxes and not specifically labor taxes. Nevertheless, the results indicate that employers perceive tax rates as high and as a greater obstacle to doing business than regulations and administrative procedures. Customs and trade regulations (35%), labor regulations (34%), tax administration (30%), and business licenses and permits (28%) figure less prominently as an obstacle to doing business. Therefore, although the results of this enterprise survey are not a direct measurement of obstacles to formal employment, they give an indication that tax rates could be a constraint for creating new formal jobs.

The incidence of labor taxes in Serbia is comparable to the incidence of labor taxes in other countries in the region or in the OECD for workers at high wage levels. The tax wedge on labor for lower wage workers is one of the highest at 36.7% as shown in Fig. 9.3. The tax wedge measures the difference between labor costs and take-home pay of workers. It expresses the costs of social security

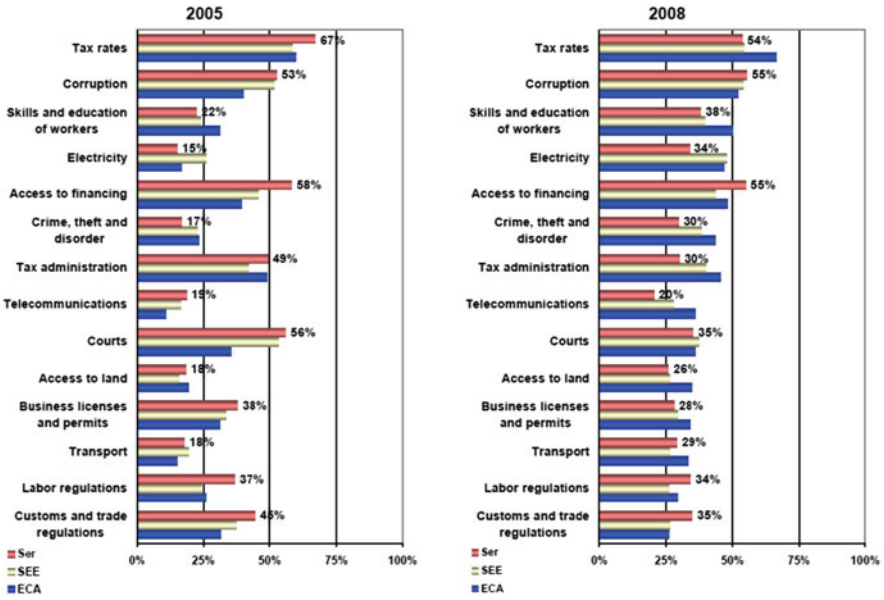

Fig. 9.2 Obstacles to doing business in Serbia 2005 and 2008 (percentage of firms indicating a problem). *Source*: World Bank (2009)

contributions by employers and employees and the personal income tax of employees as a share of total labor costs. These taxes vary depending on family type and wage level. For a single with no children who receives a gross wage of 33% of the average wage, only four countries charge higher taxes than Serbia; for a one-earner couple with two children, only three countries charge higher taxes than Serbia.[2]

Labor taxation in Serbia is not very progressive. While in most other countries, labor taxes increase significantly with the wage level—for many countries, by over 10 percentage points between 33 and 100% of average wage level—in Serbia, labor taxes increase by only 2.6 percentage points. Although countries with a high tax wedge at lower wage levels can be expected to display less progressivity, Serbia displays especially low level of progressivity as shown in Fig. 9.4.[3] Overall, for singles without children, only the Bulgarian payroll tax system displays less progressivity.

[2] In Serbia, full-time work at 33% of the average wage is below the legal minimum wage, but the same tax wedge applies to someone receiving average wage but working 33% part-time. The same holds for most other countries, although there can be slight variations of the tax wedge for part-time workers.

[3] The assumed relationship is that tax systems need to raise a certain fixed amount of resources, and those that put higher taxes on lower wages have less of need to increase taxes at higher wages and hence display less progressivity.

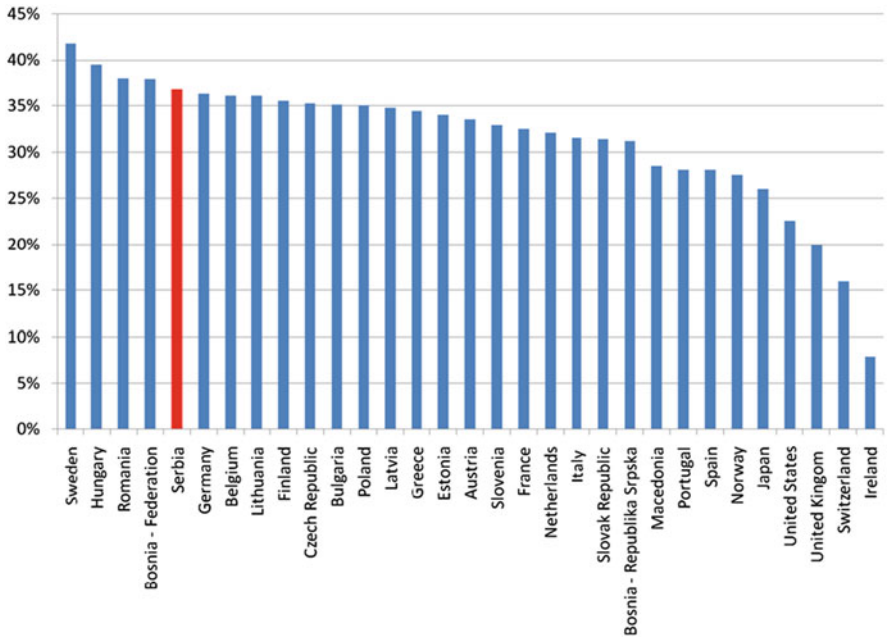

Fig. 9.3 Tax wedge for a single with no children at 33% of average wage for select countries. *Source:* Author's calculations based on OECD tax and benefit model

The reason for the high tax wedge at lower wage levels in Serbia is the minimum social security contributions that employees and employers have to pay. These minimum contributions are set at RSD 66,500 annually, equally split between employers and employees. The overall social security tax rate is set at 35.8% of gross wage: 22% for old-age pension, 12.3% for health insurance, and 1.5% for unemployment insurance. Yet, because of the minimum contribution requirement, everyone earning less than RSD 192,000 annually pays a share higher than 35.8% of gross income for social security. The minimum social security contribution is not adjusted for hours actually worked, so also part-time workers are subject to it. This means that in particular so-called mini-jobs and midi-jobs—that is, low-paid part-time jobs with few hours worked per week—have a relatively higher burden of payroll taxes.[4] In the extreme case of someone working 5 hours per week at the minimum wage, this person would receive an annual gross wage of about RSD 29,000—from which this worker would have to pay RSD 33,250 for minimum social security contributions so that he or she ends up with a negative net wage. The employer has to pay an additional RSD 33,250 for social security contributions. In other words, formal work does not pay at the lower wage levels.

[4] The terms mini-jobs and midi-jobs originate from the social welfare reforms (Hartz IV) in Germany in the early 2000s, which aimed at making work more lucrative for low-wage earners in this labor market segment.

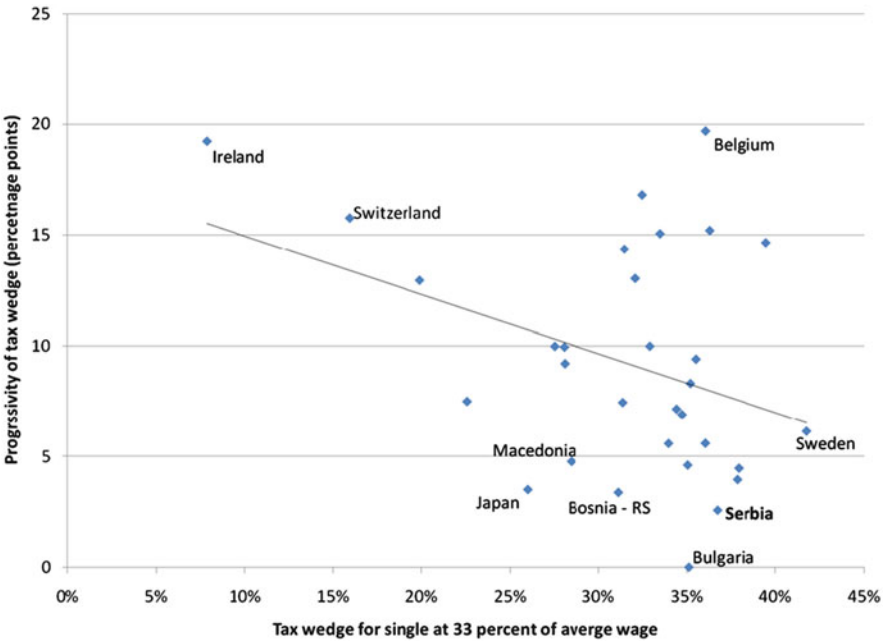

Fig. 9.4 Scatter plot of tax wedge for a single at 33% of average wage (percent) versus progressivity of tax wedge (percentage point change) for select European countries (2008). *Source:* Author's calculations based on OECD tax and benefit model

Moving along the hypothetical wage spectrum from 0 to 200% of average wage and using actual legislative data on income tax and social security contributions, Figure 9.5 depicts the tax wedge as the blue dashed graph for a single earner with no children. Figure 9.6 does the same for a one-earner couple with two children. As can be seen, the tax wedge is stable around 40% for wage levels above the minimum wage, but is significantly higher for wage levels below 25% of the average wage and lower. For wage levels below 10% of average wage, the tax wedge is close to or above 100%.

The tax wedge and the withdrawal of social benefits are the main contributors to opportunity costs of formal work. Think of an informal worker who earns a certain level of informal wage.[5] If this worker were to work in the formal sector, various implicit opportunity costs occur: First, assuming that the value of the marginal labor product does not change because of formalization, total labor costs of the informal worker have to be the same as for the formalized worker. For the informal worker, total labor costs are the informal wage. For the formalized worker, total labor costs are the net wage plus the income tax and both the worker's and the employer's

[5] Only workers who are not registered at all are considered; partially formal workers who underreport their wages are not considered.

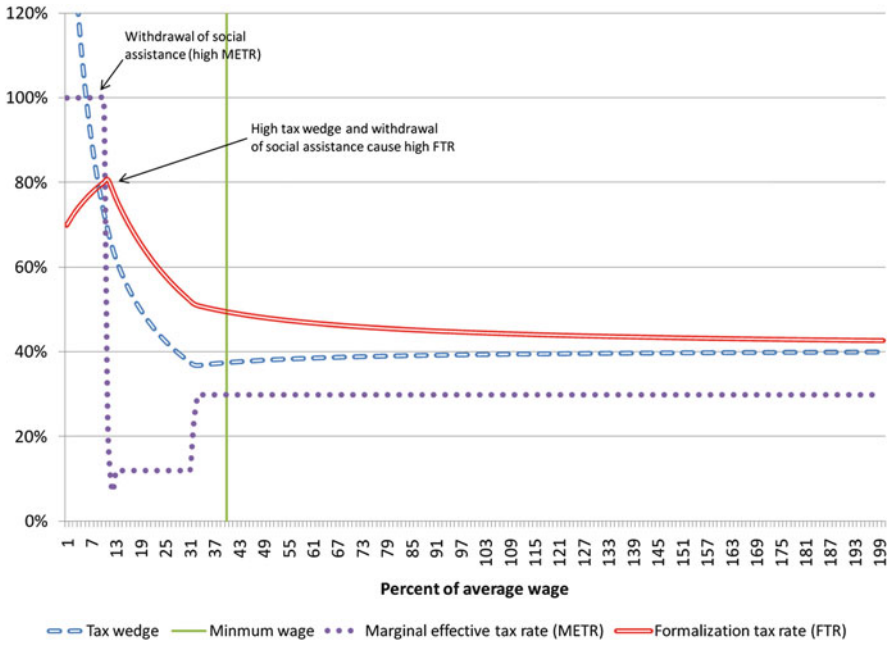

Fig. 9.5 The tax wedge, the marginal effective tax rate (METR), and the formalization tax rate (FTR) for a single with no children in Serbia (2009). *Source:* Author's calculations based on OECD tax and benefit model

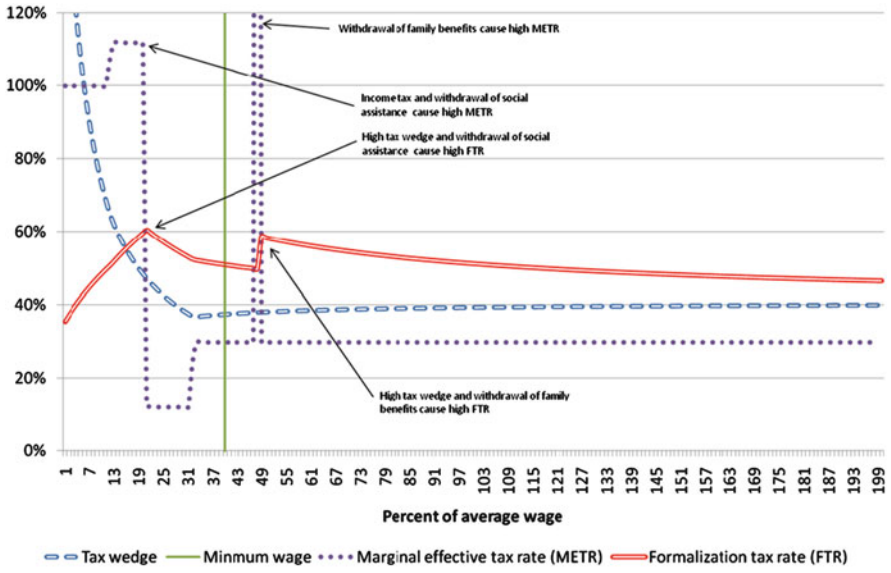

Fig. 9.6 The tax wedge, the marginal effective tax rate (METR), and the formalization tax rate (FTR) for a one-earner couple with two children in Serbia (2009). *Source:* Author's calculations based on OECD tax and benefit model

social security contributions—in other words, the net wage plus the entire tax wedge. Comparing the informal wage with the worker's potential formal net wage, the entire tax wedge enters as an opportunity cost of formal work for the informal worker. Second, informal workers also face implicit opportunity costs because they might lose parts of certain income-tested benefits—most importantly social assistance and family benefits—once they have a formal income on record. For example, if an informal worker receives a certain amount of social assistance, this benefit will be decreased or completely withdrawn if the worker formalizes and has an official income on record. This amount of the withdrawn benefit also enters as an opportunity cost of formal work.

Therefore, both of these losses—the tax wedge and withdrawn benefits—have to be taken into account when considering the implicit opportunity costs of formalization. At the same time, though, informal workers also gain from formalization: They gain a future right to an old-age pension, and they gain rights with regard to disability insurance, workers compensation, health insurance, and unemployment insurance.

Arguably, the most important of these potential gains are old-age pension and health insurance. With regard to old-age pensions, though, one has to keep in mind that especially low-wage earners tend to strongly discount future benefits because their concerns are focused on short-term income and, in cases of poverty, day-to-day consumption. With regard to health insurance, one has to keep in mind that the value of *contributing* to health insurance is considerably diminished because coverage is relatively easy to obtain for free. Many people are coinsured for free because their spouses might work in the formal sector. Yet, more importantly, for all those who have a monthly income below RSD 16,000 per month, health insurance is free. Since informal workers have no official income on record, it is therefore relatively easy for them to obtain free health insurance. They are required, though, to register as unemployed with the National Employment Service (NES), which creates additional problems further discussed below.

The implicit costs of formalization for informal workers are therefore a measurement of the necessary minimum value of social security benefits they receive in return for formalization. The value of rights to pension and unemployment insurance—but also from formal employment protection legislation—they gain from formalization must exceed their implicit opportunity costs from formalization. The red solid graph in Fig. 9.5 expresses this implicit cost to the informal worker as a share of informal income (the so-called formalization tax rate, FTR).[6] That is, it measures the difference between informal income (informal wage, social assistance, and family benefits at the level of no formal wage) and formal net income (formal net wage, social assistance, and family benefits at formal wage level) as a share of informal income. It is therefore the share of informal income that an informal worker has to give up to formalize.

For lower wage levels, the formalization tax rate is high. A single with no children who earns less than the minimum wage in the informal sector has to give up between 50 and up to 80% of income to formalize (see red, solid line in Fig. 9.5).

[6] For a detailed definition and discussion of the FTR, see Koettl and Weber (2012).

A one-earner couple with two children has to give up between 30 and 60% of informal income at very low-wage levels, and between 50 and 60% of informal income at wage levels between 10 and 100% of average wage (see red, solid graph in Fig. 9.6).

The main reasons for the high opportunity costs of formal work are the minimum social security contributions and the sudden withdrawal of social assistance and family benefits at higher wage levels. The minimum social security contributions have already been discussed above as one of the main obstacles to formal employment at the lower wage levels. Also the design of income-tested benefits plays an important role. Social assistance is paid out as a top-up to earned gross income to guarantee a minimum gross income of RSD 64,400 for a single with no children. Any earned gross income is subtracted from social assistance that is paid out. This means that any formal mini-job at wage levels below 10% of average wage does not pay—in fact, such a formal mini-job would decrease net income because of the loss in social assistance in combination with minimum social security contributions that have to be paid. Even for higher-paid midi-jobs, the net gain in income is not very high for the same reasons. For an informal worker, the sudden loss of social assistance due to even low levels of formal wage contributes to the implicit opportunity costs of formalization. A more phased-in withdrawal of social assistance could decrease this disincentive.

Family benefits also contribute to the formalization tax rate, albeit at higher wage levels of around 50% of average wage. A one-earner couple with two children receives an annual family benefit of RSD 44,700 if formal gross earnings do not exceed 50% of average wage. For higher wage levels, though, no family benefits are paid at all. This increases the implicit opportunity costs of formalization at this particular wage level (see the spike of the red, solid graph around 50% of average wage in Fig. 9.6). Informal workers with children at wage levels beyond 50% of average wage have to take into account that they would lose RSD 44,700 in family benefits annually if they worked formally.

The marginal effective tax rate (METR) also suggests that formal work does not pay in Serbia at lower wage levels. METR—depicted as the purple, dotted graph in Figs. 9.5 and 9.6—measures at a given wage levels how much of an *additional* dinar earned in formal gross wage is taxed away, either as labor tax or on the form of withdrawn benefits. It is therefore an indication of how much it pays for workers to earn more gross income, either by increasing work hours or receiving higher wages.

In Serbia, at low-wage levels (below 10% of average wage), every dinar earned is subtracted from entitlements to social assistance. Hence, 100% of any additional dinar earned is taxed away. For one-earner couples with two children, METR even exceeds 100% at wage levels between 10 and 20%, when personal income tax starts to kick in, meaning that net income decreases as gross wage increases. The same happens at 50% of average wage, with the sudden loss of family benefits.

It is unlikely that the value that informal workers put on social security benefits and employment protection exceeds the high implicit costs of formalization. The analysis above has shown that informal workers at low-wage levels have to give up significant amounts of their informal wage in order to formalize, and it is unlikely that the rights they gain in return for formalization exceed these costs. The only

relevant entitlements they gain from formalization are old-age and disability pensions and unemployment insurance. Health insurance, which is arguably the most important social security entitlement with immediate—as opposed to future—benefits, can be obtained through a spouse or by registering as unemployed, so it goes not into the value of formal benefits. The value of vested old-age pensions could be further discounted by noncontributory social assistance. The design of income-tested benefits like social assistance and family benefits also discourages formal jobs as formal income could easily lead to withdrawal of benefits.

In conclusion, formal mini-jobs and midi-jobs—that is, low-paying part-time jobs that earn less than minimum wage—do not seem economically viable in Serbia. This could lead many low-educated workers to either not work at all (and be inactive) or work informally. The previous analysis suggests that a substantial part of the informal labor force in Serbia has indeed low educational attainment and might work exactly in these kinds of mini-jobs and midi-jobs.[7]

The next section will elaborate by estimating how much informal workers are actually earning in Serbia and, based in this estimation, how much fiscal revenues are lost due to informal work.

The Impact of Informality

The majority of informal workers with labor income earn less than minimum wage. Collecting social security contributions from those earning more than RSD 200,000 could, *ceteris paribus*, boost revenue collection by up to 5% for social security institutions. The fiscal impact from creating formal mini-jobs and midi-jobs, on the other hand, is unlikely to create significant new revenues. At the same time, it would increase coverage and therefore create new liabilities for social security, but it would also decrease future poverty at old age. The impact of informality—and also inactivity—on the National Employment Service (NES) and the health insurance fund (HIF) is significant. Because registered unemployed are effectively entitled to free health insurance, many informal and inactive registered as unemployed, which puts an overwhelming administrative burden in NES. Raising even small contributions for HIF from any eventual formal mini-jobs and midi-jobs could alleviate the administrative burden for NES and raise additional resources for HIF.

The majority of informal workers earn less than the minimum wage. The section describing the characteristics of the informally employed points out that many informal workers (and also inactive) have low educational attainment. This suggests that the majority of informal workers have low (or in the case of unpaid family workers) no earnings. A more detailed exploration of the Serbian LFS and Household Statistical

[7] Clearly, no causality between high work disincentives and high levels of informal employment can be established without further empirical analysis. Koettl and Weber (2012), though, using similar concepts and a more elaborate empirical analysis find a strong positive correlation between work disincentives (METR, FTR) and informal employment in six new EU member states.

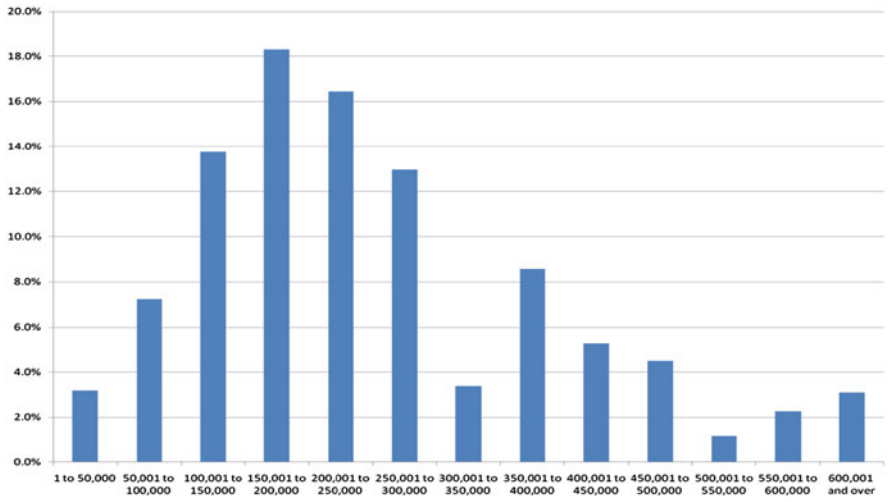

Fig. 9.7 Estimated distribution of informal workers with labor income by wage group (as share of all informal workers with labor income, 2008). *Source:* World Bank staff calculations based on Serbian LFS (October 2008) and Household Budget Survey (HBS 2008)

Office of the Republic of Serbia (SORS), Household Budget Survey (2008) confirms this conjecture. Applying a propensity score matching methodology to combine the labor status data of the LFS with the income data of the HBS suggests that about 40% of informal workers have annual labor income of less than RSD 200,000 and about 60% earn less than 250,000 as shown in Fig. 9.7.[8] To put this into perspective, the legal annual gross minimum wage in 2008 was RSD 236,000.

Therefore, the majority of informal workers with labor income face high implicit opportunity costs of formalization. The data suggest that many informal workers fall in the income range where labor taxation is disproportionally high and the potential loss from withdrawal of benefits like social assistance and family benefits is significant. In other words, for many informal workers and their employers, formal work does not pay because there are no economically viable options for formal mini-jobs and midi-jobs in Serbia. The data also suggests that informality rates are higher among low-wage earners. Among all workers with labor income, about 25–30% are working informally at lower wage levels (below RSD 200,000 annually), while at higher wage levels informality rates are generally below 20% (see Fig. 9.8).

Serbian social security institutions might lose up to 5% of total collected contributions due to informal workers earning more than RSD 200,000 a year. This estimate takes into account only labor income, but not income from self-employment,

[8] The matching procedure only takes into account labor income, not income from agriculture, self-employment, capital income, or other forms of income.

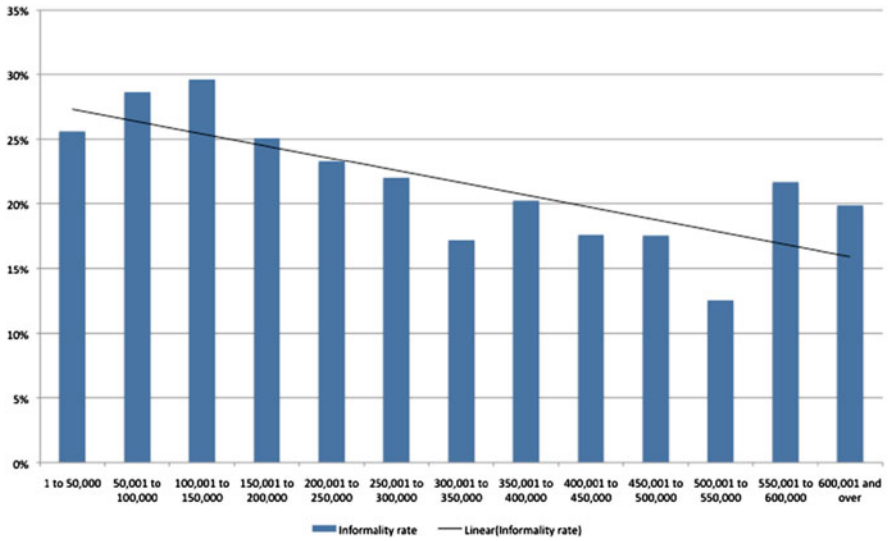

Fig. 9.8 Informality rate among workers with labor income by wage group (informal workers with labor income as share all workers with labor income by wage group, 2008) and linear trend. *Source:* World Bank staff calculations based on Serbian LFS (October 2008) and Household Budget Survey (HBS, 2008)

agriculture, capital income, and so on. Lost revenues from these income sources cannot be estimated at this point. Also, this estimation does not take into account any changes on labor supply and demand caused by changes in tax rates. Such estimation would require considerable additional analysis, based on panel data.

Lost revenues from informal workers earning less than RSD 200,000 annually seem significantly smaller. Even under the current financing rules of minimum social security contributions—which, if paid as required by law, would make most jobs in this income range not economically viable—the lost revenues for social security institutions do not seem overwhelmingly high. Hence, the fiscal impact of any reform of minimum social security contributions might not be substantial. The additional fiscal revenues generated from formal mini-jobs and midi-jobs would most likely be small.

Nevertheless, reforming the minimum social security contribution floor and the design of social assistance and family benefits could help to overcome social exclusion, formalize the informal, and activate the inactive. Because of the high informality and inactivity rate, a substantial share of the Serbian working-age population is not covered by old-age, disability, and unemployment insurance. Since these are earnings-related benefits, extending coverage will not necessarily increase the future deficit of these social security institutions. Any fiscal impact from extending coverage, though, has to be carefully evaluated, in particular with regard to any minimum entitlements (like a minimum pension). At the same time, bringing the excluded into social security does create additional revenues, can help to improve the fiscal

Table 9.7 Employment status and social security status of the Serbian population aged 15 and older (percent, 2008)

	Formally employed (%)	Informally employed (%)	Unemployed (%)	Inactive (%)	Total (%)
Population aged 15 and older	34.0	10.2	7.2	48.6	100.0
Registered with National Employment Service					
Yes	8.3	20.8	38.5	32.5	100.0
of which receive no health insurance at work	51.3	94.6			
No	43.2	8.6	1.5	46.6	100.0
Aged 75 and older	2.1	4.3	0.0	93.6	100.0

Source: Serbian LFS (October 2008)

position of pay-as-you-go schemes (especially the old-age pension), and might also reduce the future burden on social assistance. With regard to health insurance, the fiscal impact should be unambiguously positive because most of the informal and the inactive are covered without contributing even today.[9] In addition, the administrative burden on the National Employment Service (NES) from administering free health insurance for the unemployed could be alleviated substantially.

Only about 40% of the registered unemployed are actively seeking jobs; the rest are either informally employed or inactive. In 2008, about 800,000 people were registered as unemployed with NES. The LFS suggests that only 39% of the registered unemployed are actually unemployed (see Table 9.7). About 21% of the registered unemployed, though, were informally employed and another 33% were inactive.

The main motivation to register as unemployed is to obtain free health insurance coverage. Serbian law grants free health insurance to anyone who earns less than RSD 16,000 per month. Since the informally employed and the inactive have no formal income on record (other than capital income or income from property), they are all entitled to free health insurance. In order to obtain free health insurance, though, the health insurance fund (HIF) requires documentation that the applicant is unemployed and hence requires him or her to register as unemployed. Not surprisingly, almost 95% of the informal workers who register as unemployed do not receive health benefits at work (see Table 9.7). In addition, many other entitlements to benefits on municipal level—like, for example, entitlements to lower public transportation fares, school books for children, and subsidies for school tuition fees—require documentation that the applicant is registered as unemployed.

Registering the unemployed puts a serious administrative constraint on NES. Currently, NES has only about 144 caseworkers employed to assist the unemployed. This puts the number of cases per caseworker at over 5,000. Most EU countries have

[9] Only about 8% of the population is currently not covered by the Serbian health insurance fund (HIF).

less than 300 cases per caseworker. Registering such a large number of unemployed puts a significant constraint on these caseworkers as they spend most of their time with registry work as opposed to supporting the genuinely unemployed who are seeking jobs.

In conclusion, informal employment leads to significant fiscal revenues losses and puts an administrative burden on NES. A comprehensive estimate on lost fiscal revenues is not possible at this point, but might be feasible after further research. The estimates that are available at this point suggest that social security institutions could boost their revenues from contributions by about 5% if labor income from informal workers earning more than RSD 200,000 annually were properly declared. The impact from additional revenues collected from formal mini-jobs or midi-jobs is likely to be significantly smaller. At the same time, bringing the informal into the formal sector and activating the inactive—even at low earning levels—would help to decrease social exclusion, in particular with regard to old-age pension. It could therefore help to reduce future old-age poverty. Since entitlements to pensions are earnings related, the fiscal impact due to future entitlement would likely be small, yet a careful evaluation of any policy reform is necessary, in particular concerning any minimum entitlements. Health insurance coverage is already high even today, because free health insurance is easy to obtain by registering as unemployed. Any reform that would increase formal employment will therefore be fiscally favorable because no new entitlements are created while revenues are increased. At the same time, NES would profit from any reform that decreases its administrative burden stemming from free health insurance for the unemployed.

Conclusions

There are three main reform options to decrease informal employment and to activate the inactive: (1) to make formal work pay for low-wage earners, (2) to introduce mean testing for every entitlements to free health insurance or other municipal entitlements, and (3) to step up inspections and enforcement.

The two main policy tools to make formal work pay are to decrease labor taxation at the lower wage levels and to reform benefit design for social assistance and family benefits. With regard to lowering the tax wedge, the minimum social security contribution could be adjusted by actual hours worked. In other words, someone working half time at the legal minimum wage would also only pay 50% of the minimum social security contribution. This is the case in almost all EU and OECD countries and also in other countries in the region like Bosnia Herzegovina and Macedonia. Other options would be to introduce new policies like wage subsidies, social security contribution credits, or so-called in-work benefits (cash benefits conditional on formal work) for low-wage earners. These latter policies, though,

risk a certain amount of stigmatization for workers who benefit. Another way would be to channel these credits or subsidies to workers via the personal income tax as tax credits. A similar mechanism might have to be found for employers who hire low-wage earners.

With regard to reforming the design of social assistance and family benefits, the key is to keep the marginal effective tax rate in mind when designing benefit withdrawal. In other words, beneficiaries of social assistance and family benefits would gain from additional formal work—that is, any additional formal wage would also increase their net income, *including* benefits. If this is not the case, additional formal work does not pay, and beneficiaries will prefer to not work at all, or only informally, or underreport earnings. In order to reform benefits along these lines, withdrawal of benefit has to phase in slowly as income increases, so no sudden drops in net income occur. The German Hartz IV reforms offer a good example on how this can be achieved at lower wage levels.[10]

Entitlements to free health insurance could be limited to the poor, and the entitlement be based on a means test, not an income test. It is important that the poor have access to free health insurance as sickness is a serious economic risk that can further deepen poverty. Yet, if free health insurance is easily accessible also by those who can afford to contribute to health insurance, it decreases the value of formal work and increases incentives to work informally. It is therefore important to base the decision on who should have access to free health insurance on the means that a household has at its disposal and not formal income or formal employment status (like registered unemployment). This requires robust means-testing mechanisms as opposed to income testing. This can either be done by proxy means testing—like, for example, looking at electricity consumption—or by frequent contacts between a social worker and the applicant.

Finally, it might be advisable to step up labor and tax inspections. Macedonia FYR recently successfully implemented reforms along these lines. The amount of inspections, in particular of medium-sized companies in the service sector, has been increased significantly. At the same time, the maximum amount of penalties for violations was increased considerably. Although no rigorous impact evaluation is available on how inspections contributed, the number of people paying income tax and social security contributions increased by about 7% per year since 2006 (see Annex 1). More impressively, the number of people filing tax reports on nonwage income (like the self-employed) in Macedonia increased almost 13-fold within 3 years, from 20,000 in 2006 to 150,000 in 2009.

[10] Arguably, the role of social assistance in providing disincentives for formal work for a large number of people might be limited. About 170,000 people—including children and elderly—currently benefit from social assistance in Serbia, which is about 2.5% of the population, although the numbers have been increasing rapidly in recent months. In any case, as the social safety net of Serbia is being modernized, the disincentive effect and the marginal effective tax rate should be kept in mind.

Appendix

Table 9.8 Number of tax payers in contributors to social security in Bosnia and Herzegovina—Republika Srpska, Macedonia, and Serbia

	2006	2007	2008	2009	Average annual change (%)
Bosnia and Herzegovina—RS					
Number of registered payers of taxes and contributions	n.a.	974,976	1,121,126	1,197,456	10.9
Macedonia					
Number of registered contributors to pension fund	394,882	424,338	451,491	n.a.	6.9
Individuals filing tax reports on nonwage income	19,447	77,017	120,396	150,569	125.8
Serbia					
Number of registered payers of taxes and contributions	n.a.	2,188,503	2,229,236	2,162,145	–0.6

n.a. not available
Source: Administrative data

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Chapter 10
Not Just Education: The Gender Wage Gap in the Albanian Labor Markets Through Occupational Segregation, Work Experience, and Child Care

Juna Miluka

Introduction

The analysis of wage discrimination and for labor markets is a good reason and an enduring fashion in economics. Wage discrimination remains a persistent problem. In the context of a developing country such as Albania, labor market discrimination might have stronger and longer lasting impacts than elsewhere as it interacts with a number of other market imperfections. Understanding discrimination is especially important due to the impact that it may have on income inequality, the education of future generations (stemming from the expectations formed by parents), occupational distribution, women's position and opportunities, intergenerational inequality, and ultimately poverty. The lack of empirical studies focused on labor market issues in Albania makes this an even more topical issue to analyze.

Albania underwent major transformations as a result of the change from centralized planning to an open market economy. Those transformations were partly reflected in the labor market. Before 1990, the labor market was characterized by state controlled individual decision-making and a high degree of centralization. In the early 1990s, the labor market was liberalized. This new direction was associated with a period of high unemployment due to the closure of major industries and overcrowding in administrative jobs. Since the mid-1990s, there has been a considerable increase in private businesses mainly due to remittances from emigrants. However, the rate of long-term unemployment remains high, especially among women (Cuka et al. 2003).

The transitional period in Albania was characterized by wider changes, including the reintroduction of traditional law. Women were adversely affected by increased vulnerability in the labor market, and reduced economic status (Lawson and

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Saltmarshe 2000). State enterprises, which employed the majority of women, collapsed ending the social protection associated with the jobs they provided. In addition, market reforms increased earning inequalities through wage and price liberalizations and changed the characteristics of employment (The World Bank 2002). The unavailability of social protection and economic rights reinforced women's homemaking roles (Tarifa 1994). Consequently, women faced more work within the family, but less mobility and fewer chances to find jobs. With the state stopping child-care provision and long paid maternity leaves, women faced long-term structural discrimination in the labor market (Kligman 1996). With their reduced status and the additional burdens placed on them, women who were in lower occupation and were being paid less became an easily targeted group for discrimination.

Statistics from the Albanian Ministry of Labour and Social Affairs (AMoLSA) (2005) show that in 2004, employment levels were 38.3% for women and 60.1% for men, whereas unemployment was 17.5% for women and 12.4% for men. In terms of participation in the labor force, in 2003, 70.5% of men in the working age participated in the labor force compared to 46.7% for women (AMoLSA 2005). In 2004, labor force participation was 68.6% for men and 46.4% for women. Women overwhelmingly remain in the social-state-service sector, where they comprise 80% of employees (AMoLSA 2005). Men are working particularly in lawmaking, as senior officials, and as leading executives, while women are mostly found as specialists and regular employees (AMoLSA 2005). As a result of occupational segregation, women's wages are also lower than those of men even at equivalent (or higher) levels of education. In urban areas females attend universities more than men in part as a way to deal with the lower employment opportunities that they face in the labor market (The World Bank 2002).

The training curriculum also promotes occupational segregation as there is a tendency for vocational training for women to be in the traditional fields (AMoLSA 2005). Statistics from the AMoLSA show that in 2004 the vast majority of vocational training programs for females were concentrated in English, Italian, computer, secretary, sewing, and cosmetics. Only three courses offered skill training in trades, which makes it easier to find a job in the labor market. Furthermore, the educational curricula retain reproductive and gender stereotypes in the selection of the fields of study (AMoLSA 2005). In this way gender roles and occupational segregation are promoted, and a lack of career orientation related to the skills required in the labor (AMoLSA 2005).

Given that Albania had achieved almost universal literacy, high levels of women's education, high participation in the labor force, and extensive child care and maternal health during communism, it has often been difficult for policy makers to acknowledge the true position of women and recognize the burdens of paid and unpaid work. Yet failure to recognize that women might be in a less favorable position than men reinforces gender imbalances. This chapter draws on the literature and methodology of wage decompositions. It estimates the gender wage gap in Albania and identifies the different sources that account for the disparity.

Brief Literature Review

During communism wages, in almost all of the transition economies, were set according to the industry-specific wage grids responding only to worker's education and experience (Munich et al. 1999). There was a policy of full employment, and women enjoyed high education and health-care access (Munich et al. 1999). The fall of communism ended wage regulations, leading to increased returns to education and greater wage dispersion (Svejnar 1999). Different countries have experienced different levels of gender wage dispersion neglecting the skill composition, labor market institutions, and the history and culture of specific countries. Overall, during the early transition, the gender wage gap diminished in Eastern Europe, but increased in Russia and Ukraine (Brainerd 2000). During mid-transition, Newell and Reilley (2000) report that the gender wage gap remained relatively stable for most countries in the transition economies.

Human capital, work experience, occupational segregation, social norms, and household characteristics are all possible sources of the gender wage gap. As far as human capital is concerned, returns to education had more than doubled in Romania by 2000 compared to the levels under central planning (Andren et al. 2004). Skill-related wage differences generally rose in the transition economies following the political change (Svejnar 1999). In the case of Bulgaria, Giddings (2002) shows that the high levels of human capital that women had acquired during communism helped them in the transitional period by increasing their earning and improving their economic conditions. Similarly, women's higher levels of human capital helped reduce the gender wage gap in Russia (Oglobin 2005). In the case of Albania, as in many other transitional economies, the policies of the communist regime provided free education for all, full labor force participation, and a fairly small gender pay gap (Silova and Magno 2004). As a result of the high education levels inherited by women educated in the communist period, we would expect that human capital played no role (or perhaps even favored women) as far as the wage gap is concerned.

Work history and experience is also expected to affect the gender wage gap. Women have more home time than men due to the responsibilities of child bearing and parenting (Kunze 2000). They also have more interrupted work histories due to the family responsibilities (Kunze 2000). Since work experience is also one of the main components influencing wages, lower or interrupted work experience will be rewarded less by the market, thus influencing the gender wage gap.

With the fall of communism social support for child care, in Albania, suffered greatly. Day care was no longer provided by the transferring responsability to individuals. Since women are the main care providers, child bearing and parenting places additional demands on them. Thus, we would expect the lack of publically funded child care to reinforce the impact of the interrupted work experience of women and increase the gender wage gap.

Occupation segregation by industry or job status also contributes to the gender wage gap. Women comprise the majority of workers in the service occupations, while men are largely found in manufacturing jobs and industries (Kunze 2000). Differences in occupation generate differences in wages for two reasons. First, different occupations require different skills, and since some occupations reward

skills more than others, occupational segregation may increase the wage gap (Oglobin 1999). If women are segregated in the lower paying occupations, they will receive lower wages. Second, from simple supply and demand analysis, we know that if demand stays constant, but supply increases, prices will fall. If women are concentrated in certain occupations, then increased supply for those occupations can give employers some degree of monopsony power (Joshi and Paci 1998), to reduce wages. Jurajda (2003) finds that in the Czech Republic and Slovakia occupational segregation explained over one third of the gender wage gap. Similarly, Oglobin (1999) finds that gender differences in education and work experience are not enough to explain the gender wage gap in Russia. Here too it is occupation segregation which is the main determinant of gender disparity, accounting for 75–80% of the gender wage gap (Oglobin 1999). As a result of the similarities of labor market practices across the region, occupational segregation is expected to play a major role in most of the transition economies (Oglobin 1999). For example, in Albania women are mostly concentrated in the service industry and public administration (AMoLSA 2005).

Social norms may also affect the gender wage gap by promoting occupational segregation, by dictating certain gender roles, and influencing employers' preferences. In the case of the Czech Republic and Slovakia employers strongly preferred men to women in many occupations. In addition to the usual preference for men in maintenance and repair, employers also preferred male to female employers in professional, administrative, and service occupations. Overall, 36 to 58% of employers preferred males employees, while under 10% preferred women (Svejnar 1999).

Household decision making regarding labor market choices may override individual choices. Family and housework responsibilities are found to explain a large part of the unadjusted gender wage gap (Andren and Andren 2007). Women often make a choice regarding their occupation dictated by their household characteristics. Having children increases women's preference for participation in the public sector because it provides more flexibility (Gang et al. 2006). This also relates to the lack of social support for women in terms of day care and to the role of women as the main child-care providers. In the following section we explore how gender discrimination plays out in Albania, drawing on survey evidence.

Econometric Model

The data for our research is obtained from the 2005 ALSMS (Albanian Living Standard Measurement Survey study) conducted by INSTAT (Albanian Institute of Statistics) under the technical supervision of the World Bank. The 2005 ALSMS is a standard household survey. In addition to the usual household roster, community characteristics, food consumption, and other features, it includes a module providing information on labor force participation, hours worked, wages and types of jobs. The sample is stratified into four regions: coastal, central, mountain, and Tirana. It contains 3,680 households in which 5,540 individuals are of the ages 15 and above included in the labor module. A total of 1,829 of these individuals report no wages,

thus leaving the final sample with 3,703 individuals reporting wages. There are 1,111 females and 718 males in the labor module that report no wages. The average education of those that do not report any wages is of 8.13 years.

In this chapter, we use both the Oaxaca–Blinder (1973) and Lemieux (2002) methodologies to analyze the gender wage gap and its decomposition in the Albanian labor market. The Lemieux (2002) technique yields results which are easily interpreted and have economic meaning. It also goes beyond the decomposition of means to decomposing wages and wage dispersion over the full distributional case, and models residuals as the pricing of unmeasured skills, rather than as the unexplained part of the regression (Lemieux 2002).

Oaxaca–Blinder Decomposition

Following Oaxaca–Blinder (1973), the wage differential between two groups, males vs. females in our specific case, may be decomposed into (1) the proportion of the differential attributed to the shift of the coefficients $b_0^{\mathrm{f}} - b_0^{\mathrm{m}}$, which is typically regarded as pure discrimination, or the rent of being of a specific sex; (2) the explained part attributed to the differences in the coefficients b_i^{f} and b_i^{m} and the differences in the average characteristics or endowments $\overline{X}^{\mathrm{F}}$ and $\overline{X}^{\mathrm{M}}$; and (3) the unexplained or interaction between the coefficients and the average characteristics. Thus, stemming from the[1] basic equation used in this analysis, the human capital earnings function from Mincer (1974),

$$\ln w = c + rS + b_1 E + b_2 E^2 + e, \tag{10.1}$$

where w is hourly wage, c is a constant, S is years of schooling, E is years of experience in the labor market, and e is the error term—we can write the raw wage differential as

$$R = b_0^{\mathrm{f}} + \sum\nolimits_i b_i^{\mathrm{f}} \overline{X}_i^{\mathrm{F}} - (b_0^{\mathrm{m}} + \sum\nolimits_i b_i^{\mathrm{m}} b_i^{\mathrm{m}} \overline{X}_i^{\mathrm{M}}) = E + C + U, \tag{10.2}$$

where E = portion of differential attributed to differences in endowments

$$E = \sum\nolimits_i b_i^{\mathrm{f}} (\overline{X}_i^{\mathrm{F}} - \overline{X}_i^{\mathrm{M}}), \tag{10.3}$$

C = portion of differential attributed to changes in coefficients

$$C = \sum\nolimits_i \overline{X}_i^{\mathrm{M}} (b_i^{\mathrm{f}} - b_i^{\mathrm{m}}), \tag{10.4}$$

[1] The notation used in this section derives mainly from Lemieux (2002).

U = the unexplained portion of the differential due to the shifts in the coefficients $b_0^{\mathrm{f}} - b_0^{\mathrm{m}}$, and D = portion of the differential attributed to discrimination = $C + U$.

Lemieux Decomposition

Following Lemieux (2002), and using standard OLS regressions augmented by a probit model, the gender wag gap is decomposed into (1) changes in the regression coefficients, (2) changes in the distribution of the covariates, and (3) changes in the residuals, which are modeled as a function of unmeasured skills and skill prices. More specifically, in this approach, we create counterfactual wages controlling for (1) changes in prices, b; (2) changes in endowments, x; and (3) changes in unobservable, u. The first step is to run separate OLS regressions for males and females. Keeping the same endowments and error terms from the female regression, we create female counterfactual wage regressions, using the b's from the male regression. This way we can see what the female wage equation would look like if females were paid according to male wages. After controlling for changes in the price of skills, we can control for changes in endowments by creating a female counterfactual wage that keeps the b's from the female wage equation, but that gives females the endowments, x, from the male wage equation. Thus, we can see how the average wages for females would change, if they were to be paid according to the female wage equation, but having the endowments of men. In order to assign to females the average endowments of males, we run a probit equation on the entire sample of being male (using as many controls as possible) and use the propensity score to weight the female wage equation. Below we formally present the above summary of the methodology used.

Decomposition of Wages Through Changes in the Regression Coefficients

Referring to the previously mentioned wage equation from Mincer (1974),

$$\ln w = c + rS + b_1 E + b_2 E^2 + e, \tag{10.1}$$

where w is hourly wage, c is a constant, S is years of schooling, E is years of experience in the labor market, and e is the error term; let us consider a more general form of the above equation:

$$y_{i\mathrm{f}} = x_{i\mathrm{f}} \beta_{\mathrm{f}} + e_{i\mathrm{f}}, \tag{10.5}$$

where i is an indicator for each individual and f stands for female (a regression equation for females), $x_{i\mathrm{f}}$ is a $1 \times k$ vector of covariates (including a constant), β_{f} is a $k \times 1$ vector of parameters, and $e_{i\mathrm{f}}$ assumed to have $E(e_{i\mathrm{f}} | x_{i\mathrm{f}}) = 0$. In terms of our wage

equation, y_{if} is the log hourly wages for females; x_{if} is a vector of human capital and other control variables. The OLS estimated regression equation is

$$y_{if} = x_{if} b_{\mathrm{f}} + u_{if}, \tag{10.6}$$

where u_{if} is the regression residual, which by construction is uncorrelated with the covariates and has a mean of zero.

The sample average of y for females is

$$\overline{y}_{\mathrm{f}} = \overline{x}_{\mathrm{f}} b_{\mathrm{f}}, \tag{10.7}$$

where $y_{\mathrm{f}} = \sum_i \overline{y}_{if}$; $x_{\mathrm{f}} = \sum_i \overline{x}_{if}$. Consequently, we can apply the same equation to the earnings of males, in which case we would have a sample average of

$$\overline{y}_{\mathrm{m}} = \overline{x}_{\mathrm{m}} b_{\mathrm{m}}, \tag{10.8}$$

where *m* stand for male. Stemming from Oaxaca (1973) and Blinder (1973), we can decompose these changes in means as

$$\overline{y}_{\mathrm{f}} - \overline{y}_{\mathrm{m}} = \overline{x}_{\mathrm{f}} (b_{\mathrm{f}} - b_{\mathrm{m}}) + (\overline{x}_{\mathrm{f}} - \overline{x}_{\mathrm{m}}) b_{\mathrm{m}}, \tag{10.9}$$

where the first term on the right is the difference in the estimated parameters and the second term is the difference in the mean values of the covariates between females and males. Another way of interpretation is that $\overline{x}_{\mathrm{f}} b_{\mathrm{m}}$ represents a counterfactual value of *y* that would be obtained if the parameters for females were replaced by the parameters of males. Going back to the wage equation, it represents the average wage for females if the returns to human capital were the same as those of males.

This counterfactual can be written as

$$\overline{y}_{\mathrm{f}}^{a} = \overline{x}_{\mathrm{f}} b_{\mathrm{m}} \tag{10.10}$$

and it can be used to rewrite the decomposition of the difference between the average value of *y* for females and males, such as

$$\overline{y}_{\mathrm{f}} - \overline{y}_{\mathrm{m}} = (\overline{x}_{\mathrm{f}} b_{\mathrm{f}} - \overline{y}_{\mathrm{f}}^{a}) + (\overline{y}_{\mathrm{f}}^{a} - \overline{x}_{\mathrm{m}} b_{\mathrm{m}}) = (\overline{y}_{\mathrm{f}} - \overline{y}_{\mathrm{f}}^{a}) + (\overline{y}_{\mathrm{f}}^{a} - \overline{y}_{\mathrm{m}}) \tag{10.11}$$

The individual-specific counterfactual wage

$$y_{if}^{a} = x_{if} b_{\mathrm{m}} + u_{if} = y_{if} + x_{if} (b_{\mathrm{m}} - b_{\mathrm{f}}) \tag{10.12}$$

can be computed either by obtaining the sample average of x_{if} and applying $\overline{y}_{\mathrm{f}}^{a} = \overline{x}_{\mathrm{f}} b_{\mathrm{m}}$ or by computing directly the sample average of

$$\overline{y}_{if}^{a} = \sum \omega_{if} y_{if}^{a} \tag{10.13}$$

Decomposition of Wages Through the Distribution of Covariates

The decomposition of wages through the distribution of covariates may be achieved by constructing a counterfactual weight ψ_i, which yields the distribution statistic that would have existed if the distribution of x for the females had the same distribution as males. The main idea behind this type of decomposition rests in the estimation of a probit model in order to compute the reweighting factor ψ_i. The reweighting factor ψ_i is constructed by pooling together the male and female samples and estimating a probit model for the probability of being male. Conditional on x the estimated probit model estimates the predicted probability of being a male. We can denote the predicted probability as

$$P_{if} = \mathrm{Prob}(\mathrm{sex} = \mathrm{male} \mid x_{if}) \text{ and the re} - \text{weighting factor as} \tag{10.14}$$

$$\psi_i = [(1 - P_{if}) / P_{if}] \times [P_t / (1 - P_t)], \tag{10.15}$$

where P_t is the unconditional probability that an observation is male. This procedure has the advantage of not suffering from the dimensionality problem of a cell-by-cell procedure, and it can incorporate several controls by including various independent variables in the probit model. In this context the distribution of females with the distribution of covariates of males can be obtained by weighting y_{if} by ψ_i.

There is no agreement in the literature on the inclusion of control variables in the wage regression (Kunze 2000), leaving them to the discretion of the researcher and to the question that needs to be answered. In addition to the standard education and experience variables, we also include additional control variables. The number of children and the person's marital status are included because they may serve as a measure of the effect of women's double burden on their wages. The lack of social support and state-provided child care makes women the primary care givers of their children. Thus, the number of children reflects the cost of lost experience for women (Grimshaw and Rubery 2002). A married women with children might be viewed from the employer as less productive, since she might need more time off work. As a result, the employer might offer women lower wages. On the other hand, a married man might be regarded as more stable and dedicated to work since it is the wife that is expected to take care of the household. Married men may also just receive preferential treatment (Weichselbaumer and Winter-Ebmer 2005). The distance index and

social capital index are included to control for the costs or benefits of social support. Women who live in areas with adequate transportation and have social capital that facilitates child rearing might be more productive and mobile. We control for the percentage of females in each occupation as to control for occupational segregation. This variable has been widely used in the literature to capture female occupational segregation (Jurajda and Harmgart 2007; Andren and Andren 2007). Lastly, we control for regional differences, which can play a role in terms of market segmentation and supply side, as well as social, economic, and cultural aspects.

Results

The Oaxaca decomposition results over the entire group of workers show that the principal sources of the gender wage gap are education, work experience, occupational segregation, and number of children. In Table 10.1, the wage differential between males and females is decomposed into three parts accounting for (1) differences in endowments, (2) differences in coefficients, and (3) the interaction between endowments and coefficients. The total difference in endowments is insignificant.

This result is in accordance with the fact that women have on average more education than men presently in the labor market. As found in other transitional economies with high levels of education for women, differences in endowments do not contribute to the gender wage gap. The total difference in the regression coefficients between females and males, which account for the largest part of the decomposition, favors males (–0.510). The difference in coefficients is interpreted as a form of discrimination applied by the market in offering different rewards for the same skills. It means that given women's endowments, the difference between what they are actually paid and what they would get paid if given the male wage structure is negative, indicating a superior wage structure for males. If women were paid men's wages for their endowments, they would get paid more. Lastly, the interaction between endowments and coefficients, which is referred to as the unknown part of the regression, favors women.

The positive values of education in the detailed decomposition for endowments, coefficients, and interaction indicate that the higher levels of education for women give them an advantage. However, education is not enough to make up for the other sources which negatively affect their wage structure. An important variable that accounts for a large part of the differential in wages is experience. Women have on average less experience than men, which is associated with the fact that women take time off for child bearing and rearing. This is negatively rewarded by the labor market putting women at a disadvantage in the economic ladder. The impact of having children is negative and is another major factor putting women at a disadvantage. If there is lack of social support and child-care possibilities, then having children is associated with a discontinuity of participation in employment, a decrease of the stock of human capital, and therefore lower rewards in the labor market. As elsewhere in the literature, occupation segregation for women is also

Table 10.1 Oaxaca decomposition

Variables	Endowments	Coefficients	Interaction
Education	0.036	0.450	0.031
	(0.007)***	(0.088)***	(0.008)***
Experience	−0.055	−0.328	0.048
	(0.021)***	(0.198)*	(0.030)
Experience 2	0.069	0.339	−0.083
	(0.019)***	(0.117)***	(0.030)***
Occupation	−0.051	0.085	0.016
	(0.007)***	(0.052)	(0.010)
Distance index	0.001	0.01	0.010
	(0.002)	(0.004)***	(0.004)**
Social capital	0.000	0.002	0.000
	(0.001)	(0.003)	(0.001)
Number of children	−0.002	−0.13	0.010
	(0.002)	(0.039)***	(0.004)**
Married	−0.005	−0.007	0.001
	(0.005)	(0.068)	(0.007)
Divorced	−0.002	0.000	0.001
	(0.004)	(0.001)	(0.004)
Living together	0.000	0.001	0.000
	0.000	(0.001)	(0.001)
Widow	−0.005	0.002	0.008
	(0.006)	(0.001)	(0.007)
Coastal	0.002	0.004	0.000
	(0.003)	(0.018)	(0.001)
Central	0.009	0.003	0.000
	(0.004)**	(0.017)	(0.003)
Mountain	−0.005	0.022	0.001
	(0.006)	(0.017)	(0.002)
Urban	0.016	0.078	0.016
	(0.005)***	(0.034)**	(0.007)**
Constant		−1.042	
		(0.148)***	
Total	0.008	−0.510	0.059
	(0.017)	(0.026)***	(0.020)***
Observations	3,703		

Standard errors in parentheses. * significant at 10%; ** significant at 5%; *** significant at 1%
(+) indicates an advantage for females, (−) indicates an advantage for males

found to have a large impact in widening the gender wage gap in Albania, possibly through crowding of women in certain occupations and lower wages. Lastly, the shift in the constant term (−1.042), which is usually attributed to pure discrimination in the labor market (Blinder 1973) or else as pure premium of being a specific sex, largely favors males.

As would be expected, the decomposition for the highly skilled workers (holding university degrees and above) shows a smaller gender wage gap (−0.309), Table 10.2. Differences in the coefficients explain the gender wage gap mainly through the

Table 10.2 Oaxaca decomposition for higher education

Variables	Endowments	Coefficients	Interaction
Education	–0.011	–1.720	0.011
	(0.008)	(0.913)*	(0.009)
Experience	–0.239	–0.391	0.124
	(0.120)**	(0.445)	(0.142)
Experience 2	0.2	0.164	–0.075
	(0.102)**	(0.286)	(0.131)
Occupation	–0.03	0.028	0.006
	(0.015)**	(0.106)	(0.021)
Distance index	0.006	0.019	0.006
	(0.007)	(0.034)	(0.010)
Social capital	–0.008	–0.021	0.006
	(0.008)	(0.014)	(0.007)
Number of children	0.000	–0.094	0.005
	(0.003)	(0.074)	(0.007)
Married	0.059	0.295	–0.062
	(0.029)**	(0.145)**	(0.033)*
Divorced	0.000	0.000	0.000
	0.000	0.000	(0.002)
Living together	0.000	0.003	0.001
	(0.001)	(0.004)	(0.003)
Widow	–0.001	0.001	0.000
	(0.002)	(0.005)	(0.002)
Coastal	–0.007	0.026	0.003
	(0.011)	(0.023)	(0.005)
Central	–0.002	0.024	0.001
	(0.013)	(0.024)	(0.004)
Mountain	0.009	0.036	–0.003
	(0.016)	(0.026)	(0.006)
Urban	0.009	–0.029	–0.001
	(0.007)	(0.126)	(0.005)
Constant		1.343	
		(0.934)	
Total	–0.015	–0.315	0.020
	(0.040)	(0.054)***	(0.046)
Observations	589		

Standard errors in parentheses. * significant at 10%; ** significant at 5%; *** significant at 1%
(+) indicates an advantage for females, (–) indicates an advantage for males

different rewards of education, while differences in endowments and interactions are insignificant. Work experience and occupational segregation remain important sources of the gender wage gap in the endowment differences, but they lose significance in the coefficient differences. Unlike the overall decomposition, the number of children is not significant, and being married has a positive effect. In the case of highly educated workers, it might be easier to overcome the lack of state support in child care. Highly educated women are less vulnerable to taking time off from the labor markets since they might have better means of support. In the case of

Table 10.3 Oaxaca decomposition for lower education

Variables	Endowments	Coefficients	Interaction
Education	0.007	0.407	0.010
	(0.003)**	(0.118)***	(0.005)**
Experience	–0.041	–0.19	0.018
	(0.016)**	(0.244)	(0.023)
Experience2	0.060	0.281	–0.05
	(0.017)***	(0.142)**	(0.027)*
Occupation	–0.056	0.088	0.014
	(0.008)***	(0.064)	(0.010)
Distance index	0.001	0.006	0.007
	(0.001)	(0.003)**	(0.004)*
Social capital	0.000	0.004	0.000
	0.000	(0.003)	(0.001)
Number of children	–0.002	–0.128	0.006
	(0.002)	(0.045)***	(0.004)*
Married	–0.005	–0.014	0.001
	(0.004)	(0.082)	(0.005)
Divorced	–0.002	0.000	0.001
	(0.005)	(0.001)	(0.005)
Living together	0.000	0.000	0.000
	(0.001)	(0.001)	0.000
Widow	–0.009	0.002	0.014
	(0.009)	(0.001)	(0.010)
Coastal	0.001	–0.013	0.000
	(0.002)	(0.023)	(0.001)
Central	0.006	–0.01	0.002
	(0.003)**	(0.021)	(0.004)
Mountain	–0.009	0.009	0.001
	(0.006)	(0.021)	(0.002)
Urban	0.012	0.073	0.014
	(0.005)***	(0.036)**	(0.008)*
Constant		–1.054	
		(0.186)***	
Total	–0.037	–0.540	0.038
	(0.018)**	(0.029)***	(0.022)*
Observations	3114		

Standard errors in parentheses. * significant at 10%; ** significant at 5%; *** significant at 1%
(+) indicates an advantage for females, (–) indicates an advantage for males

highly skilled workers, markets seem to be less discriminatory as indicated by the loss in significance of the constant term.

Less educated workers display the largest gender wage gap (–0.539). Table 10.3 shows the largest constant term shift (–1.054), and unlike the previous results, differences in endowments favor men. The males in the lower education workers continue to obtain a superior wage structure. The negative impact of occupational segregation and number of children is the largest for this group. This means that women with less education suffer larger discrimination in the labor market. They are more likely to

Table 10.4 Log wage distribution of females and males in Albania

	Mean	Variance	
		Total	Predicted *xb*	Residual
	(1)	(2)	(3)	(4)
1. Female	9.525	0.559	0.244	0.315
2. Female with male *b*'s	9.977	0.432	0.117	0.315
3. Female with male *b*'s and *X*'s	9.893	2.132	0.095	2.037
4. Male	9.969	0.591	0.120	0.471
5. Female–male difference	–0.444	–0.032	0.124	–0.156
Effect of				
6. *b* (row 1–row 2)	–0.452	0.127	0.127	0.000
7. *x* (row 2–row 3)	0.084	–1.700	0.022	–1.722
8. Residual (row 3–row 4)	–0.076	1.541	–0.025	1.566

suffer occupational segregation and more vulnerable to staying out of the labor market for longer periods due to child-care responsibilities. The increased magnitude with which occupational segregation and child care affect women with education reduces their wages and further increases the gender wage gap. For the low education group as for the overall sample, the distance index matters for the difference in the coefficients, suggesting the importance of mobility.

Turning to Lemieux (2002) decomposition, from Table 10.4, column 1, the mean log wage difference between males and females in Albania is –0.444, which means that females earn approximately 36%[2] less than males. From column 2, we see that females have lower wage variance due to lower residual wage variance. The predicted variance is higher for females, suggesting higher between-group inequalities. However, the residual variance of wages is higher for males, suggesting larger within group inequalities. Unlike other cases where women have both lower returns to their skills and lower human capital, in Albania, women receive lower prices for their human capital, but they are relatively more educated than men. This produces a more compact distribution of covariates than men. Women in Albania are thus in the low wage/low dispersion, while males are the high wage/high dispersion.

The results from the counterfactual analysis are given in rows 6, 7, and 8 of Table 10.4. As in the Oaxaca–Blinder (1973) decomposition, most of the –0.444 wage gap between the groups is explained by the changes in the regression coefficients (row 6). The variance in row 7 column 2 has a negative sign, driven by the larger negative difference in the residual variance of covariates. This is consistent with human capital theory, which states that residual wage dispersion should increase when the price to human capital increases. Therefore, if males receive higher returns to their measured human capital, the dispersion of their unmeasured human capital is also expected to be higher.

Tables 10.5 and 10.6 show the Lemieux (2002) decomposition for high- and low-educated workers, respectively. As we saw in the Oaxaca (1973) decomposition, the

[2] This number is calculated by taking the exponential of the mean log wage difference between females and males, subtracting 1, and multiplying by 100 to get the percentage value.

Table 10.5 Log wage distribution for the highly educated

	Mean		Variance	
		Total	Predicted *xb*	Residual
	(1)	(2)	(3)	(4)
1. Female	10.114	0.225	0.044	0.181
2. Female with male *b*'s	10.408	0.282	0.101	0.181
3. Female with male *b*'s and *X*'s	10.411	0.317	0.096	0.221
4. Male	10.423	0.435	0.098	0.337
5. Female–male difference	–0.309	–0.210	–0.054	–0.156
Effect of				
6. *b* (row 1–row 2)	–0.294	–0.057	–0.057	0.000
7. *x* (row 2–row 3)	–0.003	–0.035	0.005	–0.040
8. Residual (row 3–row 4)	–0.012	–0.118	–0.002	–0.116

Table 10.6 Log wage distribution for the low educated

	Mean		Variance	
		Total	Predicted *xb*	Residual
	(1)	(2)	(3)	(4)
1. Female	9.361	0.529	0.186	0.343
2. Female with male *b*'s	9.863	0.446	0.103	0.343
3. Female with Male *b*'s and *X*'s	9.747	2.035	0.095	1.940
4. Male	9.900	0.579	0.102	0.477
5. Female–male difference	–0.539	–0.050	0.084	–0.134
6. *b* (row 1–row 2)	–0.502	0.083	0.083	0.000
7. *x* (row 2–row 3)	0.116	–1.589	0.008	–1.597
8. Residual (row 3–row 4)	–0.153	1.456	–0.007	1.463

differences in the coefficients account for the majority of the gender wage gap. With the reduction of the gender wage gap, the wage dispersion also decreases. Women in the highly educated group have lower wage variance than in the case of all workers. Unlike the results in Table 10.4, the predicted and residual variance for highly educated females is lower than that of highly educated males, suggesting lower between-and within-group inequalities. For the lower educated group, as in the case of the Oaxaca (1973) decomposition, the majority of the gap is explained by differences in the coefficients. In addition, the differences in endowments also explain some of the gender wage gap. The increase in the gender wage gap for this group is associated with a larger wage dispersion. The total and predicted wage variance for females is larger in the low education group than in the high education group. The same is true for males. As in the overall case, women have higher predicted variance indicating higher between group inequality and lower within group inequality.

From Fig. 10.1, we can also see that the two wage distributions have quite different shapes. Visually, the gap between the two densities is the gender wage gap, which is much larger on the left-hand side and middle of the distribution. The gender wage gap starts to shrink on the right-hand side of the distribution, and it vanishes for the

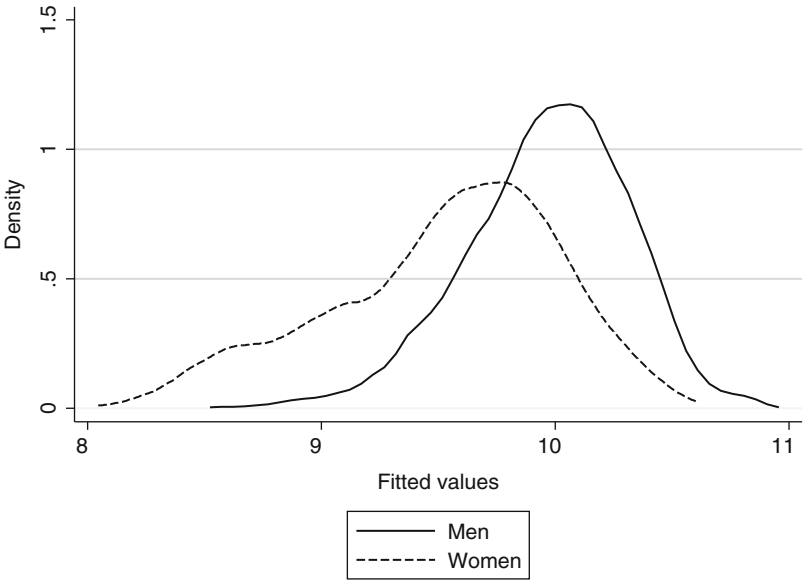

Fig. 10.1 Kernel density estimates of predicted Ln monthly wage by gender

top-skilled individuals, suggesting that wages for the highest-skilled women are similar to wages for highest-skilled men.

As Fig. 10.2 shows, when females are given the regression coefficients of the males, the two distributions look almost identical, and the gender wage gap gets significantly reduced. Thus, it suggests that the *b*'s account for most of the gender wage gap.

When females are given the covariates of the males as in Fig. 10.3, their wage distribution becomes trimodal. This suggests that, if women were given the covariates of males and were paid according to their wage structure, they would score even lower. In this case females would have lower *b*'s and lower covariates. When we look at Fig. 10.4, where females get both the *b*'s and the covariates of the males, the figure looks closer to Fig. 10.2, where only the *b*'s are of the males. This finding suggests that the differences in the distribution of the covariates have a small impact on the wage distribution. This is in line with the earlier findings from the Oaxaca–Blinder (1973) decomposition, which showed that women's covariates are not enough to make up for the differences in the wage distribution.

From Figs. 10.5, 10.6, and 10.7, we see that in the highest education groups, the gender wage gap decreases. This is indicated by the lower gap in the two distributions. In the case of the highly educated workers, since they share very similar levels of education, the two distributions look very alike in the case when females are given the *b*'s of males and in the case when females are given both the returns and covariates of males.

Lastly, in Figs. 10.8, 10.9, and 10.10, for the low education group, we see that the *b*'s account for most of the differences in distribution. When females are given

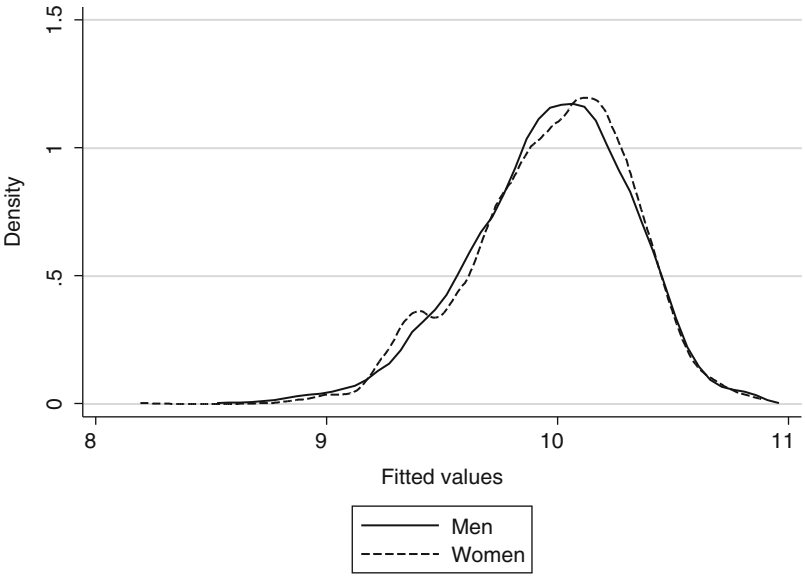

Fig. 10.2 Females with males' regression coefficients

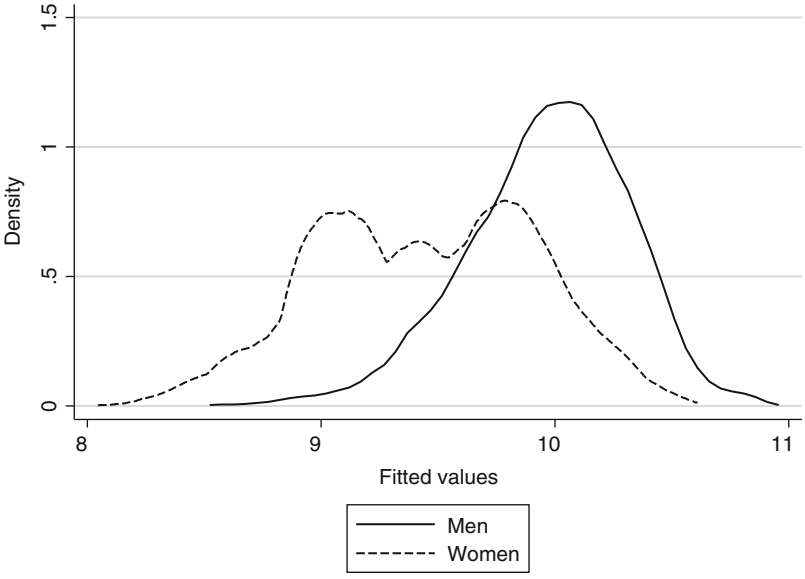

Fig. 10.3 Females with males' covariates

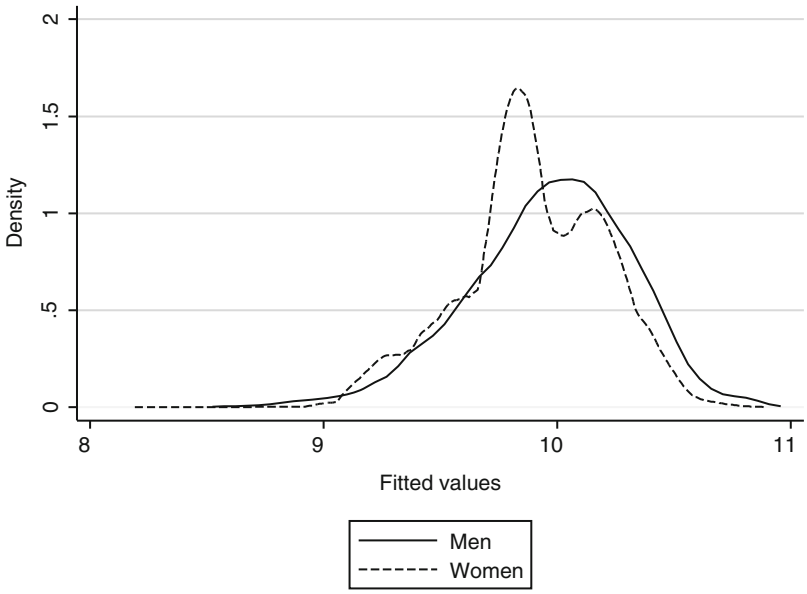

Fig. 10.4 Females with males' *b*'s and covariate distribution

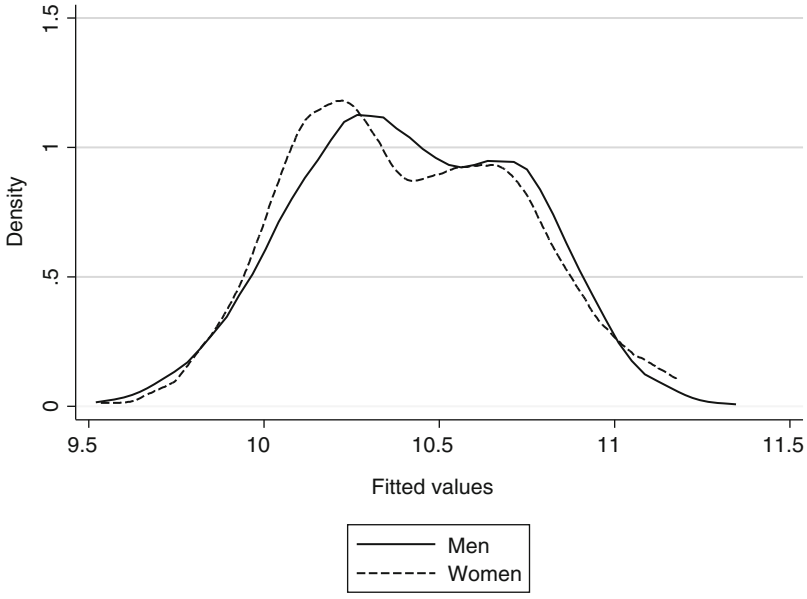

Fig. 10.5 High education females with males' regression coefficients

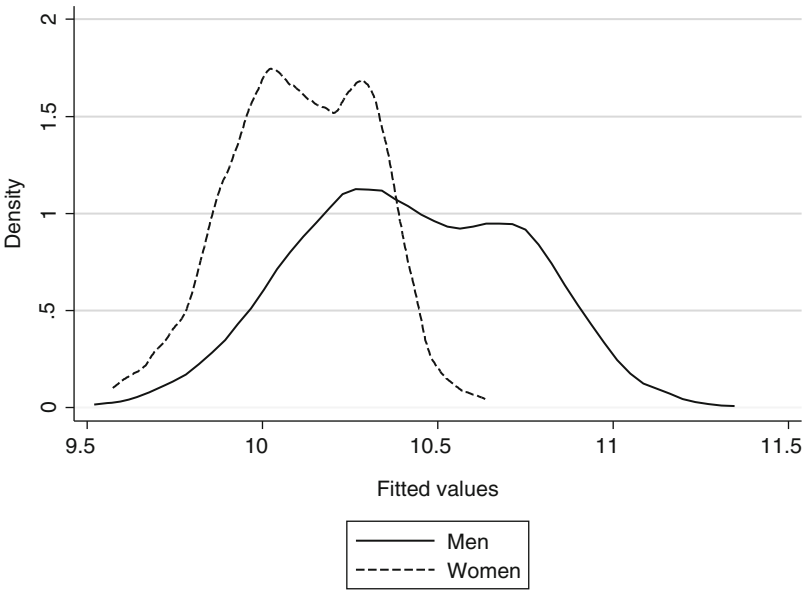

Fig. 10.6 High education females with males' covariates

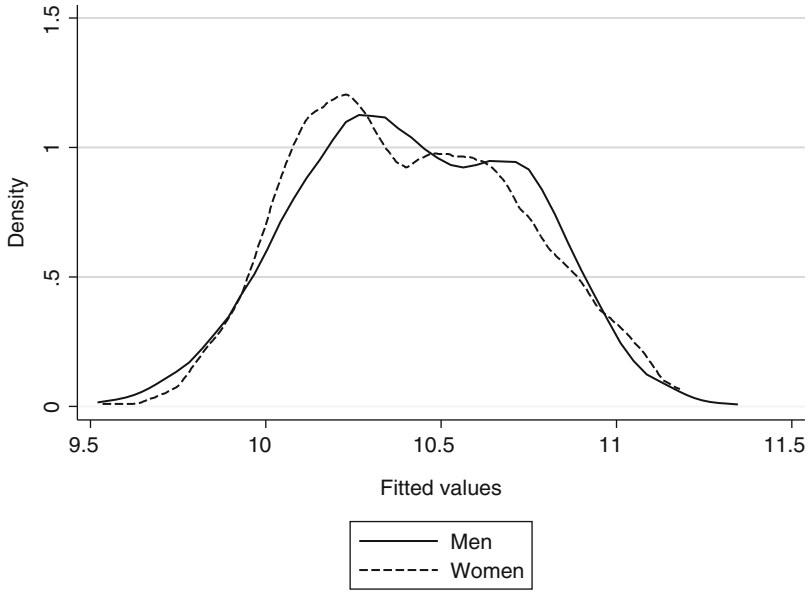

Fig. 10.7 High education females with males' *b*'s and covariate distribution

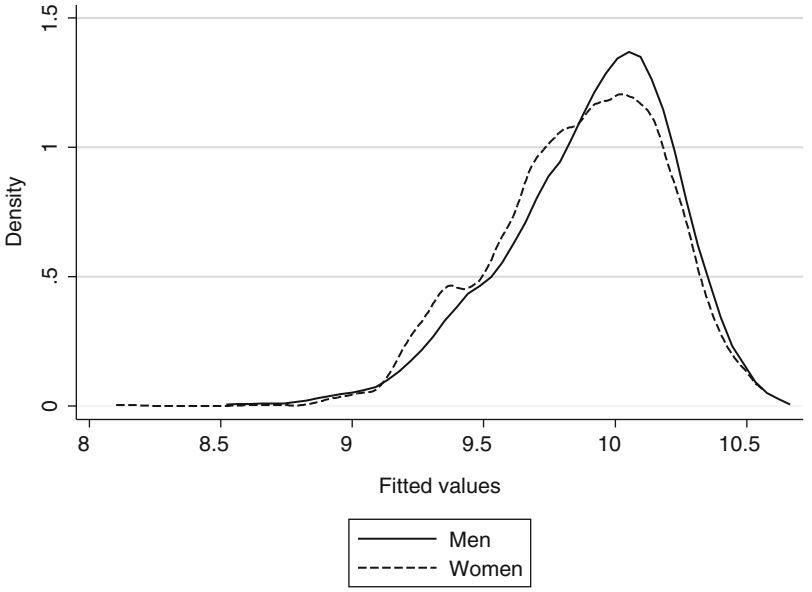

Fig. 10.8 Low education females with males' regression coefficients

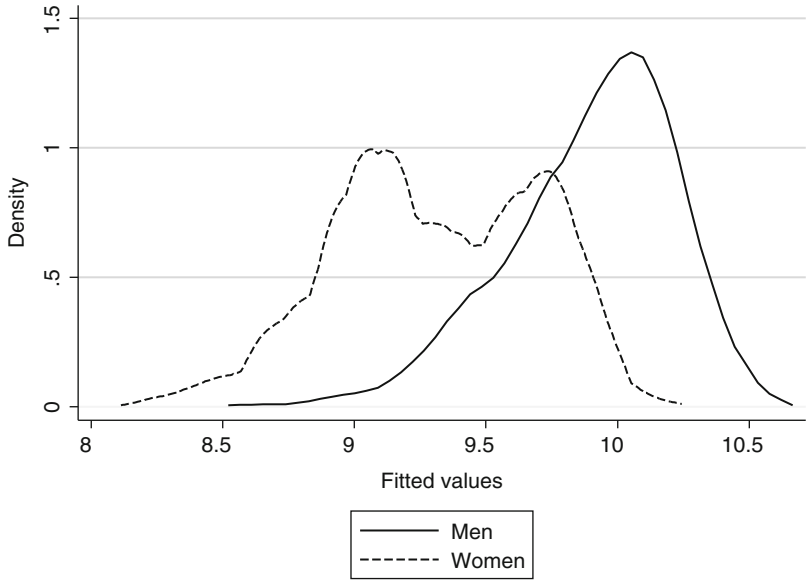

Fig. 10.9 Low education females with males' covariates

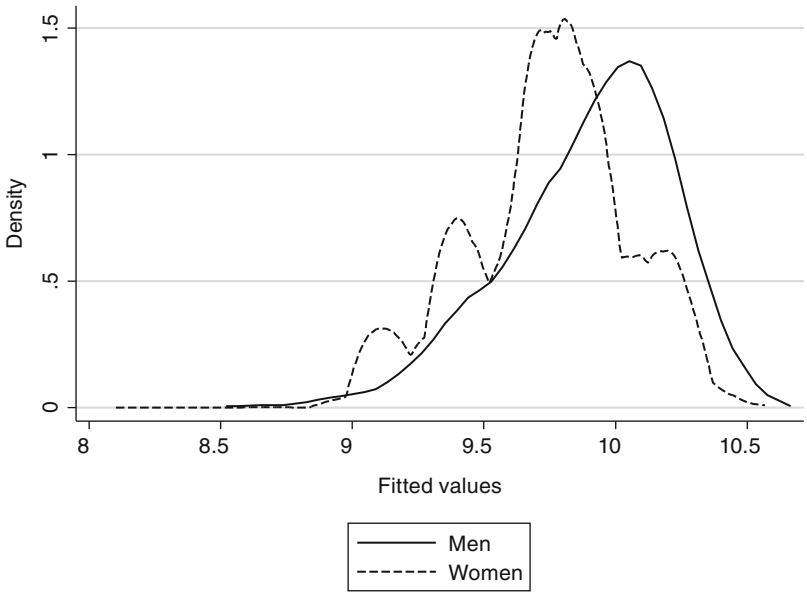

Fig. 10.10 Low education females with males' *b*'s and covariate distribution

the *b*'s of males, the wage distributions are very similar, whereas when females have only the covariates of males, their wage distribution becomes bimodal. In this case they would get even lower mean wages. Giving less-educated females both the *b*'s and covariates of males reduces their mean wages. Lower endowments put them at a further disadvantage, for which the increased *b*'s are not enough to make up for the difference.

Conclusions

This chapter provides a detailed account of the decomposition of the wage gap between men and women in the Albanian labor market using two different estimation methodologies. Using 2005 Albanian Living Standard Measurement Survey (2005 ALSMS) data, both the Oaxaca–Blinder (1973) and Lemieux (2002) wage decomposition techniques show the existence of pure labor market discrimination through a pure rent of being male. The majority of the gender wage gap is accounted for by the different rewards provided by the labor market. Overall, the different rewards provided by the labor market, the pure rent of being male, experience loss, occupational segregation, and child care, all reduce women's wages and put them at a disadvantageous position.

The results of wage decomposition in Albania share similarities with other countries in the region. As in the case of Russia and Ukraine, the gender wage gap in

Albania favors men, and occupational segregation plays an important role in increasing the gender wage gap. Education is not enough to give women in Albania an overall wage advantage as it did in Bulgaria. However, high levels of women's education help reduce the gender wage gap. The main implication of the decomposition results is that factors other than education, such as occupational segregation, less work experience—as a result of discontinued experiences in the labor market—and child care account for the bulk of the gender wage gap. Women who are currently in labor markets, the majority of whom have been educated during the communist period, have on average more education that men. If women kept their current endowments, and were paid according to the wage structure of men, their average wages would score higher than that of males reflecting their education advantage. Conversely, if their education levels decreased and were the same as those of males, they would earn even less than they do now.

Consequently, there are three main messages that come out of this chapter. First, education is key and should be given special consideration by the policy makers. However, other important factors such as occupational segregation, work experience, and child care also play a crucial role. Second, although education is not enough to make up for the gender wage gap, were education levels among females to decrease, the gender wage gap would be increased even further. Third, the problem is greatest for the low-educated group who seem to experience higher levels of labor market discrimination.

Policy makers should concentrate on designing policies that fight gender segregation and offer equal pay for equal work. In order to prevent occupational segregation, it is important that policies are designed not only for the labor market but also for the educational system. Curriculum reform should aim at broadening occupational choices for women occupation. In addition, equal pay for equal work policies should be designed in conjunction with policies for affirmative action to promote the hiring of women in fields which are predominantly male. As is the case with many transition economies, there is often a mismatch between skills and occupations. Policies should be designed such that they match women's skills and education with the appropriate occupation. Lastly, to alleviate the loss of experience and discontinuity in the labor market as a result of child bearing and parenting, policies should be designed to share either child-care responsibilities between both males and females, or to deliver better provision for child care.

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Chapter 11
Internal Migration in Albania and the Changes in Transfers Received from Family and Friends: A Study of Internal Migrants in Peri-Urban Tirana

Florian Tomini and Jessica Hagen-Zanker

Introduction

Kinship and friendship networks provide their members with continuous economic, social and emotional support both in everyday life and in the case of sudden or unforeseen events. As migration relocates family members, divides families and exposes migrants to new people and different cultural practices, it is also likely to affect the support received by family and friends. Migration can therefore be a serious threat to the support and security provided by kinship and friendship networks. Two important questions which help assess to which extent this is true are as follows: How would the composition and frequency of transfers received by relatives and friends change after migration? And would transfers from friends substitute transfers from family relatives?

This study examines the impact of internal migration to peri-urban areas of the capital of Albania (Tirana) on the composition and frequency of transfers received from family and friends. The data comes from a unique household survey that was conducted in 2008 and focused on migrants that moved to peri-urban areas of Tirana after the fall of communism. We analyse how internal migration of the households has affected the different transfers received and to what extent transfers from friends substitute for transfers from family members after migration. We focus in particular on transfers of money, goods and services received by the household. Based on the

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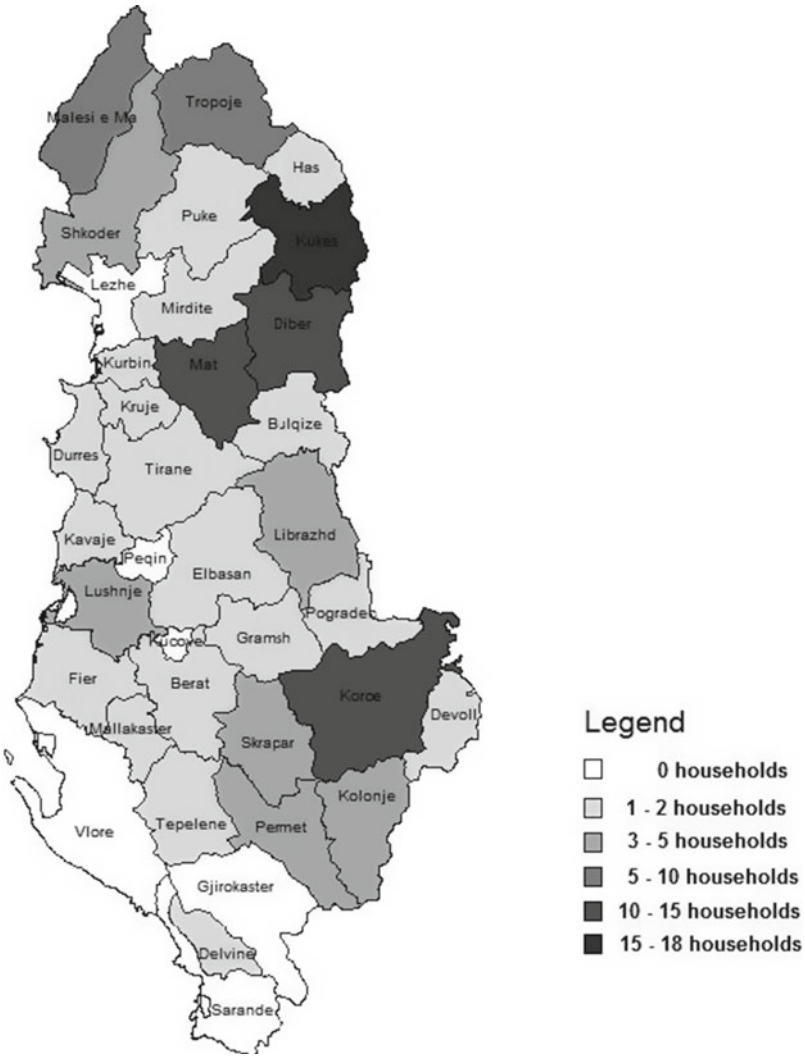

Fig. 11.1 Origin districts of surveyed households (*source*: own compilation)

literature in the field and Albania's particular migration dynamics, we test two hypotheses (1) Financial transfers have become more frequent after migration. (2) After migration, households substitute transfers from family members with transfers from non-family members (such as friends and neighbours).

The household survey was conducted in 2008 amongst internal migrant households living in peri-urban households in Tirana. It covers two types of households: nuclear households (two generation households including parents and children) and extended families (three or more generation households, multiple couple households and/or other relatives living together). Figure 11.1 depicts a map of Albania

marking the districts of origin of the surveyed households. It shows that migrant households come from nearly all districts, but especially from the northern and central mountainous areas (the darker areas on the map).

The present study relates both to the economic analysis of inter-household transfers and the impact of internal migration. It follows a number of studies (Blumberg and Bell 1959; Litwak 1960; Jitodai 1963; Bengtson and Roberts 1991) combining the two research areas. Research focusing on the impact of internal migration on transfers in the case of complete family relocation remains limited. Much of the available literature focuses on demographic changes in the United States in the mid-twentieth century. In terms of methodology, we use both qualitative interviews and econometric techniques. Furthermore, we focus on a transition economy where the role of private transfers is much more important than in more advanced market economies. Internal migration is high in Albania, poverty in peri-urban areas remains widespread, and state support is low. This makes the investigation of private transfers and their development over time an interesting and policy relevant research question.

Internal Migration in Albania

Internal migration in Albania during the communist regime (1945–1990) was centrally controlled. In fact, permanent relocation was not legally allowed (without prior permission) until 1993, although many people already started moving some years earlier. With the fall of the totalitarian regime in 1991, the country faced severe social and economic challenges. The mass layoffs that followed the shutdown of mines, plants and inefficient state-owned enterprises created immense pressures on the labour market. The agricultural land reform of 1991 authorised subdivision of former state-owned land to households using an equitable share basis (World Bank 2006). In many areas, especially the mountainous ones, the land provided to households was insufficient for survival, and the process was accompanied by many difficulties and irregularities (World Bank 2004).

Being left with few other possibilities, people from former industrial towns or remote villages started migrating either internationally (mainly towards neighbouring countries, i.e. Italy or Greece) or internally (towards the main cities in the coastal area and Tirana). Official data show that almost one in three adults has migrated internally since birth (World Bank 2007). Internal migrants occupied former agricultural land in the peri-urban areas of big cities, which soon developed into major settlements.

Internal migration in Albania is often characterised by relocation of the whole household. This contrasts with patterns of migration involving the movement of observed of one to two adults moving, as in many other contexts. Moreover, unlike the situation in other former communist countries, migration is not circular. Earlier studies indicate that internal movers come from all socio-economic backgrounds (De Soto et al. 2002; Cila 2006), will the main motivation behind economic drive to

find employment (Carletto et al. 2004). Our qualitative interviews show that often whole families and even villages have relocated to the same area, moving for environmental, employment or education reasons.

For many of the households involved, the impact of migration has been far from positive. Previous studies show that unemployment rates of peri-urban migrants are very high (Cila 2006; Hagen-Zanker and Azzarri 2010) and that consumption is lower after migration, even though household income may be higher (Hagen-Zanker and Azzarri 2010). This shows that households face volatile circumstances and may still be highly dependent on inter-household transfers, especially when migration has been less successful than anticipated. Furthermore, the composition of the support network may also be affected by internal migration. Some family members may stay behind, and others may have migrated internationally. At the same time, crowded living conditions in peri-urban areas as well as exposure to other migrants coming from all areas of Albania could lead to more exchange and interactions with non-family members than before.

Literature Review

The literature on transfers and migration can be divided into two streams. The first looks at the main factors motivating transfers and the second at the effect that migration has on such transfers.

Transfers from family and friends can be motivated by many reasons. The economic literature emphasises two main motives: altruistic motives and selfish/egoistic ones. The roots of the altruism argument can be found in socio-biological research where an altruistic person is considered someone who gives up his or her own fitness to increase the fitness of others (Hamilton 1964; Trivers 1971). In economics, an altruistic person is considered someone whose utility does not only depend on his or her own consumption but also on the consumption of their family members (Becker 1974, 1976). Consequently, an altruistic transfer will be triggered by a decrease in utility of one of the family members. The purpose of the transfers is to compensate for this utility decrease. Altruistic transfers occur mostly between close relatives (i.e. a parent caring about the utility of his/her children). Many economists argue that, even for close relatives, there may be other selfish/egoistic motives triggering the transfers. These motives relate to exchange (Chiappori 1988; Cox and Rank 1992), indirect returns or induced reciprocity (Fehr and Gächter 1998).

Some commentators maintain that "genetic roots" are a definite feature of family-based altruism, while transfers to friends are believed to be motivated more by non-altruistic motives like social norms of reciprocity, common interest and self-interest (Trivers 1971; Kolm 2006; Cox & Fafchamps 2007).

Whether migration takes place at all is also influenced by the strength of kinship networks (Mulder and Cooke 2009). The migration literature shows how kinship

networks help potential migrants migrate and then find employment, housing, and other necessities (Blumberg and Bell 1959; Goss and Lindquist 1995). Choldin (1973) analyses chain migration which may help in reproducing social networks in the new community. An important aspect of rural-to-urban migration is that relatives coming from the same area often relocate to the same area (Blumberg and Bell 1959; Hendrix 1975). This may lead to the preservation of previous relationships and habits and may even reinforce them. What is clear is that there is often a circular relationship between migration and networks: The availability of networks may trigger the decision to migrate, and at the same time migration impacts the relationships within the same networks.

Previous studies have shown that permanent internal migration has pervasive effects on families and kinship networks. Duke-Williams (2009) argues that mobility and migration are key drivers of change in households, mobility contributing to the separation of households and the creation of new households. Blumberg and Bell (1959) argue that rural-to-urban migration changes the structure of kinship relationships. They trace the changes to the "dysfunctionality of the urban setting for a kinship relationship". The same authors argue further that in urban settings transfers from family tend to decline, while residual functions (i.e. visits) may stay intact and even become stronger. In contrast, other studies cited by Blumberg and Bell (1959) show that many rural migrants receive help from friends or relatives when they first move to urban areas.

There is a rich literature exploring the relationship between migration and friendship contacts. Litwak's (1960) study in New York concludes that mobility reduced face-to-face contact, but not "extended family identification" that is, feeling close to the extended family. He finds that being in touch with family remain a constant, but that long-term residents are more likely to be in contact with neighbours or to belong to a club. Jitodai (1963) finds that at arrival rural migrants in Detroit have higher rates of contact with their kin than urban migrants, possibly because rural migrants are followed by their family. Over time contact rates for rural migrants stay stable, while those for urban migrants increase, becoming similar to the contact rates of natives and of rural migrants. Migration thus does not necessarily hinder migrants in keeping in touch with their kin. Wellman et al. (1997) also looked at social networks in Toronto in the 1970s. Out of all relationships, kinship ties were most likely to remain strong 10 years after the original survey, excluding for households that moved. Ruan et al. (1997) look at the changing structure of social networks in Tianjin, China, and find that between 1986 and 1993 individuals named fewer kin members as close, while friends became relatively more important. The authors attribute this to changing policies in China that allowed for more residential and occupational mobility. This has some similarities to Albania's situation after 1989.

There are few existing studies with regard to the type of support received by households in transition countries. Cox et al. (1997) compare family solidarity before and after transition (1987 vs. 1992) in Poland. They find the same incidence of financial transfers in real terms, despite a worse economic situation. Vullnetari and King (2008) describe a growing trend towards "care drain" in Albania, with the

migration of adult children reducing the support for elderly parents. They depict a pattern of fewer visits and less care, both by parents (care of the grandchildren) and children (care of their parents). Even though financial transfers from migrant children to parents rise in some instances, they do not make up for the shortfall in physical care. In short, family solidarity weakens as a result of migration.

Based on the previous literature and the experience it documents, in the Western Balkans might be expected to internal migration, influence: the type of transfers exchanged and the overall support received from family members and friends. As migration increases the distances between family members and in theory generates greater financial resources, we expect the importance of financial transfers to grow and services to decrease after migration. Even if extended family members move together in groups (as it is often the case in Albania), we expect that the increasing support from new friends and acquaintances (due to the exposure of migrants to the new community) will augment existing kinship ties. We explore each of these propositions in the survey outlined in the next section.

The Survey

The survey was administered by the authors in April 2008, with the assistance of a team of students from Tirana University. The survey sample was selected from Tirana's four main migrant neighbourhoods that were populated after 1990 with a large migrant population, each of those neighbourhoods has a slightly different mix. For example, households living in Bathore are more likely to come from the northern mountainous areas of Albania and are more likely to live in extended families. The households selected were distributed across the sample areas according to the size of these areas and their respective migrant populations. Thus 39% of the sample was collected in Bathore, as this is the biggest peri-urban area and also has the largest migrant population.

Given the absence of street names and accurate population registers, the sample was quasi-randomised by sub-dividing selected areas into strata of around one km^2 using satellite maps. The sub-sections were then assigned to interviewers, who randomly selected households and marked the exact location of the interviewed households on the map. If selected households did not fit the criteria of being an internal migrant household (11.5%) or refused to participate (25.7%), a neighbouring house was chosen. In total 112 households were interviewed. Four of these interviews were incomplete reducing the total sample for this analysis to 108 households. Table 11.1 shows the number of households selected in each of the areas.

Two types of questionnaires were used. The main questionnaire had 137 questions ranging from information on the main households' demographics, education, employment, income and migration history to the key section on family solidarity. The main questionnaire was administered to all the households surveyed. Twenty-six households were also interviewed in semi-structured interviews using additional open-ended questions.

Table 11.1 Household characteristics in the sampled areas

Area	5 Maji	Bathore	Selite	Senatorium	Total
Age household head	53.53	49.6	50	52.75	50.93
Education household head	11.37	10.4	10.93	11.65	10.92
Household head Muslim	0.74*	0.89	0.89	0.90	0.87
Household head coastal origin	0.05	0.02*	0.25***	0.00	0.08
Household head central origin	0.63**	0.09***	0.61***	0.45	0.38
Household head north central origin	0.11	0.22**	0.04*	0.10	0.13
Household head mountain origin	0.21*	0.67***	0.11***	0.45	0.41
Household is extended family	0.21	0.33**	0.11*	0.15	0.22
Household arrived before 1997	0.37	0.49	0.32	0.45	0.42
Number of household members	4.74	5.87***	4.32**	4.35	5.02
Number of observations	*19*	*42*	*27*	*20*	*108*

Asterisks indicate whether the mean for each group is significantly different from the total mean (*significant at 10%; **significant at 5%; ***significant at 1%)

In the module on family solidarity, households were asked in great detail about transfers between them and a random selection of extended family members and neighbours, with whom they were in regular contact both before and after the move. Households were first asked to list all relatives and friends living outside the household and with whom they were in contact on a regular basis. After this the interviewer randomly selected two relatives in each of five broad categories of relatives (i.e. parents, children, siblings, other relatives and friends) by choosing two relatives whose first name comes earlier in the alphabet. This was followed by basic demographic questions on all relatives and friends. Further questions on the socio-economic characteristics of the relative/friend and on transfers received/given were only asked about the selected relatives.

Households were questioned on the transfers (financial or in kind as goods and services) exchanged, in the last 12 months and before the move. To explore the latter transfers, different questions were developed for households who had migrated before and after 1997. The year was chosen both as a chronological milestone and because the turmoil that followed the collapse of the financial pyramid schemes led to an increase in the number of very poor migrants to peri-urban areas of large cities. In order to get a similar basis of comparison, migrants who had moved before 1997 were asked about the transfers during the last 12 months before 1991, another turbulent year that people were likely to remember. Households who had moved after 1997 were asked about transfers during the last 12 months before 1997. Detailed questions were asked on the type, amount and frequency of the transfer whether

given before or after the move. In this study, we only make use of the data on the receipt of transfers because this allows us to have more control variables based on household information. Furthermore, we only use the data on transfer frequency and not transfer amount, as recall is likely to be of higher quality for these relatively simple questions.

Some Descriptive Statistics

Table 11.1 gives a short description of the socio-economic characteristics of the survey sample by neighbourhood. Around 96% of the household heads sampled were male. 90% were married, with no significant differences by area.

On average household heads were 51 years old and had 11 years of education with no significant differences between areas. Most household heads were Muslim. However these were significantly fewer Muslims in 5 Maji, a more recent peri-urban area. Households from coastal origins were more strongly represented in Selite and household from central origins in 5 Maji and Selite. Both were under-represented in Bathore, where household were significantly more likely to come from north central and especially the mountain areas.

Most households interviewed were nuclear families, including only spouses and their unmarried children. There were variations, however, with households in Bathore significantly more likely to live in extended families, including at least three generations and/or multiple married couples). This was reflected in the number of family members per household. More households arrived before 1997 in Bathore and Senatorium (these were the first settlements of internal migrants), but the reported difference was not significant.

Next, Table 11.2 shows the incidence of payments was received from kin members and friends, grouped into five broad categories. The data tracks whether the household had received finance, goods or services from a particular relative/friend before/after migration.

Before migration, siblings were the relatives most likely to give a transfer to the household (compared to other kin groups). They remained equally important after migration, though the incidence of financial transfers for this group was no longer statistically different from transfers from others. After migration children were more likely to provide transfers than before migration. This may also be linked to demographic changes (i.e. children growing up), since households were least likely to receive money from their children before the move than from any other categories. Households were also significantly more likely to have received services from their children before and after the move compared to other kin and friends. Before migration, households were significantly more likely to receive goods from friends, whereas after migration they seemed to be more likely to receive more from parents and children, though the changes between groups are not statistically significant.

Table 11.2 Incidences of transfers received from family and friends ("Did the household received any transfer from the mentioned relatives?")

Type of kin the household receives transfers from	Parents and parents-in-law	Children	Siblings	Relatives	Friends	Total
Household received financial transfer before migration	0.08	0.00	0.15***	0.07	0.04	0.10
Household received financial transfer now	0.15	0.09***	0.20	0.10	0.17	0.15
Household received goods before migration	0.23	0.15	0.26	0.14	0.32**	0.22
Household received goods now	0.34	0.39	0.29	0.15	0.26	0.26
Household received services before migration	0.34	0.46**	0.36	0.21	0.37	0.31
Household received services now	0.36	0.42**	0.32	0.16**	0.33	0.29
Number of observations (varies for transfers before and after migration)	71–86	22–34	196–216	107–126	24–106	1,064

Asterisks indicate whether the mean for each group is significantly different from the total mean (*significant at 10%; **significant at 5%; ***significant at 1%)

Table 11.3 below shows the average frequency of transfers received from different types of kin. There are not many significant differences in the average number of financial transfers received either before or after migration. However that the average number of financial transfers per household increased from 0.34 to 0.60 transfers received. There were no significant differences between relatives for good transfers.

While services remain by far the most frequent transfer received, on average fewer service transactions were received per household after migration. The average number of services decreased from 9.11 to 6.65 per household. On average children still provided the most frequent services transfers, both before and after migration.

Qualitative Analysis

The open-ended questions were asked to 26 households selected at random. Only 19 of them were fully completed and used for this analysis. The answers were first coded into groups with similar answers, and conclusions were drawn based on the frequency of certain answers. Table 11.7 in the Appendix gives an overview of

Table 11.3 Average numbers of transfers received from family and friends (for the whole sample)

Type of kin the household receives transfers from	Parents and parents-in-law	Children	Siblings	Relatives	Friends	Total
Frequency financial transfer before migration	0.29	0.02	0.25	0.66	0.04	0.34
Frequency financial transfer in past 12 months	0.50	0.17	0.68	0.42	0.92	0.60
Frequency goods transfer before migration	3.26	0.70	3.50	2.18	2.36	2.89
Frequency goods transfer in past 12 months	3.16	2.56	2.39	1.62	1.26	2.18
Frequency services transfer from before migration	11.26	14.38	10.88*	4.79***	7.93	9.11
Frequency services transfer in past 12 months	8.81*	12.89***	7.08	3.35***	6.73	6.65
Number of observations	*61–151*	*18–54*	*182–407*	*110–235*	*25–132*	*397–987*

Asterisks indicate whether the mean for each group is significantly different from the total mean (*significant at 10%; **significant at 5%; ***significant at 1%)

questions asked, the coding and number of observations for each type of responses.

According to the in-depth interviews, migration has had little effect on relationships with relatives. Eight of the interviewed households claimed that they met their families more frequently than they had before migration. Half of the interviewed households (13) also claimed that their relationship to other family members did not change, with about the same number of households citing an improvement or a worsening of their relationships. While some families talked about relationships and lives having become more distant and separate, other respondents explained how the separation itself has made them closer:

> "My father often goes to visit them. He has a lot of nostalgia."
>
> "Yes my relationship with them didn't change. The distance can't change the affection we have for each other."

Many households also felt much closer to their families because they shared the experience of moving. Most families moved together with their nuclear family, extended family or even the whole village (ten households mentioned this explicitly). This meant that their whole family or social network was replicated in the city. One household head explained:

> "All our neighbours are blood-related; it's the same big family… All our neighbours here were neighbours there."

Another household told a similar story:

> "The village of K., around 16 houses, has moved together to this place. The entire block belongs to the S. family…. The strongest relations we keep with our neighbourhood, the S. families. We are all brothers or cousins up to the fourth degree. We have very good relationships."

There were roughly an equal number of households claiming that they had more/fewer friends or contacts with neighbours after migration. This leads us to believe that a considerable number of households were still in contact with the same people.

While family relationships often remained close, the type of goods and services exchanged between household members changed. Despite the high unemployment which almost all respondents named as their greatest problem, in general households benefited financially from migration (see also Hagen-Zanker and Azzarri 2010). This helps to explain why financial transfers became more important. Three out of five households said they received more financial transfers. Exchange of services seem to have decreased: four out of five households said that they received less services. The shift from services to financial transfers was clearly articulated by many respondents:

> "To be realistic, if I would have to help everyone I would have to give up my day of work, so the help is more limited to monetary terms and not physical anymore."
>
> "At that time you needed some help to work the land. Now you need more financial help.
>
> …Yes, with money now and in the past with work."

One respondent even declared that financial transfers replaced other social interactions to some extent:

> "Economic relations are better now. Affective relationships are less good. When you get a bit richer you grow apart a bit."

The interviews also showed that certain transfers, in particular food products, had become less important. Migrant had households grow and collect less produce than in rural areas and are therefore less able to give food products, as these respondents explained:

> "Here we buy all things in shops. There is no reason to ask your neighbour for something because the shop is there. Before it was different, we exchanged more goods."
>
> "We help each other less because now we don't own agricultural land, so we have fewer products to help each other."
>
> "Yes, there [referring to village of origin] the people can help more than here because they have cows, grow vegetables etc."

In conclusion, migration seems to have had minor impacts on the relatives that households chose to exchange goods and services with the relative importance of services. The preference for known relatives remained intact. Furthermore, financial transfers were considered more important than before migration.

Methodology and Results

Methodology

The aim of this study was to test the determinants of inter-household transfers and to analyse the impact of migration on transfer patterns. In order to measure the latter, we analyse the frequency of receiving monetary, goods and services before migration and in the last 12 months before the survey was administered (referred as after migration). We focus on the receipt of transfers, although the analysis on giving yields very similar results (reproduced for the all transfers category in Table 11.10 in the Appendix).

The data from before and after migration was pooled and we accounted for when the transfer took place with a migration dummy. To make the pooling of data possible, we used the same variables for before and after migration. When applicable, the variable factors, such as age and number of children, was adjusted to the period before migration.

As the transfers occurred within a defined time limit and the probabilities of consecutive transfers were not dependent on each other, we assume that the distribution of transfer frequencies follows the Poisson distribution. Consequently, the count rate can be calculated as:

$$\mu_i = E(y_i) = \exp(x_i \beta) \tag{11.1}$$

where μ_i is the expected value of the model dependent on a vectors of covariates, β is a vector of estimated coefficients and x_i includes characteristics of receiving household and sending family member or friend. The probability of observing a specific count is:

$$\Pr(Y_i = y_i) = \frac{e^{-\mu_i} \mu_i^{y_i}}{y_i!}, \quad y = 0,1,2,\ldots n \tag{11.2}$$

where, for the ith count, y_i is the count.

However our data showed some particularities that do not satisfy this distribution. We found over-dispersion (that is a variance greater than mean) and also presumed an excess of "zero" values. The latter may be the result of two distinctive features in the data:

The first is the random heterogeneity in frequencies of received transfers. In other words, households "faced" the same probability of receiving zero or any other frequency of transfers, but some households received more zero or "low count" transfers, and others received more "high count" transfers due to idiosyncratic factors or a random bias.

Secondly, it may be the case that some households were systematically not receiving transfers because of their characteristics. For example, respondents may have had limited contacts with their relatives or friends in the last 12 months before the move.

The standard Poisson model therefore does not satisfy the features of our data. In order to investigate what drives the over-dispersion in our data, we extensively compared different count models. We compared the "negative binomial regression model" (NBRM) to the "zero-inflated Poisson" (ZIP) and "zero-inflated negative binomial regression" (ZINBR) which uses a two-stage approach. In the first stage, "zero" and "non-zero" outcomes are modelled, and in the second stage, the remaining counts are modelled according to the standard Poisson (ZIP) or the negative binomial (ZINBR).

The predicted values of NBRM, ZIP and ZINBR models are compared in Table 11.8 in the Appendix. The tests confirmed that a simple Poisson model is inappropriate in this context, having far less accurate predictions than the other models discussed. For all types of transfers, the ZIP model performed better than the standard Poisson, but the predictions are less accurate than NBRM and ZINB. This indicates that transfers "suffer" mostly from an idiosyncratic and random bias rather than inflated zeros. In fact, NBRM and ZINB perform similarly in predicting the probability of counts, providing less evidence in favour of the "inflated zero" distortion. As presumed, the results of the ZINB estimates show that the data may have an excess of zero values because of kin members not living in the same district or because of living in an extended family (that counts as one household). However, the improvement to the overall predicted values by using the ZINB model is not high, and statistical tests show that both models are comparable.[1] We therefore use the NBRM estimates as this model explains the hidden heterogeneity in transfer frequency the best. The NBRM accounts for heterogeneity amongst count outcomes. The predicted count probability is:

$$\Pr(Y = y_i) = \frac{\Gamma(y_i + \phi)}{\Gamma(\phi) y_i !} \left(\frac{\phi}{\mu_i + \phi} \right)^{\phi} \left(\frac{\mu}{\mu_i + \phi} \right)^{y_i}, \quad y = 0,1,2,\ldots n \qquad (11.3)$$

where the variance in the predicted counts is increased through a parameter ϕ^{-1} accounting for the suspected (over-)dispersion (see also Freese and Long 2006).

Finally, the models were run separately for transfers received before and after migration to check for the consistency of our pooled data. The comparison of such results did not show any significant differences in terms of key social and demographic variables indicating that we can safely pool these data (the results of Hausman specification tests are available from the authors).

In order to verify how the support from different members within the kinship network has after migration, we estimate NBRM models separately for before and after migration. Differences between coefficients are then tested for significance using a generalised Hausman specification test (see also Weesie 2000) for the dummy variables corresponding to relatives.

[1] ZINB results for monetary, goods and service transfers are available on request from authors.

Econometric Results

Table 11.4 gives the results from the NBRM regression for financial, goods and services received. As we did not find any significant changes in the determinants of transfers for before and after migration, we have pooled the data accounting for when the transfer took place with the migration dummy. To achieve this, we used the same variables for before and after migration (see "Methodology" section for further details).

The statistical tests at the bottom of Table 11.4, and in Table 11.8 in the Appendix measure whether the NBRM model is the appropriate model to use in this context. The results in Table 11.8 show the actual and predicted mean count for all transfers for each of the models as well as the difference between them (i.e. how much the prediction diverges from the actual count). The Pearson test is a chi-squared test of independence and also indicates how close the predicted count is to the actual count. Generally the NBRM model is one of the better prediction models. In Table 11.4, the likelihood ratio chi bar-squared statistic shows whether the NBRM should be used instead of standard Poisson. As mentioned earlier, the very low values of the probability suggest over-dispersion, and therefore, the use of NBRM is appropriate.

The variable of interest "transfer after migration", which was a dummy variable ("0" for the transfers before migration and "1" for the transfers after), was highly significant for all transfers combined (see Table 11.9) and the separate transfers. This shows that the frequency of transfers received had changed significantly after migration. Below we discuss the the effect on different types of transfers.

The variable "transfer after migration" had a strong significant effect for financial transfers. This means that, all other parameters staying constant, financial transfers were received 0.3 more frequently after migration by an average household. Financial transfers had become more frequent after migration confirming the findings from the in-depth interviews and Hypothesis 1.

The dummy variables for different relatives showed that friends gave money less frequently than parents and siblings but more frequently than children or other relatives. However, this effect was not statistically significant for any of these relatives.

The dummy variable, "gender of household head", had a positive effect on the transfers received (female-headed households receive more frequently), and "gender of relative" had a negative effect (female-headed households gave less frequently). This does not necessarily mean that women gave less frequently, but rather that transfers could be explained by the particular financial situation of the household. Most of the female-headed households were in financial difficulties either because of the loss of the main breadwinner (widows dominated this category as divorces were very rare) or due to notable informal employment that was particularly unstable for women. Albanian society has patriarchal norms with men being household head, and therefore, male-headed households constitute most of our sample.

Table 11.4 Frequency of the receiving transfers: results from NBRM

	Financial transfers		Good transfers		Service transfers	
	Coef.	St. error	Coef.	St. error	Coef.	St. error
Main regression						
Transfer after migration	1.01***	0.32	−1.08***	0.26	−1.00***	0.28
Relative parent	0.05	0.61	1.28**	0.54	−1.09*	0.60
Relative child	−0.51	0.86	2.10***	0.64	0.48	0.67
Relative sibling	0.25	0.41	0.73*	0.37	−0.81*	0.42
Relative other	−0.26	0.47	0.02	0.38	−1.83***	0.45
(Friends)						
Age household head	−0.03**	0.01	−0.02*	0.01	−0.01	0.01
Household head female	1.35**	0.64	−0.91	0.64	−0.27	0.82
Education years household head	−0.04	0.06	0.08**	0.03	0.08*	0.05
Household head's religion Muslim	1.00*	0.52	0.99**	0.43	0.28	0.48
(Household head's religion Catholic, Orthodox or other)						
Household head's origin central	−0.65	0.54	0.50	0.44	0.91*	0.50
Household head's origin north central	−0.24	0.61	0.32	0.53	0.57	0.58
Household head's origin mountain	−0.73	0.54	−0.50	0.47	0.25	0.51
(Household head's origin coast)						
Household is extended family	0.37	0.29	−0.60**	0.27	−0.61**	0.28
Number of children household	−0.15	0.15	−0.06	0.12	0.35***	0.13
Years since migration	−0.06*	0.04	0.05**	0.02	0.01	0.03
Age relative/friend	0.02	0.01	0.00	0.01	−0.01	0.01
Relative/friend female	−1.30***	0.29	−0.06	0.26	0.34	0.27
Education years relative/friend	0.07	0.05	0.00	0.04	−0.09**	0.04
Household head and relative/friend same religion	−0.58	0.58	0.13	0.52	−0.37	0.65
Household head and relative/friend live in same district	1.15***	0.32	0.26	0.29	1.17***	0.29
Constant	−2.19	1.66	0.25	1.33	2.84*	1.51
Ln α	2.18***	0.13	2.16***	0.08	2.36***	0.07
Number of observations	882		880		877	
Log pseudo likelihood	−613.47		−1,564.72		−1,128.67	
P-value χ^2	0.00		0.00		0.00	
Pseudo R^2	0.0628		0.0198		0.0323	
LR $\overline{\chi}^2$	1,276.72		150,000		6,017.65	
P-value $\overline{\chi}^2$	0.00		0.00		0.00	

Note: Frequency of transfers refers to the number of times the transfer has been received in the past 12 months/before migration. Reference categories are in brackets

*Significant at 10%; **significant at 5%; ***significant at 1%

Households that moved before 1997 received monetary transfers less frequently than others. This can be explained by the "relative success" that these households have in financial terms due to more stable and better-paid jobs (see Hagen-Zanker and Azzarri 2010). Most other control variables were significant, and the coefficients had the expected signs.

With respect to goods, the variable "transfer after migration" appeared highly significant and negative. Keeping all other variables constant, there were on average 1.9 fewer transfers of goods received after migration. Based on the semi-structured interviews, it appears that this pattern was driven by changes in the nature of goods received (see also the discussion in section "Qualitative Analysis"). After migration households exchanged gifts on special occasions (e.g. birthdays), perhaps due to changing cultural practices and to more financial wealth from migration. These were more one-time gifts on certain occasions and therefore did not appear to be that frequent. Food products—dependant on having larger areas of agricultural land—became less frequent, which is not surprising given the crowded living conditions in peri-urban areas.

For received goods, we found that family relatives were generally more important givers than friends. The results were statistically significant for parents, children and siblings but not statistically significant for "other relatives". The variable "education years of household head" had a positive and significant effect indicating that the most educated received goods from their kin members more frequently. Extended family households received goods less frequently, presumably since they had stronger links with persons within their own household (the survey only measures inter-households transfers).

Finally, for service transfers, the variable "transfer after migration" was strongly significant and negative. All other variables being equal, there were 5.2 fewer service transfers received by a given household after migration. The findings that fewer goods and services and more financial transfers were received by households after migration is consistent with the broader evidence to that emerge from the literature. Semi-structured interviews helped to identify some of the underlying mechanism at work. With relatives likely to have migrated internally or internationally, they were much more able to provide financial transfers as a result of better-paid employment. At the same time, they had less time to spend on other transfers (such as services) due to increased distances and a different employment structure.

All variables for relatives (except children) are significantly less important than friends in terms of frequency of service transfers. Again we suspected this to be a consequence of migration, and we confirmed this by running the econometric models separately for before and after migration (see discussion below). As before, the education of the household head had a positive effect on frequency of services confirming the same trend observed for goods. Both outcomes may indicate a possible exchange of transfers, with more highly educated (heads of) households receiving goods and services and providing money or advice (which is not captured in here). Likewise, the number of children has a positive effect, suggesting that most of services exchanged were childminding activities. As expected, living in the same

district has a strong positive effect. This confirms the findings from previous studies that highlighted the importance of geographical proximity for receiving service support (e.g. Mulder and van der Meer 2009). The other variables have the expected signs and are generally significant.

An NBRM regression that measured the frequency probability of all transfers combined[2] was also tested. The results are reproduced in Table 11.9 in the Appendix and strongly confirm the other findings. Increased monetary transfers after migration were combined with a great decrease in goods and services. Therefore, the overall effect of migration was a decline in combined transfers. We can also attribute this to the greater value placed on individuality and independence after migration. This observation was captured in the semi-structured interviews.

When all types of transfers were considered, friends transferred more frequently than parents, siblings (not significant) or other relatives, but less than children. We assume that this pattern had changed significantly after migration (see Hypothesis 2) and therefore investigated it further.

Table 11.5 reproduces estimates of the differences in coefficients using Hausman specification tests for different relatives as compared to friends (estimated in separate NBRM regressions for before and after migration). The control variables used are the same as in earlier regressions.

For financial transfer, we see that the variables for siblings and other relatives become relatively less important compared to friends after migration, as shown by the negative and significant difference in coefficients. The same holds for parents though the difference was not significant. Transfers from children, however, did not decline in frequency, even though children gave few financial transfers both before and after migration (see Table 11.6). This trend was also found in other post-communist countries (see also Kuhn & Stillman 2004).

For goods transferred the positive and significant difference of coefficients for children showed that this group was transferring more frequently after migration. Transfers from other relatives seemed to be partially replaced by transfers from friends (not significant results however).

The variables for services transferred showed similar patterns and most of the differences in coefficients for the family members were significant (except for transfers from children). The size of the change was greater for services transferred. This is unsurprising since proximity is essential in delivering frequent services to relatives.

Generally, the results from the Hausman specification tests confirm that transfers from children and friends became more important after migration, in particular for services. The results are consistent but not always significant. The findings show that support network changed partially after migration, thus confirming Hypothesis 2.

[2] A variable that is the sum of the frequencies of all transfers received.

Table 11.5 Frequency of receiving transfers before or after migration: results from NBRM and tests of differences in coefficients

	Financial transfers			Good transfers			Service transfers			All transfers combined		
	Before migr.	After migr.	Diff. (after-before)	Before migr.	After migr.	Diff. (after–before)	Before migr.	After migr.	Diff. (after-before)	Before migr.	After migr.	Diff. (after-before)
Parent	2.67	1.41	−1.26	2.02	0.94	−1.08	1.02	−1.23	−2.25**	1.26	−0.17	−1.43
Child	−15.15	−0.6	14.55***	0.16	2.75	2.59**	1.25	1.13	−0.12	1.24	1.23	−0.01
Sibling	3.29	0.52	−2.77***	1.15	0.25	−0.9	0.96	−0.94	−1.9***	1.06	−0.51	−1.57***
Other	2.32	−1.11	−3.43***	−0.45	−0.2	0.25	−0.56	−2.13	−1.57**	−0.41	−1.44	−1.03
(Friends)												
(Other variables included)*	(+)	(+)		(+)	(+)		(+)	(+)		(+)	(+)	
Constant	−1.03	−8.41	−7.38**	−1.44	0.34	1.78	3.37	1.3	−2.07	2.91	0.92	−1.99
Ln α	1.73***	1.92***		2.28***	1.72***		2.21***	2.36***		1.86***	1.52***	
N	340	542		345	535		346	531		356	524	
Log-likelihood	−167	−416		−484	−610		−731	−820		−860	−1,188	
P-value χ^2	0.000	0.000		0.000	0.000		0.000	0.000		0.000	0.000	
Pseudo R^2	0.1490	0.0863		0.0352	0.0726		0.0184	0.0316		0.0208	0.0351	

Note: Frequency of transfers refers to the number of times the transfer has been received in the past 12 months or 12 past months before migration. The dummy for transfers from friends is the reference category for transfers received from all other family members

All other control variables included are the same as in Table 11.4 (The variable "transfer after migration" does not apply here)

*Significant at 10%; **significant at 5%; ***significant at 1%

Discussion and Conclusions

The empirical results confirm that financial transfers became more frequent after migration. The shift towards financial transfers is logical as after migration households are in greater need of financial transfers than they were before. Previous studies (Cila 2006; Hagen-Zanker and Azzarri 2010) have shown that unemployment was high amongst internal migrant households and that living costs were higher compared to living in rural areas (e.g. the cost of water). Migrants living in the densely populated and informal peri-urban areas—where the role of the state was weaker and poverty rates were higher than the inner city (Zezza et al. 2005)—faced higher vulnerability than other population groups, and the dependency of households on informal financial transfers from family and friends was greater. While one would expect that households have a greater income after migration, the higher vulnerability and uncertainty migrant households face may explain why these households were more reliant on financial transfers to a greater extent after migration.

The change in the frequency of goods received after migration shows an interesting pattern. There was a large decrease in transfers of good. Data from the semi-structured interviews showed that this pattern was driven by changes in the nature of the goods that were exchanged. After migration households transferred gifts on special occasions (e.g. birthdays). These were more one-time gifts and therefore did not appear to be that frequent. Food transfers became less frequent.

Finally, the results showed that migrant households received services less frequently after migration. This is logical, as services require proximity of transaction partners and migration is likely to have increased distances between family members. This conclusion is reinforced by the finding that service transfers were more likely and frequent, if the household and kinship member lived in the same district. Furthermore, kinship members that also migrated internally were probably less able to give services due to lack of time as a result of volatile employment and more time spent on job search.

The findings also confirmed a shift of importance of transfers from family members to friends (Hypothesis 2). For all transfers combined, we saw that after migration the role of transfers received from family members decreased compared to friends. With the exception of children, transfers from friends became more frequent than from all other family members (but the effect was not statistically significant due to a low number of friends present also before migration). This finding seemingly contradicted the data collected in the semi-structured interviews, which showed that entire extended family networks and even villages moved together and that migrant households had a very conservative attitude towards strangers. The in-depth regression analysis established that siblings remained an important source of financial help after migration, but that friends became more important than siblings for financial transfers after migration, and for both siblings and other relatives for services. This may be related to the nature

of financial transfers. The rising importance of friends despite the conservative attitude of internal migrant households may be linked to the emergence of less personal transfers.

Although we tried to limit the measurement challenges that exist for long recall periods, the study still has a number of limitations. Firstly, our sample is drawn from a small-scale household survey in a very specific context. In the Albanian case, whole families and even villages relocated permanently. Due to the specific nature of Albanian internal migration patterns and the conservative nature of migrants, transfer networks stayed closely integrated. In other countries, internal migration flows exhibit very different patterns. For instance, in China it is much more common for only one or two family members to move different patterns are likely to affect the continuation and strength of pre-migration networks. Depending on the context.

It is not fully clear if our findings can be attributed primarily to migration or to structural changes in Albanian society over the two last decades. We have reasons to believe that most of these changes in support network are caused by migration. Migration creates greater physical distance between family members and thus makes it more difficult to exchange goods and services. Furthermore, migration towards (better-) paid employment allows people to exchange more financial transfers. However, further empirical analyses are required to confirm a causal relationship between internal migration and inter-household transfers to family and friends.

We recognize that the accuracy of retrospective data is often contested. It is widely accepted that estimating remittances and transfers over long recall periods is a challenging task and fraught with measurement errors. This study tried to overcome this problem by employing two strategies: by asking for information on transfers before two memorable years the recent history of Albania, and, by focusing on the frequency of transfers (as the amounts may be harder to remember rendering the findings more disputable). However, we acknowledge that some of the measurement problems may still remain, especially with respect to the recall of transfers taking place before 1991).

While we had a varied range of control variables, our survey did not provide us with information on household income or wealth before migration. We are aware that economic well-being is important in explaining differences in transfer patterns. Therefore, we have tried to control for it by using present income as a proxy for past incomes. While the results are not included in this chapter they are available from the authors, and are very similar to those from other analyses.

As a general conclusion, our results demonstrates that and high levels of informal transfers to migrant households are prevalent in peri-urban areas, where poverty is widespread and state support is low. Contrary to expectations on migration (moving for a better job and having more incomes), the receipt of financial transfers increased after internal migration. It is uncertain whether this is because households are more vulnerable or because kinship exchanges are now more oriented

towards financial transfers (our survey data showed that giving financial transfers to other kinship members had also increased after migration). Independently from the motivation behind these transfers, their elevated frequency showed that internal migrant households relied largely on support received from relatives and friends. While informal transfers are highly valuable in a context where poverty is widespread and state support is low, it is questionable how sustainable such transfers are given the changes in the migrant network that we identify as this study showed. Further research should investigate the sustainability and adequacy of these informal transfers and the role that the state should play in supplementing them.

Appendix

Table 11.6 Transfers received before and after migration

	Before migration (last 12 months in 1991 or 1997)			After migration (last 12 months before the interview)		
	No	Yes	% yes/total	No	Yes	% yes/total
Financial transfers						
Parents and parents-in-law	46	5	9.80%	70	15	17.65%
Children	10	0	0.00%	30	4	11.76%
Siblings	130	33	20.25%	170	45	20.93%
Relatives	99	9	8.33%	110	14	11.29%
Friends	26	1	3.70%	84	20	19.23%
Total	311	48	359	464	98	562
% no(yes)/total	87%	13%	100%	83%	17%	100%
Good transfers						
Parents and parents-in-law	37	15	28.85%	52	33	38.82%
Children	7	3	30.00%	20	14	41.18%
Siblings	117	49	29.52%	150	61	28.91%
Relatives	92	17	15.60%	104	20	16.13%
Friends	17	8	32.00%	79	25	24.04%
Total	270	92	362	405	153	558
Service transfers						
Parents and parents-in-law	33	20	37.74%	54	30	35.71%
Children	4	6	60.00%	21	13	38.24%
Siblings	98	66	40.24%	156	58	27.10%
Relatives	86	23	21.10%	109	15	12.10%
Friends	17	10	37.04%	69	35	33.65%
Total	238	125	363	409	151	560

Table 11.7 Codified results from the qualitative interviews

Approximate response	Number of observations
Question E.6 What kinds of contact do you have?	
More frequent	8
Less frequent	6
Question H4.1 How did the move to Tirana change your relations with other people (including family)?	
Feel closer	7
Feel same	13
More distant	6
Family moved as well (physically closer)	10
(Interact) more with friends	5
Same	4
Less	6
Question H4.4 Can you describe the kind of support you receive from others? How is this different to the past, before you moved?	
Receive more support	6
Receive same support	5
Receive less support	5
More financial support	3
Same financial support	0
Less financial support	2
More goods	0
Same goods	1
Less goods	6
More services	0
Same services	1
Less services	4

Table 11.8 Sum of predicted and actual mean count of the tested models for frequencies of all transfers

	Actual mean count	Predicted mean count	Difference	Pearson
PRM	0.788	0.597	0.852	8,959.342
NBRM	0.788	0.804	0.109	41.762
ZIP	0.788	0.614	0.234	4,409.25
ZINB	0.788	0.801	0.105	41.056

PRM Poisson regression, *NBRM* negative binomial regression, *ZIP* zero-inflated Poisson regression, *ZINB* zero-inflated negative binomial regression

Table 11.9 Frequency of receiving all types of transfers combined: results from NBRM

	NBRM	
	Coef.	St. error
Main regression		
Transfer after migration	–0.71***	0.2
Relative parent	–0.22	0.42
Relative child	0.70	0.48
Relative sibling	–0.36	0.3
Relative other	–1.23***	0.31
Age household head	–0.01	0.01
Education years household head	0.18	0.51
Household income/per capita, in logs	0.09***	0.03
Household head's religion Muslim	0.53	0.33
Household head's origin central	0.68*	0.35
Household head's origin north central	0.43	0.41
Household head's origin mountain	0.02	0.36
Household extended family	–0.46**	0.20
Number of children household	0.21**	0.10
Household moved before 1997	0	0.02
Age relative/friend	–0.01	0.01
Gender relative/friend	0.06	0.19
Education years relative/friend	–0.06**	0.03
Household head and relative/friend same religion	–0.25	0.45
Household head and relative/friend live in same district	0.88***	0.21
Constant	2.21**	1.03
Number of observations	860	
Number of zero observations		
Log pseudo likelihood	–2,074	
LR χ^2	86.79	
P-value χ^2	0.00	
McFadden's R^2	0.020	

Note: Frequency of transfers refers to the number of times the transfer has been received in the past 12 months/before migration

Base for relatives (friends), religion (other religions), household origin (coast)

*Significant at 10%; **significant at 5%; ***significant at 1%

Table 11.10 Frequency of giving transfers to relatives and friends: results from NBRM

	Financial transfers		Good transfers		Service transfers	
	Coef.	St. error	Coef.	St. error	Coef.	St. error
Main regression						
Transfer after migration	0.82**	0.33	−0.97***	0.23	−0.98***	0.29
Relative parent	1.71***	0.58	1.16**	0.45	0.87	0.57
Relative child	0.57	0.71	2.08***	0.56	0.26	0.65
Relative sibling	0.42	0.41	0.89***	0.32	−0.24	0.4
Relative other	−0.56	0.43	0.17	0.34	−1.83***	0.45
Age household head	0.01	0.01	−0.02	0.01	−0.01	0.01
Gender household head	−0.86	0.9	−1.35**	0.66	0.6	0.76
Education years household head	0.04	0.05	0.07*	0.04	0.05	0.05
Household head's religion Muslim	1.52***	0.52	1.20***	0.39	0.29	0.5
Household head's origin central	0.17	0.52	−0.65	0.41	0.34	0.49
Household head's origin north central	0.39	0.61	−0.93*	0.48	0.37	0.58
Household head's origin mountain	−0.41	0.54	−1.36***	0.43	0.15	0.49
Household is extended family	0.17	0.32	−0.65***	0.24	−0.58*	0.3
Number of children household	0.2	0.13	0.02	0.10	0.08	0.13
Years since migration	0.05	0.04	0.08***	0.02	0.10***	0.03
Age relative/friend	−0.01	0.01	0.00	0.01	−0.02*	0.01
Gender relative/friend	−0.89***	0.28	0.01	0.22	−0.09	0.26
Education years relative/friend	0.01	0.05	−0.00	0.03	−0.00	0.04
Household head and relative/friend same religion	−1	0.66	−0.05	0.50	−0.29	0.66
Household head and relative/friend live in same district	0.25	0.31	0.71***	0.25	0.88***	0.28
Constant	−1.58	1.72	0.64	1.37	1.07	1.5
Ln α	2.28***	0.10	1.89***	0.08	2.36***	0.07
Number of observations	880		868		867	
Log pseudo likelihood	−847		−1,351		−1,567	
P-value χ^2	0.00		0.00		0.00	
Pseudo R^2	0.033		0.0327		0.0323	
LR $\overline{\chi}^2$	2,867.73		6,789.35		6,017.65	
P-value $\overline{\chi}^2$	0.00		0.00		0.00	

Note: Frequency of transfers refers to the number of times the transfer has given in the past 12 months/before migration

"Transfer after migration" is a dummy variable that is one for the observations for the period after migration

Reference categories as in Table 11.4

*Significant at 10%; **significant at 5%; ***significant at 1%

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Chapter 12
Together or Apart? Attitudes Towards Multi-ethnic State and Ethnically Mixed Communities in Post-independence Kosovo

Artjoms Ivļevs and Roswitha M. King

Introduction

Ethnic diversity is a constituent feature of Kosovo. Against the backdrop of a violent conflict during the 1990s characterised by atrocious human rights abuses and acute ethnic tensions, —the country became independent in 2008. Kosovo's constitution states that the country shall be a multi-ethnic state and its flag bears six stars, representing the six largest ethnic groups. However, neither the ethnic Albanians nor the ethnic Serbs—the two biggest ethnic groups—are happy to embrace the national symbols of the new multi-ethnic state, preferring to associate themselves with either Albania or Serbia. Rapaj (2010) considers this as a serious problem for Kosovo, arguing that if its own citizens do not recognise Kosovo, other countries will also find it difficult to recognise the state. Moreover, the term "ethnic" appears with disturbing frequency and in unpleasant context in the press (Bancroft 2009; Martin 2009). Some still fear, and others hope, that the overwhelmingly ethnic Serb population in the north of Kosovo may be sectioned off from the newly independent state (BalkanInsight 2008; The Telegraph 2008).

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Beyond the political dimension, analysis of the country's ethnic fault lines is of great relevance for understanding the prospects of Kosovo becoming an inclusive and prosperous society. Indeed a large literature has linked ethnic, religious and linguistic diversity to the economic and social circumstances of a community, region or country. For example, Alesina et al. (2003) and Alesina and La Ferrara (2005) show that ethnic and linguistic fractionalisations are likely to be important determinants of country-level GDP growth, literacy rate, infant mortality, public good provision, corruption and political freedom. Montalvo and Reynal-Querol (2005) show that ethnic and religious polarisation have a negative effect on economic growth via reduced investment and increased likelihood of civil war. Alesina and Zhuravskaya (2011) find that, keeping the level of ethnic fractionalisation constant, a higher level of ethnic segmentation (the extent to which different ethnic groups are geographically separated) is negatively correlated with government quality.

In this study we analyse how ethnicity is mapped into attitudes towards integration by asking Kosovars themselves what they think about the viability of their nation as a multi-ethnic state and about ethnically mixed communities.

To understand the Kosovars' perceptions of viability and form of a multi-ethnic state, we use an interview survey of 1,367 respondents that was conducted in Kosovo in June 2008—4 months after independence. The survey was designed and commissioned by the authors of this chapter to capture potential differences in perspectives connected to ethnicity. The econometric analysis of data suggests that, compared to the ethnic Albanian majority, ethnic Serbs in Kosovo are less likely to believe in the viability of Kosovo as a multi-ethnic state. Furthermore, there is markedly less support among ethnic Serbs for the concept of ethnically mixed neighbourhoods and communities. These findings are rather disturbing, given Kosovo's official commitment to the development of a multi-ethnic state. But we also find differences in perspective based on age, gender, income, employment status, rural versus urban residence. This suggest that the impact of ethnicity is mediated by other factors, which potentially can be affected by policies.

This chapter starts out by providing a brief overview of Kosovo's history since the Second World War. It then sets out the data and the model used to examine attitudes towards multi-ethnicity. We conclude by discussing our results.

Kosovo: A Brief Post War History

From World War II onwards, the name Kosovo appeared as the "Autonomous Region of Kosovo and Metohija", located within Serbia. The degree of autonomy slowly increased up to 1989, especially after the adoption of the new Yugoslav Constitution in 1963. Kosovo's autonomy was further strengthened, both within the Socialist Republic of Serbia and within the Socialist Federative Republic of Yugoslavia, following amendments to the constitution in 1967, 1968 and 1971. The amendments also led to the autonomous region beinf renamed the "Socialist Autonomous Province of Kosovo". This situation prevailed until the events of 1989,

which saw the end of the autonomy of the provinces Kosovo and Vojvodina and moves towards the dissolution of the Yugoslav federation. In 1991 there was a referendum, conducted without legal authorisation, in which 90% of participants voted for an independent Kosovo.

At that time, it was already quite noticeable that the Albanian ethnic majority and the Serb minority tended towards living segregated lives. Each ethnic group had its separate arrangements for health care and education. Kostovicova (2005), for example, identifies Kosovo's parallel education systems as an important producer of the nation's symbolic coordinates. What started as a tendency towards segregation increasingly turned into a tendency towards new national identities, political polarisation and conflict.

In 1998 the international community began to push for for renewed autonomy for the province of Kosovo embedded in what remained from the Federal Republic of Yugoslavia namely Serbia and Montenegro. However, an agreement between Kosovo Albanians and the political establishment in Belgrade proved to be elusive despite numerous diplomatic attempts at finding a solution.

In March 1999, NATO began its air attack on Serbia. The attacks lasted until June of the same year. International police and military forces established a presence in the province of Kosovo. United Nations Security Council resolution 1244 called for a United Nations Interim Administration Mission in Kosovo (UNMIK), a United Nations police force (UNMIK police) and international military forces, Kosovo Forces (KFOR), whose task was to administer the province of Kosovo. Later these task forces were joined by the European Union Rule of Law Mission in Kosovo (EULEX) with its central aim to back up Kosovo authorities in the implementation of the rule of law.

The events described above created migration flows which altered the ethnic composition of Kosovo. The 1981 census reported Kosovo's ethnic population proportions as 77.4% Albanian, 13.2% Serb and 9.3% other ethnicities. The Census of 1991 supplemented by estimates[1] of the former Federal Institute of Statistics reported an ethnic composition of 81.6% Albanians and 9.9% Serbs with other ethnic groups together accounting for 8.5%. For 2005 Kosovo's statistical office estimates a composition of 88% Albanian, 6% Serb and 6% other ethnic groups (Statistical Office of Kosovo 2006). Thus between 1981 and 2005, the proportion of ethnic Albanians increased at the expense of the Serb minority, and other ethnic minorities. In April 2011, another census was conducted in Kosovo, but the exercise was largely boycotted by the predominantly ethnic Serb populated northern regions.

While this historical account points to a troubled past it does not explain how perceptions, expectations and plans for the future will affect prospect for the development of an inclusive and multi-ethnic Kosovo. The targeted interviews outlined in subsequent sections provide insight into the attitudes that will shape the future.

[1] Ethnic Albanians did not participate in the census.

Data and Descriptive Statistics

Our empirical analysis is based on data from an interview survey conducted in Kosovo in June 2008. The survey was commissioned by the authors of this chapter and carried out by the *Ipsos Strategic Puls* Research Institute (based in Belgrade, Serbia), a regional office of the *Ipsos* Public Opinion Research Company, a worldwide research company with representation in 64 countries. The survey consists of 1,367 face-to-face interviews with people aged 18–86.[2]

Eight hundred and forty-five of the respondents identified themselves as ethnic Albanians that speak primarily Albanian with their family members, 482 identified themselves as ethnic Serbs who speak primarily Serbian with family members, and 40 identified themselves as other ethnic minorities principally Turkish, Bosnian, Ashkali, and Roma, though they may speak Albanian, Serbian or other language with family members). Given the limited sample size of the non-Serb minorities, we interpret the results concerning this group with caution. The Serb sub-sample was greater than its population share in order provide a greater insight attitudes in this politically important minority.

The survey questions were written by the authors of this chapter. They addressed various issues, ranging from migration to attitudes towards ethnically mixed areas of residence. The main two questions of interest for this study are as follows: (1) "Do you think Kosovo can work out as a multi-ethnic state?" with possible answers "No", "Probably no", "Probably yes" and "Yes" and (2) "Do you think it is better that different ethnic groups live separately or in mixed areas?" with possible answers "Better live separately" and "Better live in mixed areas". Tables 12.1 and 12.2 show the distribution of answers to the two questions by respondents' ethnicity.

Table 12.1 suggests that most ethnic Albanians and non-Serb minorities are confident that Kosovo can work out as a multi-ethnic state, while most ethnic Serbs are sceptical about successful co-location of different ethnicities. Table 12.2 points in the same direction: more than 70% of the ethnic Albanians and non-Serb minorities think that different ethnicities should live together in mixed areas, while 70% of the ethnic Serbs think that different ethnicities should live separately.

[2] Ipsos Strategic Puls follows the standards of the International Statistical Institute (ISI) and the European Society for Opinion and Marketing Research (ESOMAR) with regard to sample size, data collection and processing and data analysis method. The sampling frame is based on the so-called polling station territories, which represent the approximate size of census units. These base units allow for the most reliable available sample selection, as these units provide the most complete data. The sampling unit hierarchy consists of: polling station territories (920 in the sampling universe), each coming with 10 sampling points, households (420,000 in the sampling universe) and respondents (1,320,000 in the sampling universe). To reduce sampling error, the strata are defined by criteria of optimal geographical and cultural uniformity, with the first-level strata consisting of regions and the second-level strata consisting of urban versus rural settlements. Within this sampling frame, the applied type of sample is the three-stage random representative stratified sample.

Table 12.1 Answers to the question "Do you think Kosovo can work out as a multi-ethnic state?" by respondents' ethnicity

	Whole sample[a], % (n=1,367)	Ethnic Albanians, % (n=845)	Ethnic Serbs, % (n=482)	Non-Serb minorities, % (n=40)
No	8.92	5.44	66.39	2.50
Probably no	5.45	5.80	5.81	0.00
Probably yes	39.77	42.96	7.68	25.00
Yes	40.72	40.95	8.09	70.00
No answer/ do not know	5.14	4.85	12.03	2.50

[a]Ethnically weighted data

Table 12.2 Answers to the question "Do you think it is better that different ethnic groups live separately or in mixed areas?", by respondent's ethnicity

	Whole sample[a], % (n=1,367)	Ethnic Albanians, % (n=845)	Ethnic Serbs, % (n=482)	Non-Serb minorities, % (n=40)
Better live separately	22.83	20.83	69.92	5.00
Better live in mixed areas	68.54	71.48	8.92	85.00
No answer/do not know	8.64	7.69	21.16	10.00

[a]Ethnically weighted data

The Model

To determine which individual-level characteristics result in more positive attitudes towards multi-ethnic state and ethnically mixed residence, we estimate the following models:

Model 1:

$$Pro\_multi\_ethnic = \alpha * individual\,characteristics + \beta * region\,fixed\,effects + unobserved\,error\,term$$

Model 2:

$$Pro\_mixed\_habitats = \alpha * individual\,characteristics + \beta * region\,fixed\,effects + unobserved\,error\,term$$

The first model draws on the question "Do you think Kosovo can work out as a multi-ethnic state?" Given the qualitative and ordered nature of the answers to this question, we estimate the model with an ordered probit approach. As the non-response/"do not know" rate for this question is relatively low (Table 12.1), we exclude the respondents that do not answer this question from our analysis.[3]

[3] Our results remain qualitatively unchanged if the non-respondents form a middle category of the ordered answer scale ("No", "Probably no", "Do not know/No answer", "Probably yes", "Yes").

The second model draws on the question "Do you think it is better that different ethnic groups live separately or in mixed areas?" With only two pre-set answers and a relatively high non-response/"do not know" rate, especially among the ethnic Serbs, we decide not to exclude the non-respondents. The dependent variable now consists of three categories, which cannot necessarily be ordered, and we estimate the model with multinomial probit.

For both models, the set of explanatory variables includes the following individual characteristics: ethnicity (Albanian, Serb, and others), age, dummy variables for gender, marital status, having children, six income levels (including non-reported income), three education levels, being a student, being unemployed and living in rural area. In addition, five regional dummies capture broad region-specific effects on attitudes towards multi-ethnic state and ethnic co-location.

We exclude pupils (seven respondents) and those at the time of the survey principally residing abroad but in Kosovo for holidays (five respondent).

Results

First, we estimate the models for the full sample. Given that the survey contains an overrepresented sample of ethnic Serbs, we ethnically weight the data to rebalance the three ethnic groups according to the actual ethnic distribution in Kosovo (Kosovo Albanians—88%, Kosovo Serbs—6%, other minorities—6%). Second, we estimate the models separately for the ethnic Albanians and ethnic Serbs. Due to the low sample size, we do not run regressions for the non-Serb minority group.

Full Sample

Table 12.3 shows the regression results for the whole sample. We report only the marginal effects and the level of significance of the regressors. The full set of results (i.e. ordered and multinomial probit coefficients) is available from the authors upon request. In all regressions, standard errors are corrected for heteroscedasticity.

The left panel of Table 12.3 reveals the factors affecting the probability of providing positive and negative answers to the question "Do you think Kosovo can work out as a multi-ethnic state?" (Model 1).

Respondents' ethnicity has a strong effect on their confidence in Kosovo as a multi-ethnic state. The results suggest that, compared to ethnic Albanians, and keeping other factors constant, ethnic Serbs are significantly less likely to answer "yes" to the question "Do you think Kosovo can work out as a multi-ethnic state?" The finding that the Serb minority is less in favour of a multi-ethnic Kosovo could be linked to a conjecture that they do not support the independence of Kosovo in the first place. Support for this conjecture is provided by the fact that the Assembly of the Union of Serbian Municipalities and Settlements in Kosovo and Metohija has rejected the independent state status of Kosovo. The assembly considers the "entity"

Table 12.3 Attitudes towards multi-ethnic state and ethnically mixed habitats, whole sample, marginal effects

	Model 1: Do you think Kosovo can work out as a multi-ethnic state? Ordered probit				*Model 2: Do you think it is better that different ethnic groups live separately or in mixed areas? Multinomial probit*		
	No	Probably no	Probably yes	Yes	Separately	In mixed areas	Do not know
Ethnicity							
Albanian	Ref.	Ref.	Ref.	Ref.	Ref.	Ref.	Ref.
Serb	0.670***	0.059***	−0.284***	−0.445***	0.656***	−0.680***	0.025
Non-Serb minority	−0.060***	−0.049***	−0.216***	0.325***	−0.170***	0.114*	0.056
Age/10	−0.011***	−0.007**	−0.016***	0.034***	0.000	−0.010	0.009
Male	0.013	0.008	0.020	−0.041	0.085***	−0.046	−0.039**
Married	0.013	0.008	0.018	−0.039	0.086	−0.081	−0.005
Has child(ren)	0.002	0.001	0.003	−0.006	−0.063*	0.037	0.026
Income							
No income	0.012	0.007	0.016	−0.035	−0.059	0.031	0.028
<50 EUR	Ref.	Ref.	Ref.	Ref.	Ref.	Ref.	Ref.
50–150 EUR	−0.016	−0.010	−0.027	0.053	−0.060	0.012	0.048
150–300 EUR	−0.033**	−0.023**	−0.068*	0.124*	0.020	−0.061	0.042
>300 EUR	−0.045***	−0.034**	−0.124*	0.204**	−0.048	−0.010	0.058
Income non-reported	−0.060***	−0.049***	−0.218***	0.327***	−0.012	−0.134	0.146**
Education							
Primary	Ref.	Ref.	Ref.	Ref.	Ref.	Ref.	Ref.
Secondary	−0.024*	−0.015*	−0.036*	0.074*	−0.058	0.066	−0.008
Tertiary	−0.021	−0.014	−0.038	0.073	−0.106***	0.081	0.025
Student	−0.041***	−0.030***	−0.097**	0.168**	−0.029	0.043	−0.014
Unemployed	−0.038***	−0.026***	−0.079***	0.143***	−0.062	0.037	0.024
Lives in rural area	−0.016	−0.010	−0.023	0.048	−0.053*	0.062*	−0.009

(continued)

Table 12.3 (continued)

	Model 1: *Do you think Kosovo can work out as a multi-ethnic state?* *Ordered probit*				*Model 2:* *Do you think it is better that different ethnic groups live separately or in mixed areas?* *Multinomial probit*		
	No	Probably no	Probably yes	Yes	Separately	In mixed areas	Do not know
Region							
South-east	Ref.	Ref.	Ref.	Ref.	Ref.	Ref.	Ref.
South-west	0.004	0.002	0.005	–0.011	–0.077*	0.053	0.023
Central	–0.003	–0.002	–0.004	0.009	0.006	–0.076	0.069*
North	0.068**	0.037***	0.054***	–0.159***	–0.088**	–0.047	0.136**
North-western	0.050**	0.028**	0.050***	–0.128***	0.183***	–0.132**	–0.051*
	Number of observations: 1,253; pseudo $R^2=0.109$; $\chi^2=445.9$; prob$>\chi^2=0.000$				Number of observations: 1,351; $\chi^2=550.0$; prob$>\chi^2=0.000$		

Notes: Robust standard errors used to calculate regressors' level of significance. *$p<0.1$, **$p<0.05$, ***$p<0.01$

called Kosovo as an "inalienable part of Serbia, namely, Serbia's autonomous province" (Djukanovic 2008, see also Zejneli and Cvekic 2009). In addition, Serbs in the northern part of Kosovo, bordering on Serbia, may want to hold out in the hope that these ethnic Serb-dominated regions will one day be annexed by Serbia. After Kosovo declared independence, the ethnic Serb-dominated enclaves in the north of Kosovo have continued to receive wage payments as well as political directives from Belgrade, and the Serbian Dinar has continued as the principal medium of exchange (Mayr 2008). Episodes of interethnic clashes, some of which led to displacement of Kosovo Serbs from their homes (Bancroft 2009; Martin 2009; Flottau 2008), might also have undermined the Serbs minority's belief that Kosovo can function as a multi-ethnic state.

Interestingly, non-Serb minorities are more confident in the existence of multi-ethnic Kosovo than the ethnic Albanians. This could be because non-Serb minorities have always seen Kosovo as a multi-ethnic state (or region of Serbia) and have regularly been in contact with other ethnicities. For these minorities, Kosovo has never been and can hardly be imagined as mono-ethnic. Alternatively, as described in Djukanovic (2008), the "ethnic distance" between the Albanian majority and the non-Serb minorities is less than that between ethnic Albanians and Serbs, making coexistence easier.

Age has a significant bearing on ethnic attitudes. Older respondents are more likely to consider that Kosovo can work out as a multi-ethnic state. This may be because older generations have pre-conflict memories and are able to recall a time when different ethnicities lived in relative peace. By contrast, the lives of younger generations have been marked by war and inter-ethnic conflict, making it harder for them to accept, or even imagine, the idea that Kosovo can work out as a multi-ethnic state. In addition, older people (i.e. pensioners) might no longer compete in the labour market and may be less likely to run for public office creating less exposure to situations where ethnic discrimination is known to ignite conflict. By contrast young people who want to build their careers are highly sensitive to what they may perceive as ethno-economic discrimination.

People with higher incomes are more likely to think that Kosovo can work out as a multi-ethnic state. A possible explanation is that the entrepreneurs, who tend to have higher incomes may believe or hope that a state with harmonious ethnic relations would benefit their business prospect in a larger ethnically mixed market.

Education is an important indicator for social attitudes on multi-ethnicity. We find that respondents with finished secondary education are more likely to think that Kosovo can work out as a multi-ethnic state than the respondents with only primary education. Interestingly, there is no statistical difference between those with primary and higher education. However, current students are significantly more likely to say "yes" to a multi-ethnic Kosovo. Given that the current students may be the future elite of the country, this provide potential hope for the development of a multi-ethnic state.

Other things equal the unemployed are also more likely to believe that Kosovo can work out as a multi-ethnic state. One possible explanation is that the unemployed tend to spend more time at home among family and friends and less time in employment situations where they may be exposed to discriminatory or demeaning treatment based on ethnicity. Alternatively the attitude of the unemployed may be may explained by a belief that one relatively larger ethnically mixed labour market would provide better job prospects than very small ethnically segmented labour market. It should be understood that the unemployed in Kosovo form an unusually large proportion of the population. Around 45% of the population is unemployed, and youth unemployment is reported at 76% (World Bank 2008; UNDP 2006).

The right panel of Table 12.3 reports the results of the second model, where the dependent variable is based on the question "Do you think different ethnicities in Kosovo should live separately or in mixed areas?"

As in the first model, we find that respondent's ethnicity has a strong effect on the answers—in this case, reflecting attitudes towards ethnic co-location. Compared to the ethnic Albanians and keeping other factors constant, ethnic Serbs are less likely to consider that different ethnicities in Kosovo should live together and more likely to consider that different ethnicities should live separately. The are also more likely not to express an opinion. By contrast non-Serb minorities are less likely to believe that different ethnicities should live separately.

Among the other correlates, males are more likely than females to think that different ethnicities in Kosovo should live separately and less likely to abstain from providing an answer to the question. This may be because males have, in their work environments for example, encountered more ethnic conflict situations than females. War-time experiences as soldiers may also make some males unfavorable to the idea of ethnic co-location.

Compared to respondents with primary education and keeping other factors constant, respondents with tertiary education appear less likely to support ethnic segregation.

Interestingly, people living in rural areas are more supportive of different ethnicities living in mixed locations and less likely to favour living separately. This could be explained because rural areas are marked by deeper ethnic integration, or that the costs of moving towards ethnic segregation—particularly having to leave one's land are considered too high to pay. Alternatively, people in rural areas with relatively low population density may have been less exposed to media or propaganda promoting ethnic hostility.

Ethnic Albanians

Table 12.4 reports the results of the two models estimated for the ethnic Albanian sub-sample. The findings are broadly in line with those for the whole sample, which is not surprising given that the ethnic Albanians constitute the majority of

Table 12.4 Attitudes towards multi-ethnic state and ethnically mixed habitats, ethnic Albanians, marginal effects

	Model 1: Do you think Kosovo can work out as a multi-ethnic state? Ordered probit				*Model 2: Do you think it is better that different ethnic groups live separately or in mixed areas? Multinomial probit*		
	No	Probably no	Probably yes	Yes	Separately	In mixed areas	Do not know
Age/10	−0.008**	−0.006**	−0.016**	0.030**	0.000	−0.010	0.009
Male	0.008	0.006	0.017	−0.032	0.082**	−0.042	−0.040**
Married	0.005	0.004	0.010	−0.019	0.067	−0.068	0.000
Has child(ren)	0.007	0.005	0.014	−0.026	−0.060	0.019	0.040
Income							
No income	0.011	0.008	0.021	−0.040	−0.050	0.027	0.023
<50 EUR	Ref.	Ref.	Ref	Ref.	Ref.	Ref.	Ref.
50–150 EUR	−0.008	−0.006	−0.018	0.031	−0.049	0.009	0.040
150–300 EUR	−0.024**	−0.021*	−0.070	0.116*	0.039	−0.064	0.024
>300 EUR	−0.039***	−0.038***	−0.164*	0.241**	−0.089	0.022	0.067
Income non-reported	−0.050***	−0.052***	−0.278***	0.380***	−0.026	−0.129	0.156**
Education							
Primary	Ref.	Ref.	Ref	Ref.	Ref.	Ref.	Ref.
Secondary	−0.019*	−0.015*	−0.041*	0.075*	−0.052	0.055	−0.003
Tertiary	−0.012	−0.010	−0.030	0.052	−0.098**	0.069	0.029
Student	−0.027**	−0.024*	−0.082	0.133*	−0.020	0.031	−0.011
Unemployed	−0.030***	−0.027***	−0.091**	0.148***	−0.056	0.025	0.031
Lives in rural area	−0.015*	−0.012*	−0.032*	0.059*	−0.045	0.062*	−0.017

(continued)

Table 12.4 (continued)

	Model 1: Do you think Kosovo can work out as a multi-ethnic state? Ordered probit				*Model 2: Do you think it is better that different ethnic groups live separately or in mixed areas? Multinomial probit*		
	No	Probably no	Probably yes	Yes	Separately	In mixed areas	Do not know
Region							
South-east	Ref.	Ref.	Ref	Ref.	Ref.	Ref.	Ref.
South-west	0.007	0.006	0.014	−0.027	−0.047	0.012	0.035
Central	0.004	0.003	0.008	−0.015	0.040	−0.094*	0.054
North	0.079***	0.050***	0.075***	−0.204***	−0.112***	−0.021	0.132**
North-western	0.050***	0.035***	0.070***	−0.156***	0.203***	−0.149**	−0.054**
	Number of observations: 797; pseudo $R^2=0.0448$; $\chi^2=68.88$; prob$>\chi^2=0.000$				Number of observations: 838; $\chi^2=119.5$; prob$>\chi^2=0.000$		

Notes: Robust standard errors used to calculate regressors' level of significance. *$p<0.1$, **$p<0.05$, ***$p<0.01$

the whole (ethnically weighted) sample. The ethnic Albanians, who believe that Kosovo can work out as a multi-ethnic state, are more likely to be older, wealthier, unemployed, students, secondary educated and living in rural areas. In contrast, those ethnic Albanians living in north and north-western regions of Kosovo are less confident in Kosovo as a multi-ethnic state. This is an interesting result given that the northern municipalities tend to be ethnically mixed and in many cases Serb dominated, while the north-western municipalities tend to be ethnically homogenous and Albanian dominated. So, it seems that both the exposure and the lack of exposure to the ethnic minority result in more negative attitudes towards Kosovo as a multi-ethnic state.

A different picture emerges if we look at the attitudes towards ethnically mixed living areas. While ethnic Albanian respondents from the north-west are more likely to report that different ethnicities should live separately, those from northern Kosovo are less likely to be in favour of ethnic segmentation. So, even if co-location with the ethnic minority may generate negative attitudes towards the multi-ethnic state (as suggested by the results of Model 1), it does not necessarily result in more negative attitudes towards ethnically mixed areas.

Ethnic Serbs

Table 12.5 reports the results of the two models for the ethnic Serb sub-sample. Compared to the ethnic Albanian sub-sample we obtain less significant predictors of attitudes towards multi-ethnic state and ethnically mixed areas. This could partly be explained by the smaller ethnic Serb sub-sample size. The results of Model 1 suggest that people reporting that they have no income and those refusing to report their income are less likely to believe in Kosovo as a multi-ethnic state. In contrast to the case of ethnic Albanians, the ethnic Serbs living in rural areas are less likely to think that Kosovo can work out as a multi-ethnic state. Unsurprisingly, ethnic Serb attitudes towards a multi-ethnic state are also more negative in the northern municipalities—the Serb-dominated region that refuses to accept the legitimacy of an independent Kosovo.

The results for Model 2, reported in the right panel of Table 12.5, suggest that for the ethnic Serbs the probability of favouring ethnic segmentation decreases with the age, perhaps because the elderly remember the "good old" times when different ethnicities lived in relative peace. Ethnic Serbs living in Central Kosovo municipalities are less favorable towards ethnic segregation. Contrary to the results for ethnic Albanians, the ethnic Serbs with relatively high incomes are less supportive of ethnically mixed areas.

Table 12.5 Attitudes towards multi-ethnic state and ethnically mixed communities; ethnic Serbs, marginal effects

	Model 1: Do you think Kosovo can work out as a multi-ethnic state? Ordered probit				*Model 2: Do you think it is better that different ethnic groups live separately or in mixed areas? Multinomial probit*		
	No	Probably no	Probably yes	Yes	Separately	In mixed areas	Do not know
Age/10	–0.028	0.005	0.009	0.014	–0.032*	–0.004	0.036**
Male	0.026	–0.005	–0.009	–0.013	0.012	0.014	–0.026
Married	–0.027	0.005	0.009	0.013	0.011	–0.017	0.006
Has child(ren)	0.007	–0.001	–0.002	–0.004	–0.010	0.036	–0.026
Income							
No income	0.192**	–0.040**	–0.066**	–0.087**	0.027	–0.067	0.039
<50 EUR	Ref.	Ref.	Ref.	Ref	Ref.	Ref.	Ref.
50–150 EUR	0.117	–0.024	–0.040	–0.053	0.049	–0.102***	0.053
150–300 EUR	0.088	–0.017	–0.030	–0.041	0.094	–0.091**	–0.003
>300 EUR	0.086	–0.017	–0.029	–0.040	0.126	–0.079**	–0.047
Income non-reported	0.154*	–0.032	–0.053*	–0.068**	0.210**	–0.103***	–0.108
Education							
Primary	Ref.	Ref.	Ref.	Ref	Ref.	Ref.	Ref.
Secondary	–0.006	0.001	0.002	0.003	0.082	0.057	–0.140**
Tertiary	0.004	–0.001	–0.001	–0.002	0.010	0.070	–0.080
Student	–0.125	0.019	0.038	0.067	0.068	–0.029	–0.039
Unemployed	–0.048	0.008	0.015	0.024	–0.045	–0.049	0.095
Lives in rural area	0.137**	–0.022***	–0.043**	–0.072**	–0.007	–0.033	0.041

Region							
South-east	Ref.	Ref.	Ref.	Ref	Ref.	Ref.	Ref.
South-west	–	–	–	–	–	–	–
Central	0.049	−0.009	−0.016	−0.023	−0.316***	0.045	0.272***
North	0.103*	−0.018*	−0.034	−0.051*	−0.051	0.016	0.035
North-western	–	–	–	–	–	–	–
	Number of observatio ns: 417; pseudo $R^2 = 0.0241$; $\chi^2 = 17.69$; prob > $\chi^2 = 0.342$				Number of observations: 473; $\chi^2 = 80.61$; prob > $\chi^2 = 0.000$		

Notes: Robust standard errors used to calculate regressors' level of significance. *$p < 0.1$, **$p < 0.05$, ***$p < 0.01$

Conclusion and Discussion

This chapter explores attitudes towards a multi-ethnic state and ethnically mixed communities in post-independence Kosovo. Ethnicity emerges as an important determinant of whether or not people think that Kosovo can work out as a multi-ethnic state. Ethnicity also plays a role in determining whether people think that Kosovars should live in ethnically mixed areas or in ethnically homogenous enclaves. Compared to the ethnic Albanian majority, the ethnic Serbs in Kosovo are less likely to believe in the viability of Kosovo as a multi-ethnic state, and less likely to support the idea of ethnically mixed neighbourhoods and communities. By contrast, non-Serb minorities are significantly more likely (relative to the Albanian majority) to believe that Kosovo can work out as a multi-ethnic state. Yet we also find differences in perspective based on age, gender, income, education, employment status and rural versus urban residence. These variables appear to mediate and nuance the (1) role of ethnicity, suggesting that identity cannot be reduced to binary ethnic variables. They also suggest that policy factors and economic incentives might strengthen prospects for the development of a more inclusive society.

The picture that emerges from our survey raises concerns about unresolved ethnic issues that threaten to hamper building in this young and fragile state.

One of the limitations of our research lies in the fact that we are taking a "snapshot" of attitudes towards ethnic co-location at a particular point in time. In order to see whether progress is being made (or not) in matters of ethnic relations, attitudes should be surveyed repeatedly over time. Furthermore, it would be interesting to probe how and why respondents have arrived at their particular view. Understanding the role of personal experience, the attitude of family and friends, the media and statements of politicians or other officials, might help identify strategies for reconciliation. In addition, it may be fruitful to expand this type of study to include the other successor states to the Yugoslav Federation, some of which also display significant ethnic minorities.

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Chapter 13
Social Safety Nets in the Western Balkans: Design, Implementation, and Performance

Boryana Gotcheva and Ramya Sundaram

Introduction

This chapter provides a comparative perspective on the design, implementation, financing, and performance of non-contributory cash transfer programs (social assistance) across the six countries in the Western Balkan region[1] and benchmarks their performance against similar programs in other countries in Central and Eastern Europe. The primary focus of the analysis is the means-tested last-resort social assistance programs that exist in all six Western Balkan countries. We examine their core features, taking stock of basic indicators of their scope and performance and reviewing their financing, institutional set-up, eligibility criteria, main design aspects, and implementation processes in the context of the main functions of social protection—the three "P"s for resilience and opportunity: (1) prevention against drop in well-being, income, and expenditure shocks; (2) protection from destitution and losses of human capital; and (3) promotion of human capital development, opportunities, livelihoods, and better jobs (World Bank 2011a; Grosh et al. 2008).

The recent severe economic crisis posed challenges across the region. Real GDP growth in six Western Balkan countries was robust before the crisis—at 6.8% in 2007 and 5.9% in 2008– and the region was less severely affected by the crisis than

[1] Albania, Bosnia and Herzegovina, FYR Macedonia, Kosovo, Montenegro, and Serbia.

The findings, interpretations, and conclusions expressed in this chapter are those of the author and do not necessarily reflect the views of the International Bank for Reconstruction and Development/ The World Bank and its affiliated organizations or those of the Executive Directors of The World Bank or the governments they represent. The World Bank does not guarantee the accuracy of the data included in this work.

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other countries in Eastern Europe and Central Asia. The average GDP decline was 1.7% in 2009,[2] and growth resumed in 2010–2011 (World Bank 2011d). Nevertheless, the risk of being in poverty in 2010 remained as high as in 2009, as a result of job losses, less hours worked, lower earnings, and wage arrears. Remittances fell undermining the informal safety nets and coping capacity of households. It is unlikely that remittances will recover quickly as they mainly originate from countries affected by the euro zone crisis. Growth projections are modest, assuming that the crisis can be managed without a disorderly default and contagion effects. However, should the crisis worsen, economic performance in the Western Balkans could be much more significantly affected than it has been so far (World Bank 2011d).

During the crisis and in its aftermath, the demand for unemployment benefits and social assistance increased while government revenues decreased, resulting in pressures to reduce spending on social protection, health, and education. Maintaining effective protection within a reduced post-crisis fiscal envelope requires significant reforms to curtail spending on rights-based or categorical (non-means-tested) benefits, increase uptake and extend the coverage of means-tested social assistance. Governments also need to reduce the work disincentives that are built into the design of last-resort social assistance, and increase their flexibility and responsiveness of safety nets to crises and shocks. The internal demand for reforms is reinforced by the prospect of joining the EU. Even though the Western Balkan countries do not have to comply with mandatory *social acquis* (social dimensions of integration), their safety nets should support the EU's employment activation and social inclusion agenda.

Safety Net Architecture

Western Balkan countries operate *two types* of safety nets, which reflect the two different systemic approaches adopted with the transition to democracy. The two entities of Bosnia and Herzegovina (BH)—the Federation of Bosnia and Herzegovina (FBH) and the Republika Srpska (RS)—in addition to FYR Macedonia, Montenegro, and Serbia undertook evolutionary and gradual improvements to the structure and design of the pre-transition safety net, whereas Albania and Kosovo completely overhauled their old systems and introduced entirely new benefits. The systems that undertook gradual reforms are generous in terms of the scope of risks covered. However, they provide multiple and often categorical benefits that are fragmented, which undermines the efficiency of social assistance as a whole. The new systems have fewer types of benefits and therefore less fragmentation. But they provide lower levels of protection, especially for families with children and the unemployed.

[2] Compared to an overall GDP decline of 5.2% of GDP in Europe and Central Asia.

Both types of systems are faced with a region-specific need to protect those who suffered as a result of the regional armed conflicts of the 1990s. They also face region-specific difficulties in identifying and reaching the poor and socially excluded in the aftermath of mass migration and internal displacement.

Reflecting the historical legacy of these systems and their multiplicity of objectives, the mix of non-contributory (social assistance) programs in the Western Balkan countries typically consists of four broad categories (1) last-resort social assistance programs, mostly targeted to the chronic poor and with less capacity to identify and protect the transient poor; (2) family and child protection benefits with multiple objectives (to alleviate poverty of families with children, as well as increase fertility rates, encourage child raising in family environment, and protect the jobs and incomes of mothers of young children), means tested rather than universal, and in limited number of cases conditional on behavior that promotes early childhood development; (3) disability benefits for those without disability insurance; and (4) region-specific benefits for war veterans and for their families, for the families of fallen soldiers, and for civilian victims of war which combine elements of social assistance with recognition and reward. The countries also provide in-kind benefits in the form of direct and indirect subsidies, cash utility subsidies, community- and home-based social services, as well as institutional care for children deprived from parental care, for the elderly, and for people with disability. The safety net usually includes health insurance coverage as an associated right to last-resort social assistance or disability benefits.

In the 2000s, the regulatory and institutional framework was changed significantly in most of the Western Balkan countries to (1) eliminate or reduce regional differences in the provision of last-resort social assistance (mostly in Serbia); (2) clarify the division of labor between the central and local levels with respect to the design, financing, and implementation of last-resort programs; and (3) reduce errors of inclusion. The institutional structures that have been established to design and deliver the safety net benefits are similar among the Western Balkan countries. Program design, planning, monitoring, and oversight are the responsibility of the central governments (except in Bosnia Herzegovina, BH) where these are entity-level responsibilities, while implementation is delegated to the local level (see Fig. 13.1). All Western Balkan countries operate a network of Centers for Social Work or Welfare (CSWs), which are either municipal (local level) implementation units or deconcentrated structures of the central ministry. The CSWs play no role in policy development in either case since they only deliver non-veteran-related cash transfers or, as in the case of Serbia, share the delivery with municipalities.

Two specific characteristics of the safety nets' institutional arrangements stand out. First, there is a high degree of fragmentation. Not all social assistance is concentrated in the respective ministries of labor and social policy or welfare. Some noncontributory programs, notably utility benefits or subsidies for rural residents, are designed and managed by other ministries and state agencies. Not all programs are financed through the state budgets for social assistance. Cantons in the FBH and municipalities across the Western Balkans have the right to establish and finance own benefits. Second, the benefits for war veterans and families of fallen soldiers

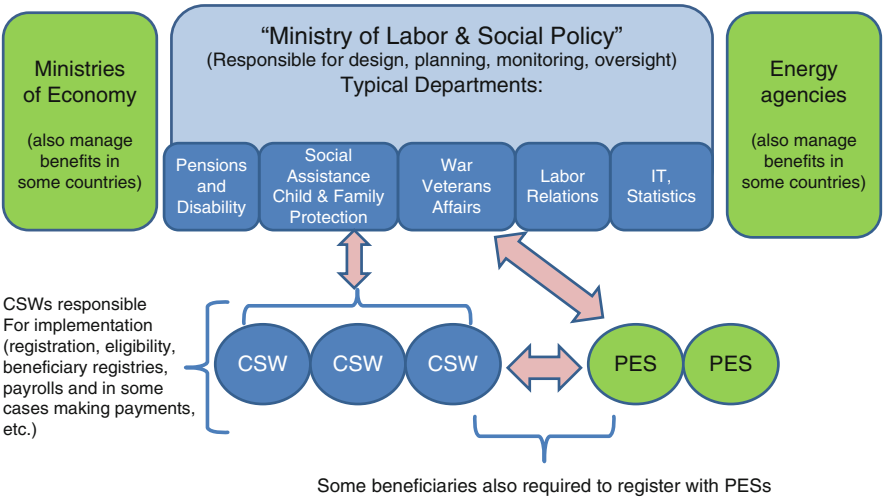

Fig. 13.1 Typical institutional structure for the safety net in the Western Balkans. *Source*: World Bank (2011c). *Note*: PES denotes public employment service

are managed separately from "mainstream" social assistance. Designated esignated ministerial departments (in Serbia, Montenegro, Kosovo, the RS) or separate ministry (the FBH) are responsible for policymaking, while the benefit delivery is assigned to separate departments for veteran protection in the municipalities.

Expenditure on Social Assistance

Public outlays on social assistance in the Western Balkan countries, measured as a share of GDP, are comparable with the other countries from the World Bank's Europe and Central Asia (ECA) region (see Fig. 13.2): they amount to 1.8% of GDP compared to average spending in all ECA countries of 1.7% of GDP. BH is a notable exception. With 3.33% of GDP going to social assistance in 2008–2009 and even more—3.9% of GDP—in 2010, BH is one of the biggest spenders in ECA. However, if expenditure on war veteran benefits was brought down to the average regional level of 0.4–0.5% of GDP, overall spending on social assistance in BH would go down to the average for the Western Balkan countries.

Spending on social assistance is inequitable, with a growing share of allocations to categorical programs. Throughout the 2000s, categorical benefits were consistently absorbing a higher share of social assistance spending than means-tested benefits. Only FYR Macedonia spends more on means-tested than on categorical programs. However, after 2008, the share of categorical benefits in the overall

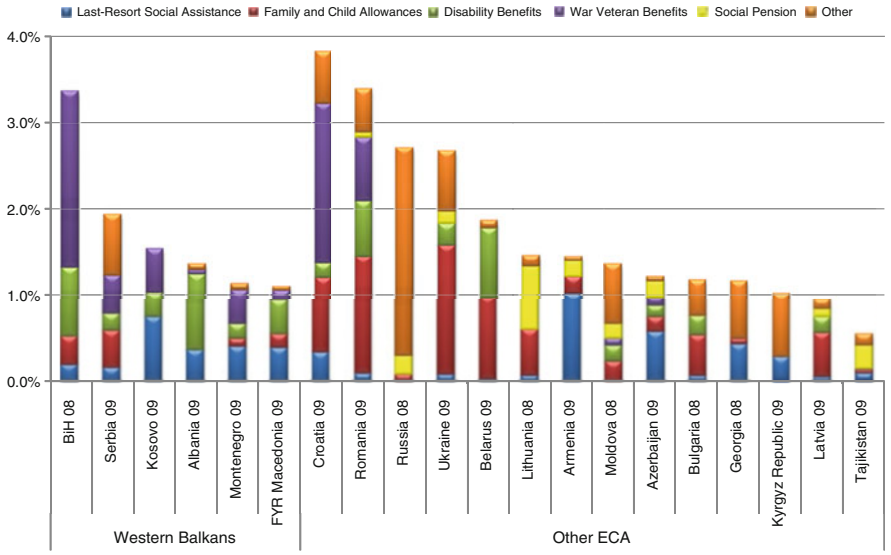

Fig. 13.2 Social assistance spending by main types of programs (% GDP, 2008–2009). *Source*: Europe and Central Asia Social Protection Database, World Bank

spending envelope increased there as well[3] due to the elimination of the means test for some of the child allowances and the main categories of disability benefits. While in Kosovo and Montenegro spending on categorical and means-tested programs is almost at parity, the bias toward categorical benefits is pronounced in Albania and Serbia due to spending on disability benefits (Albania) and wage compensation during maternity leave (Serbia). The high level of spending on categorical benefits in the two BH entities is mostly due to a plethora of categorical benefits paid to war medal holders, demobilized soldiers,[4] disabled war veterans, and families of fallen soldiers. The history of these programmes is indicative of a wider problem. Easy to inflate in good times they are but very difficult to contract when the budget envelope tightens. Over time the composition of spending is shifting toward categorical programs (see Fig. 13.3).

Spending priorities differ across countries. Expenditure on last-resort social assistance is relatively high in Montenegro (close to 0.5% of GDP) and also in FYR Macedonia and highest in Kosovo (over 0.7% of GDP), where it reflects the high incidence of poverty and the concentration of spending over fewer benefit programs. Spending on last-resort social assistance is very low in Serbia and BH, resulting in

[3] In 2008, the means-tested programs in FYR Macedonia absorbed 0.75% of GDP, against 0.22% of GDP allocation on categorical programs. In 2009, the spending on means-tested programs increased marginally to 0.77% of GDP compared to a significant growth in the spending on categorical programs that reached 0.34% of GDP.

[4] Only in FBH, until 2010.

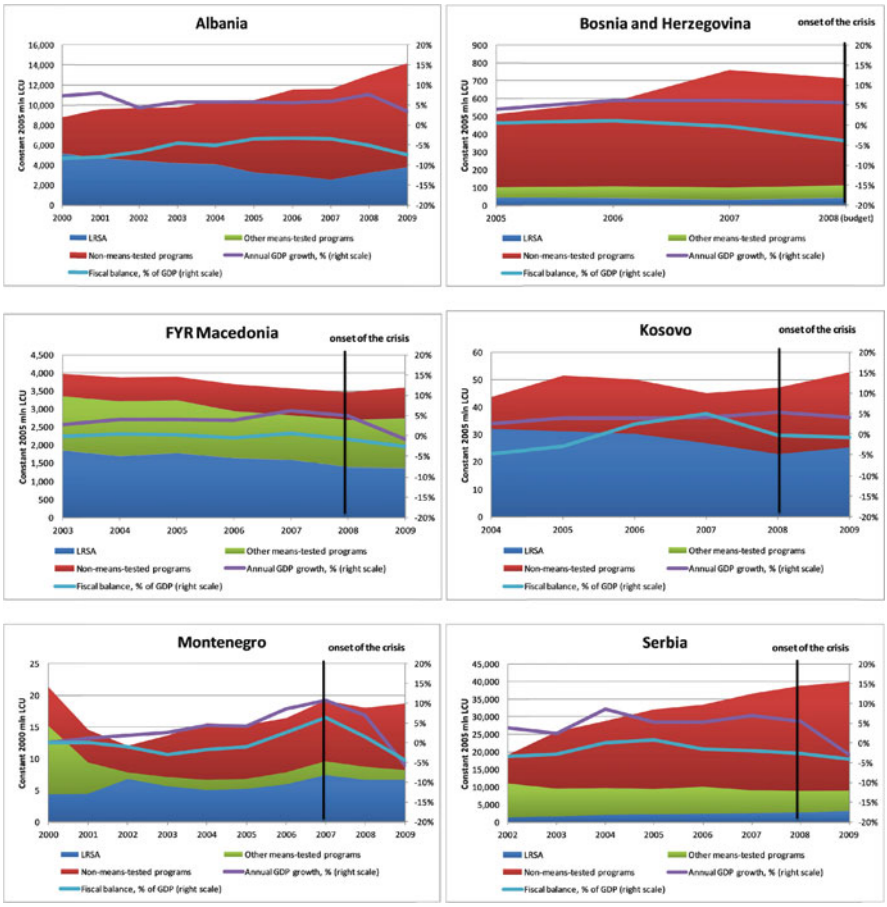

Fig. 13.3 Spending on social assistance by targeting method (% of GDP, 2009). *Source*: Europe and Central Asia Social Protection Database, World Bank

small-scale programs with narrow coverage and big exclusion errors. At the same time, the Western Balkan countries spend more on disability allowances than other Europe and Central Asia countries, with Albania having the largest spending (0.9% of GDP) in the region and Montenegro having the highest growth rate in spending on disability benefits in recent years. Expenditure on child allowance is higher among ECA countries outside the Western Balkans where Albania and Kosovo have no stand-alone child benefits, while other countries restrict benefits by targeting the monthly child allowance with a rigorous income test (Serbia, BH) or means test (Montenegro). Spending on war veterans' benefits dominates the spending in BH and is also high in Kosovo.

Most last-resort social assistance programs are financed from the central budgets. The only exception to this rule is the FBH where it is the responsibility of the

cantons.[5] The centralized financing is earmarked and takes the form of capitation grants that also consider the size of the units of assistance (families). Albania and Kosovo are exceptions. In Albania the central budget allocates block grants to the municipalities, and in Kosovo the municipalities are provided with block non-earmarked grants. Conventional wisdom in the public finance literature suggests that redistribution is a role most appropriately handled by central governments, because they are inherently in the best position to handle inter-regional inequalities and risk pooling (Grosh et al. 2008). Decentralized financing has the potential to ensure a faster flow of funds and an allocation of resources in accordance with local priorities. However, it is prone to local political bias. The small size of municipalities and their limited tax base, is another constraint. The finance that they have available for safety net programmes would not be sufficient for meaningful reductions in poverty and vulnerability, particularly during economic downturns.

Performance of Social Assistance

We use household survey microdata to assess safety net performance outcomes against three criteria. Those are ***coverage***, measured by the share of the poorest quintile receiving benefits; ***targeting accuracy***, as indicated by the share of benefits going to the poorest quintile; and ***generosity (adequacy)*** using the average transfer amount as a fraction of average consumption for beneficiary households in poorest quintile, and unit transfers as a fraction of minimum wage. We use standardized methodology to develop the performance indicators. Welfare is measured with a harmonized consumption aggregate,[6] and individuals are ranked based on per capita consumption before cash transfer.[7] Standardized software (ADePT SP) is used to compute indicators. For comparative purposes, those belonging to the quintile with the lowest consumption are defined as poor.

The targeting accuracy of all social assistance programs is respectable. Due to the means testing of a wide range of programs, overall social assistance is accurately targeted to the poor in Montenegro and Serbia (see Fig. 13.4). In Albania and Kosovo, where last-resort social assistance largely represents the whole of social assistance the targeting performance is also high as expected. Leakage to the richest quintile is negligible: less than 5% in Serbia, Kosovo, and Albania; 7% in

[5] Except for one of the ten cantons where the canton shares the responsibility for financing with the municipalities.

[6] Developed by the World Bank's poverty team—a standard basket of goods and services across all countries and all expenses are similarly deflated across countries and expressed in per capita terms.

[7] Individuals are sorted into quintiles for each transfer using "per capita consumption—per capita social assistance transfers."

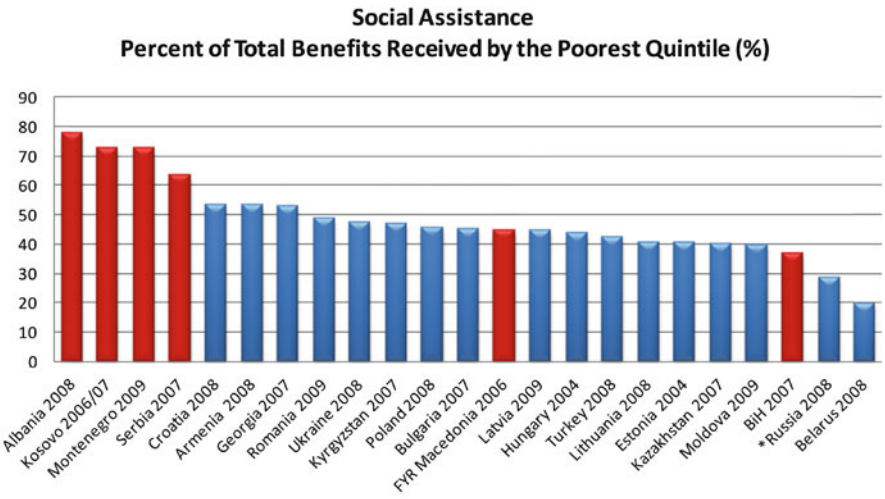

Fig. 13.4 Targeting accuracy of all social assistance in the Western Balkan countries. *Source*: Europe and Central Asia Social Protection Database, World Bank

Montenegro; and 10% in FYR Macedonia. The exception is BH, which has the second largest leakage of social benefits to the nonpoor and rich—due to the regressive cash transfers to veterans—over 17% of all social assistance is provided to the richest population quintile.

The broadly impressive targeting accuracy of social assistance is overshadowed by a weak performance in terms of coverage. The coverage of the poorest quintile with all types of social benefits is low in all Western Balkan countries (see Fig. 13.5). The highest coverage has been registered for the safety net in Kosovo. However, coverage is limited to only 40% of the poorest quintile. Coverage is extremely low even in countries which have multiple safety net programs designed to provide protection and mitigate risks related not just to poverty but also disability, temporary loss of job due to child care and an increase in the number of dependent children in the family. The safety nets of Montenegro and the two entities of BH reach only 20% of the poorest quintile. Low safety net coverage is associated with program design features which limit access and allows for substantial errors of exclusion. For example, in the FBH, access to civilian disability benefits is granted only in case of 90–100% disability (i.e., disability which is permanent, irreversible, and requiring care and attendance by other persons). In some countries, the noncontributory disability benefits and the monthly child allowances are income tested or means tested with the same targeting mechanism as the last-resort benefit. Finally, the extremely low coverage of last-resort social assistance in BH, Serbia, and Montenegro undermines the capability of their safety nets to reach a higher share of the poor with at least one type of noncontributory cash transfer.

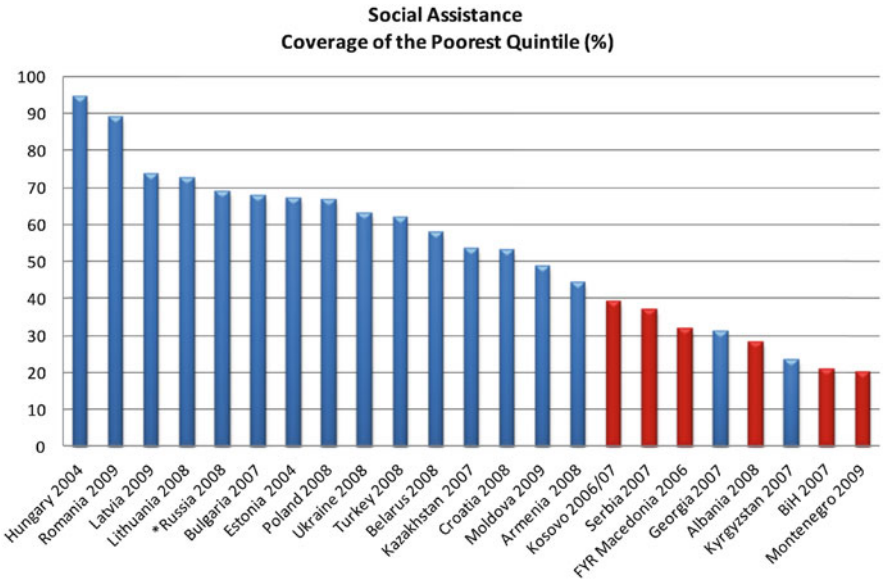

Fig. 13.5 Coverage of all social assistance in the Western Balkan countries. *Source*: Europe and Central Asia Social Protection Database, World Bank

The generosity of benefits varies significantly among the Western Balkan countries. When measured as a fraction of the post-transfer consumption of beneficiary households, the generosity of all social assistance is relatively high compared to social assistance schemes delivering similar benefits in ECA countries (see Fig. 13.6). Another measure of the generosity of benefits that can be useful in considering adverse incentive effects is the comparison of benefit levels to minimum wages. From Table 13.1, we can see that, except in the case of Montenegro, where the social assistance transfer is about 75% of the minimum wage, social assistance benefits in the Western Balkans are not very generous compared with minimum wages—ranging between 7 and 20% of the minimum wage level.

The targeting accuracy of some of the Western Balkan last-resort social assistance programs is very high. Last-resort social assistance in Montenegro transfers more than 80% of all program budget to the poorest population quintile. Programmes in of Serbia and Kosovo transfer more than 70% to the poorest quintile, making them some of the most accurately targeted programs in ECA and comparable to countries like Lithuania, Bulgaria, and Romania (see Fig. 13.7). The last-resort social assistance in Albania and FYR Macedonia also seems relatively well targeted. These programs manage to transfer between 50 and 60% of their benefits to the poorest quintile. However, they suffer from leakage of resources to the non-poor, with over 9% of last-resort benefit in FYR Macedonia and 6.5% in Albania received by the wealthiest quintile – an example of elite capture. Targeting accuracy is much weaker in BH, where the poorest quintile receives only 40% of all benefits

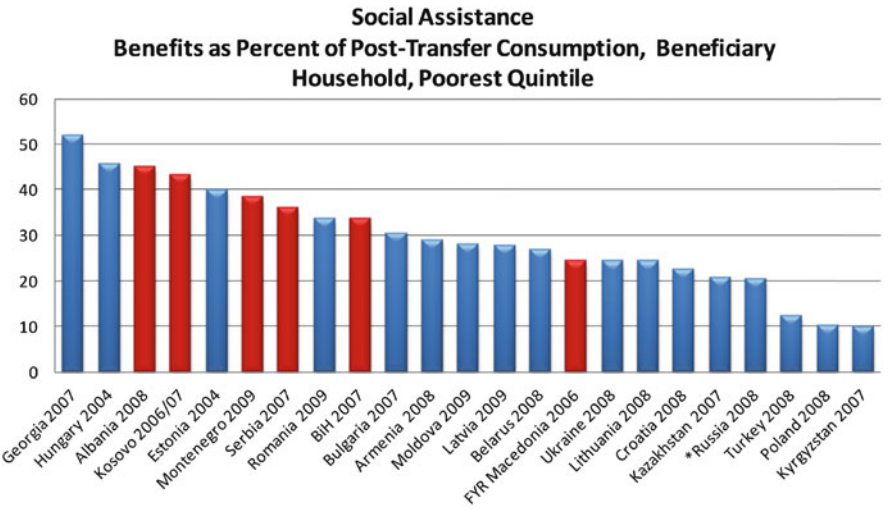

Fig. 13.6 Generosity of social assistance in the Western Balkan countries. *Source*: Europe and Central Asia Social Protection Database, World Bank

Table 13.1 Average transfer value of overall social assistance (beneficiary households of indicated transfer only) as a share of minimum wage (%)

Albania NE 2008	15.0%
Bosnia-Herzegovina CSW 2007	19.5%
FYR Macedonia SFA 2006	Na
Kosovo NS 2006/07	7.2%
Montenegro FMS 2008	74.8%
Serbia MOP 2007	17.6%

Source: Household budget survey data, staff calculations. World Bank (2011c)

delivered by the CSWs, while a significant share of the benefit budget is captured by the richest 20% of the population.

The last-resort social assistance programs are an important element of the social assistance in the welfare systems of the Western Balkan countries. Their main goal is to alleviate poverty of chronic and transient poor and promote the social inclusion of vulnerable and marginalized segments of the population. However, their coverage. The biggest programs are to be found in Albania, covering over 12% of the population. Coverage of the poor is the highest in Kosovo, with two out of five individuals in the poorest quintile receiving last-resort social assistance (see Fig. 13.8). However, this is low when compared to Kosovo's poverty rate—almost 35% of Kosovo's population currently lives below the poverty line of 1.55 € per

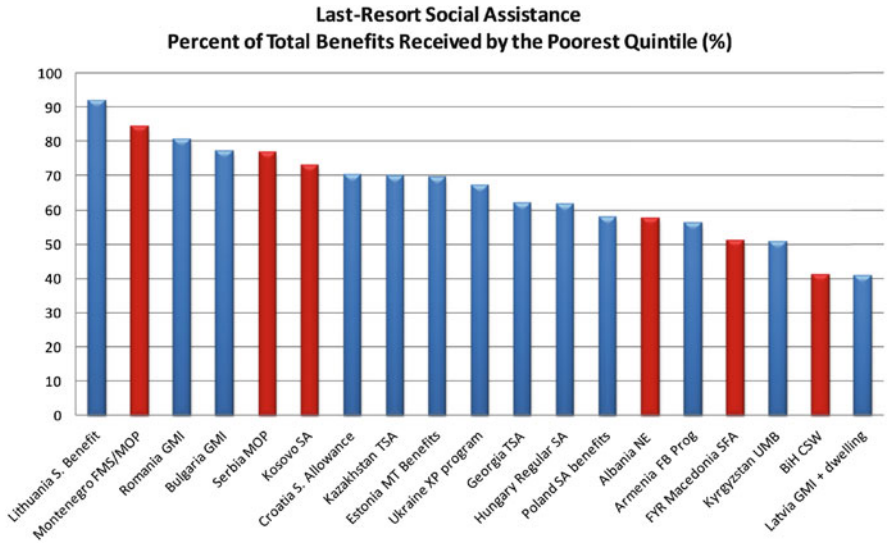

Fig. 13.7 Targeting accuracy of last-resort social assistance in the Western Balkan countries. *Source*: Europe and Central Asia Social Protection Database, World Bank

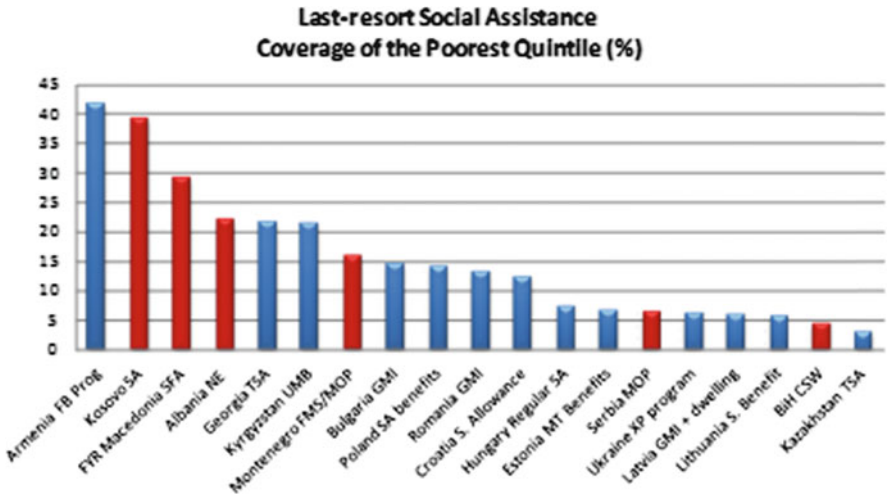

Fig. 13.8 Coverage of last-resort social assistance in the Western Balkan countries. *Source*: Europe and Central Asia Social Protection Database, World Bank

person per day, and 12% of the population lives in extreme poverty on less than 1.02 € per adult equivalent per day (World Bank and Statistical Office of Kosovo 2011). When measured with administrative data, last-resort social assistance in BH is negligible in scope reaching only 0.25% of the population, followed by FYR Macedonia

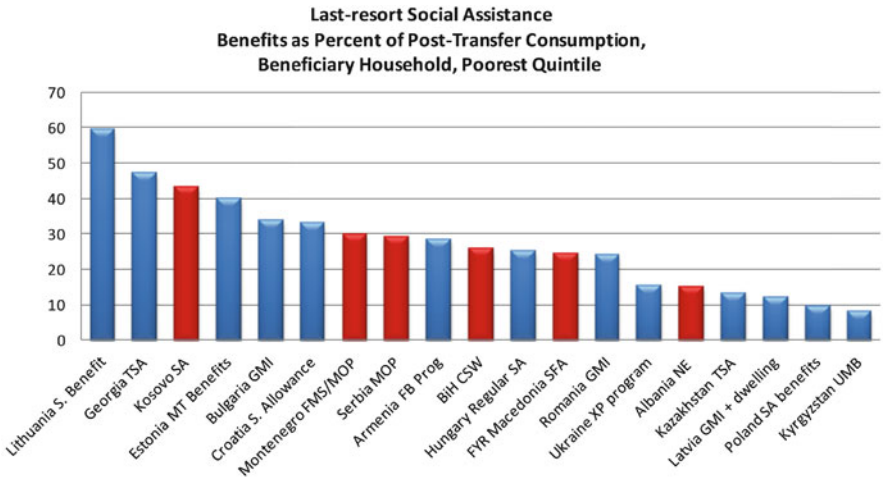

Fig. 13.9 Generosity of last-resort social assistance in the Western Balkan countries. *Source*: Europe and Central Asia Social Protection Database, World Bank

with coverage of 0.5% of the country's population[8] in 2009 and 2010. Coverage of the poor is particularly low in BH, where fewer than 5% of individuals in the poorest quintile receive last-resort assistance, family and child protection or civilian disability benefits combined. Last-resort program coverage is also low in Serbia, though it has increased in recent years. Whereas 6% of the poorest quintile was covered in 2007 it has reached over 10% in 2011. Increases in the eligibility thresholds, which are adjusted at the rate of inflation have been the primary reason for this expansion.

The generosity of last-resort social assistance is uneven. Albania's Ndihma Ekonomike is the least generous program while the Kosovo's program appears to be the most generous (see Fig. 13.9). Each of the other programs accounts for between 25 and 30% of the post-transfer consumption of the poorest quintile. When measured as a fraction of the minimum wage, last-resort social assistance appears less generous. It is typically less than 15% of the minimum wage and just 4% of the minimum wage in Albania. The exception to this picture is Montenegro where the transferred amount represents a substantial fraction (about 43%) of the minimum pay standard (Table 13.2).

In summary, the last-resort social assistance schemes in the Western Balkan countries have an impressive record in terms of their targeting accuracy and a relatively good record in terms of their generosity, but they tend to have only very limited coverage of the poor.

[8] Administrative data and staff calculations; estimates/approximate numbers for Albania because administrative data is collected for households only (102,000 households at the point of estimation).

Table 13.2 Average transfer value of last-resort social assistance (beneficiary households only) as a share of minimum wage (%)

Albania NE 2008	4.1%
Bosnia and Herzegovina CSW 2007	14.7%
FYR Macedonia SFA 2006	Na
Kosovo NS 2006/07	7.2%
Montenegro FMS 2008	43.5%
Serbia MOP 2007	12.9%

Source: Household budget survey data, staff calculations. World Bank (2011c)

Design Characteristics of Last-Resort Social Assistance

Last-resort social assistance programs in the Western Balkans are centrally designed, have national coverage, and treat all citizens equally by legislating common eligibility criteria and uniform application procedures nationwide. The two exceptions are Albania, where targeting rules are not standardized and geographic targeting produces regional variations in treatment, and the FBH where the benefit mix and main eligibility criteria are set in entity-level legislation, while other design elements and even the amounts to be paid can be regulated by the cantonal level social protection laws. Where the safety nets have evolved from the former Yugoslav system (BH, FYR Macedonia, Montenegro, and Serbia), the last-resort programs are designed along the lines of the "minimum resources," "last-resort subsidy," or near "last-resort subsidy" models that exist in many of the EU Member States (EU 2006). In the case of Kosovo, the benefit for the poor also contains elements of child protection benefit and unemployment benefit. The main design characteristics of the last-resort cash transfers in the Western Balkan countries are summarized in Table 13.3.

Eligibility for last-resort social assistance is determined by social workers at the CSW based on the centrally defined eligibility criteria, which can include an income and asset test and additional indicators of the economic and demographic status of the unit of assistance. The "burden of proof" rests with the applicant, and presented documents are subject to verification. Administratively preset minimum income thresholds serve as eligibility cutoffs and also as "ceilings". The thresholds are set in different ways: as nominal levels using implicit national equivalence scales taking into account family size (Montenegro, FYR Macedonia, Kosovo), family size and composition (Albania), explicit equivalence scale (Serbia), or flat rate without equivalence scale (the RS). In FBH the setting of eligibility thresholds is done differently in each of the ten cantons by linking to the cantonal average minimum wage, the minimum wage in FBH or government defined income minima. In all countries, the eligible beneficiaries receive the *difference* between the administratively set ceiling and the actual income of their unit of assistance. Most administrative authorities rely on easily verifiable income reports to determine eligibility. Only Serbia CSWs make efforts to assess incomes from informal employment, land, savings, property, or intellectual rights. Incomes from social transfers and active labour

Table 13.3 Design elements of last-resort social assistance in the Western Balkans

	Albania	Bosnia and Herzegovina	FYR Macedonia	Kosovo	Montenegro	Serbia
Institutional level at which the benefit is designed	Central government and local governments	Cantonal governments (FBH), Central government (RS)	Central government	Central government	Central government	Central government
Regional differentiation	Municipal	Cantonal (FBH)	No	No	No	Before 2004—municipal
Income test	No. Imputed income from land and livestock	Income thresholds differentiated with size of the unit of assistance Implicit equivalence scales				OECD equivalence scale
Disregards of incomes from other benefits	Disability benefit and pensions	All social assistance	Social assistance with exceptions	Basic and disability pension, one-time social assistance	All social assistance	All social assistance
Earned incomes disregards	No	No	No	No	No	Yes, from ALMPs
Asset test	Yes, verified through official registries and home visit					
Exclusionary filters	Car, land, livestock, agricultural produce	Land 0.5 ha	Second dwelling, productive assets, savings, arable land, livestock	Land 0.5 ha, business, vehicles, livestock	Land 0.5 ha	Land 0.5 ha immobile or mobile property
Benefit formulae	Full benefit (urban); discount of imputed income from agriculture (rural)	Difference between maximum benefit due/benefit base (which varies depending on the number of members of the household or family) and actual income of the unit of assistance				
Linkage with other benefits and rights	Conditional to community work or public works participation	Health insurance, public works, job brokerage, training	Health insurance, public works, job brokerage, training	None	"Package" of benefits, public works, job brokerage, training	Health insurance, public works, job brokerage, training

Source: National social protection laws. World Bank (2011c)

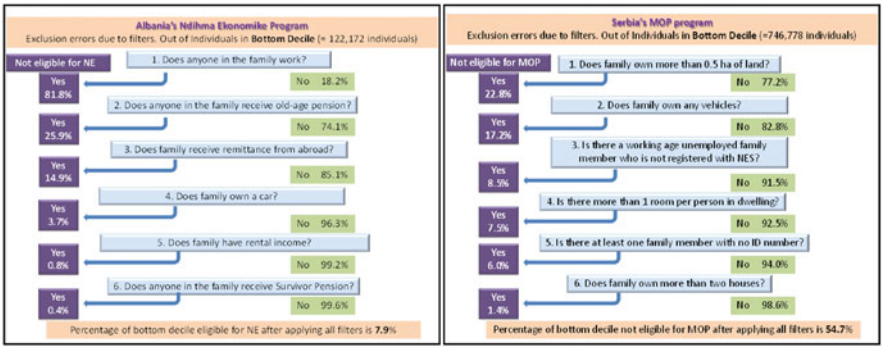

Fig. 13.10 Excluding poor with "filters" in Albania and Serbia. *Source*: Staff calculations with most recent household level microdata. World Bank (2011c)

market programmes are disregarded. In Serbia this could cause disincentives to work due to the infinite marginal taxation effect.

In parallel with low income thresholds, the CSWs determine eligibility for last-resort social benefits by applying a variety of *exclusionary filters* and denying claims of applicants who are in possession of certain immobile or mobile assets included in negative lists, participate in economic activities or employment, or are in receipt of remittances. Permanent address and citizenship status are also used as filters which has the effect of excluding refugees, internally displaced persons, traveling Roma, and other migrant population. The filters are binary: possession of assets automatically disqualifies the applicant, regardless of the size of the measured income or needs. Figure 13.10 provides two examples of how the application of exclusionary filters affects the access to last-resort social assistance in different program design contexts.

While the *intention* of the filters is to improve targeting accuracy and to ensure that benefits are only given to those who are truly unable to work or have low incomes, they produce some perverse *results*. For example, the filters can cause significant errors of exclusion among the poor (one of the factors that contribute to low coverage) and possible disincentives to work among able-bodied adult applicants due to the requirement to register as unemployed which also serves as a verification of not having any income from work. Along with the low income thresholds that determine eligibility, the filters make last-resort social assistance more readily available to the chronic long-term poor but often disqualifies the transient poor.

One common filter—which can be either exclusionary or non-exclusionary—is the proof of unemployment status or mandatory registration with the public employment services. In Montenegro, BH, FYR Macedonia, Serbia, and Albania, the requirement that claimants register as unemployed is a way to ascertain that the relevant member of the household receiving assistance is not working and is receiving no formal income. In the absence of unemployment registration, the application will be disregarded (in Montenegro for single-member families) or

income from work will be imputed in the overall family income (in FYR Macedonia). Unemployment registration is also a way to ensure that able-bodied recipients of social assistance can potentially be offered participation in public works or active labor market programs. In most of the Western Balkan countries, unemployment status serves as a stand-alone filter with a significant power to exclude, as already shown in the case of Albania. The existence of this filter precludes protection of the working poor through the last-resort social assistance program.

The determination of benefits often incorporate assumptions which penalize excessively large unit of assistance. This is because benefits are intended to ensure basic food consumption, and because poverty is correlated strongly with family size, larger families are disproportionately at risk of being poor. Large units of assistance are also discriminated against by limitations in the number of eligible recipients in any one unit of assistance. Many programs lack proper indexation (to inflation) rules for eligibility thresholds and benefit levels. Moreover, because the benefits are not linked to national poverty lines and/or other minimum income or consumption standards, and purchasing power and adequacy are not monitored against these thresholds.

Implementation Arrangements for Last-Resort Social Assistance Programs

Implementation arrangements for last-resort social benefits have many strong features, including on-demand applications, clear initial points of contact, regular verification of eligibility, and clear recertification procedures. However, they are also administratively burdensome (requiring in some cases over 20 different documents) and costly (see Table 13.4 for details).

The CSWs determine eligibility based on detailed rulebooks that try to limit discretion in decision-making. Information from the presented documents is reconciled through data matching with official registries (including tax, cadastre, agricultural land, vehicle, housing registry), direct verification with issuing agencies, and home visits all playing a role. Eligibility is usually determined through a two-stage process that allows appeals to a second level body on issues regarding eligibility or amounts. The social workers not only guide the application process but are also tasked with referring the applicant to other benefits or social services if available within the safety net system. As a whole, the last-resort social assistance programs in the Western Balkan countries apply more stringent verification of applicants' eligibility when compared to other benefits, such as disability and/or family and child benefits. The CSW staff has a greater degree of discretion in some cases, but the system is still over-reliant on administrative data and paper-based documents.

Table 13.4 Last-resort social assistance programs: summary of implementation responsibilities and functions by level of government

	Albania	Bosnia and Herzegovina	FYR Macedonia	Kosovo	Montenegro	Serbia
Institutional level at which the benefit is implemented	Municipal	Cantonal (FBH) Central through deconcentrated units (RS)	Central through deconcentrated units (CSWs)	Municipal	Central through deconcentrated units (CSWs)	Central through deconcentrated units (CSWs)
Intake, registration	Local	Local (at CSWs)	Local (at CSWs)	Local	Local (at CSWs)	Local (at CSWs)
Eligibility determination	Central and local	Central (RS) Cantonal (FBH)	Central	Central	Central	Central
Verification	Local	Local (CSWs)	Local (CSWs)	Local	Local (CSWs)	Local (CSWs)
Database management	Local	Local (FBH) Central (RS)	Local (CSW level)	Central	Central	Central
Existence of central registry	No	Yes (RS) No (FBH)	Yes	Yes	Yes	Yes
Payment authorization	Local	Central (RS) Cantonal (FBH)	Central	Central	Central	Central
Payments process	Local—post offices (rural) Banks (urban)	Cantonal—post offices and banks (FBH) Central—post offices and banks (RS)	Central/local—post offices via post office bank	Local—post offices	Central—banks	Central—banks
Oversight	Central and local	Central (RS) Cantonal (FBH)	Central and CSWs	Central and local	Central and CSWs	Central and CSWs
Local level independent	Linked to central ministry	Linked to central ministry (RS), cantonal, and municipal (FBH)	Linked to central ministry	Linked to municipal government	Linked to central ministry	Linked to central ministry

Source: National legislations and CSWs administrative rulebooks. World Bank (2011c)

Beneficiaries increasingly receive payments through the banking system rather than through the post offices. The exceptions are Montenegro and Kosovo where payments are made only through the post offices. In Albania local communities and leaders get involved in the payment of last-resort social assistance, sometimes even determining the amount that each beneficiary household should receive.

Benefit administration suffers from a number of weaknesses. Application processes are separate for each type of benefit, other than in Montenegro where some are delivered under the same eligibility rules and application process. The processes are complex and bureaucratic, requiring the applicant to produce up to 27 official documents (which can be costly and time consuming to obtain) and to make multiple visits to the CSW office, as well as to submit to home visits by social workers for verification.

The Western Balkan countries are investing in upgrading their registries (program-specific databases) and in improving the existing data management and information flows. However, registries are still too incomplete to constitute management information systems. In effect they are stand-alone databases that are not integrated into country-level automated welfare information systems as is the case in many developed countries. At best, they cover payroll data for approved beneficiaries. Data on rejected applicants are not digitalized, and therefore, policymakers have no way to monitor and evaluate errors of exclusion. Also, except for the databases in Serbia and Montenegro, there is no information about the family as a single unit of assistance. It is difficult to track benefits and services that are provided to the *whole* unit, and not to separate individuals. The registries are also not connected online to other government databases, and internal and external cross-checks are either not performed or slow and ineffective. Finally, oversight and control mechanisms are inadequate and inefficient.

These design and implementation problems contribute to the mixed performance outcomes of last-resort social assistance programs in the Western Balkan countries. The very strict rules of eligibility and their rigorous enforcement reduce errors of inclusion but limit coverage. The use of filters makes determination of eligibility inequitable (high errors of exclusion) less transparent (lack of objective or transparent "weights" across eligibility criteria) and inefficient (through possible disincentives to work). Often, the means test and filters are supplemented by a mandatory "field/house visit" to check for eligibility with vaguely defined scope of verification and high discretionary power in ultimate decision making on the part of officials.

Few of the programs make any outreach efforts to cover deserving poor who are left behind. Instead most take a predominantly bureaucratic and paper-based approach to identifying beneficiaries. Programs are open for applicants on demand, but the information made available about the programs is not always sufficient, particularly in terms of reaching vulnerable groups. The eligibility determination is complicated and not always transparent, and practices can vary across CSWs. The burden and financial costs of applying and collecting supporting documents are borne entirely by the applicants.

Work Disincentives in Last-Resort Social Assistance?

Some last-resort social assistance programs in the region may contain some inadvertent disincentives to work. Existing evidence as to whether recipients become dependent on transfers and experience disincentives is mixed. Design features such as the exclusionary filters regarding labor market participation, the weak or absent work availability test, the very broad definition of those who are not expected to work, and the unlimited duration of benefit receipt, along with price effects (marginal tax wedges), introduce potential disincentives for able-bodied adults. Disincentives for formal work could also be associated with the benefit formula which discounts each additional amount earned from the benefit amount due. Work disincentives could potentially diminish benefit generosity. However, except in the case of Montenegro, benefit levels do not seem to be so generous as to create major disincentives for able-bodied adult beneficiaries to substitute inactivity for labor.

Administrative data provides complementary evidence on relative benefit size. It indicates that benefits in the Western Balkan last-resort programs, with the exception of the Montenegro family assistance benefit, are set at sufficiently low levels to make it unlikely that they create disincentives to work. Moreover, in the analysis above, we compare the benefit level for the first member of the unit of assistance for a single-member unit of assistance to the benefit levels for larger units. The low benefit level combined with steeply declining implicit equivalence scales used in determining benefit levels for multimember units of assistance leads us to conclude that there are fewer disincentives to work in the Western Balkan last-resort programs than in most OECD and EU member states. Montenegro is an exception. The benefit level there is above the minimum pay standard for low-skilled laborer after tax. Moreover, eligibility for last-resort social assistance in Montenegro is associated with up to ten additional rights to benefits and services (health coverage, child allowance, electricity subsidy, and other provisions) making it even more generous. To curtail this effect, able-bodied persons with no dependent children are made ineligible for the benefit.

Evidence of marginal taxation on earnings has been obtained[9] for three Western Balkan countries—BH (each entity), Serbia, and FYR Macedonia (Table 13.5). As discussed in the Serbian case presented in Chap. 9, this research reveals that people working in low-skilled, low-paying jobs have a fairly high tax wedge on their earned incomes, which is likely to give them a disincentive to graduate from social assistance into full-time work. Compared with the situation in the OECD and EU countries for which similar data is computed regularly, the tax wedge in FYR Macedonia and the RS is at the low end of the spectrum, while the tax wedge in Serbia and the

[9] Calculated using the OECD tax-benefit model, see Annex 5.

Table 13.5 Tax wedge at various levels of the average wage in BH, FYR Macedonia, and Serbia (%, 2008)

	Bosnia and Herzegovina	FYR Macedonia	Serbia
Tax wedge for single earner with no children			
33% of average wage	37.8 (FBH) 31.1 (RS)	28.5	36.7
50% of average wage	39.5 (FBH) 32.8 (RS)	30.9	38.0
100% of average wage	41.8 (FBH) 34.5 (RS)	33.2	39.3
Tax wedge for one-earner couple with two children			
33% of average wage	37.8 (FBH) 30.6 (RS)	28.5	36.7
50% of average wage	37.8 (FBH) 30.6 (RS)	30.9	38.0
100% of average wage	37.9 (FBH) 33.0 (RS)	33.2	39.3

Source: OECD tax and benefit model. World Bank (2011c)
Notes: The tax wedge is defined as the share of income tax and social security contributions by employers and employees over total labor costs. The numbers presented in this table refer to a one-earner couple with two children who receives average wage and works 33 or 50% part time or full time. Alternatively, in most, though not all, countries this can be interpreted also as the tax wedge of a one-earner couple with two children, working full time, but receiving 33, 50, or 100% of average wage. In the latter case, working full time at 33% of average wage might be below the legal minimum wage. Values refer to 2009

FBH is considerably higher than the median. The gap between the tax wedge on low wages (33% of the average wage, which is used as an approximation of a minimum wage) and the full average wage in the Western Balkan countries is narrower than in the comparator countries. This implies that there are fewer incentives to move out of welfare and into work when the job is a low-paying one.

Long-term reliance on social assistance is reinforced by the very weak or virtually absent coordination of cash transfers with social care services, and by a failure to address in a holistic way multiple vulnerabilities of those who can work. Services in support of employment are not integrated with cash social assistance and the social care services. Provision is separated institutionally, with employment offices/public employment services covering work-related activities while social assistance is provided by the CSW, although both offices often work with the same clients. Case management for job brokerage and employment is separate from the case management for social assistance (income smoothing). The concept of "one-stop shop" delivery has not yet been yet embraced, and only Serbia is piloting models aimed at linking social assistance to activation. The only formal institutional linkage between the employment services and CSW is exercised through the mandatory registration of unemployment. The data exchange between the CSW and the employment services is sporadic with real-time connectivity and reciprocal access to databases unavailable. The able-bodied beneficiaries of social assistance are rarely treated with activation policies and even more rarely sanctioned for not taking offered jobs or training. The scope of application for work tests/workfare requirements is extremely limited due to the lack of institutional capacity, notably with respect to human and financial resources. Concurrently, the supply of active

labor market programs which are specifically targeted at activation of hard-to-serve individuals such as the long-term unemployed and those on social assistance is limited for the same reasons.

A Roadmap for Reforms

In the aftermath of the first wave of the global crisis and in anticipation of new challenges, the Western Balkan countries face enormous fiscal pressures. Demand for social assistance, which might increase following persistent high unemployment, will have to be met with a reduced fiscal envelope. Increased cost-effectiveness of spending is vital. Maintaining effective protection will require measures that make benefits more flexible and responsive to crises and policy shocks; incentive compatibility, so that those who are capable of working are motivated to do so; and policies that make receipt of benefits conditional on using social, health, education, and job search services.

The last-resort programs in the Western Balkan countries need to build on the existing foundations of social assistance by undertaking a number of measures to make these benefits more *equitable, efficient, and transparent*. Among the requirements:

1. *Increasing coverage of the poor and the poorest quintile*, by (a) protecting and even increasing spending on means-tested programs, particularly those programs with very good targeting accuracy, and shifting spending away from categorical programs; (b) decreasing errors of exclusion by modifying eligibility criteria; and (c) introducing smart design features that reduce work disincentives (see 3 below), but provide last-resort benefit coverage to the working poor.
2. *Strengthening and standardizing eligibility criteria using a continuous (nonbinary) scoring formula*. In economies with a significant informal sector, the income tests do not work well. They need to be supplemented by additional information on the applicant's poverty status. The application of filters on top of (weak) means testing results in significant distortions (errors of exclusion and possible disincentives for work) and suffers from non-transparent relative weighting across eligibility criteria. We recommend the standardizing and improving of eligibility criteria by (a) eliminating the use of binary filters and (b) strengthening means testing[10] using a single continuous scoring formula that incorporates objective weights and variables that are empirically associated with poverty status. This formula could be adapted for urban (non-farming

[10] It is interesting to note that there is a complete disconnect between the poverty line in a particular country and the income threshold for eligibility for the last-resort social assistance program in that country. Setting eligibility thresholds closer to the poverty line (or to a relative poverty line) can further assist in the LRSA program achieving its goal of protecting the chronic poor—such linking of eligibility thresholds and poverty lines will also address some of the concerns related to regularly indexing the thresholds to price inflation.

households) and rural (farming households) areas. This would reduce errors of inclusion (leakages to the non-poor) and exclusion (the denial of benefits to poor families due to the application of ad hoc filters), lower potential disincentives to work (from the application of binary filters that exclude anyone with labor market participation), and increase transparency in the system (through the use of explicit, objective weights across eligibility variables).

3. *Introducing features to reduce work disincentives*, such as gradual benefit reductions as a recipient's earned income increases. Higher exit thresholds from social assistance, earned income disregards (up to a certain level), and the elimination of binary filters that bar beneficiaries from participating in the labor market are among the reforms required.
4. *Increasing the generosity of the last-resort social assistance* by indexing benefits and eligibility thresholds to price inflation. The generosity of the programs can be further enhanced in some countries by changing the implicit equivalence scales to increase the size of the benefit to large multimember families, which tend to be poorer than smaller families.
5. *Strengthening benefits administration* by (a) automating information systems and creating a national registry of all applicants and beneficiaries; (b) simplifying and standardizing intake and application procedures; (c) increasing the benefit take-up by reducing the financial, time, and psychological (stigma) costs of application; (d) improving monitoring, oversight, and controls to reduce fraud and errors; and (e), to the extent possible, integrating the registry systems for all social assistance benefits (not just last-resort programs) to enable cross-check and to unify benefits management. These improvements would not only increase equity and efficiency, but would also make the system more transparent, thereby helping the government improve accountability to the public.
6. *Improving and streamlining implementation*, even prior to the complete automation of information systems and national registries, by (a) reducing the number of required documents and minimizing the number of documents that have to be submitted for recertification; (b) ensuring that all of the documents required to prove eligibility are provided free of charge and that as much as possible the flow of documents is through administrative channels and do not require beneficiaries to travel extensively to collect and submit these documents; (c) improving the screening for welfare characteristics during the home visits by more structured observations; and (d) increasing outreach efforts.
7. *Strengthening the links between the last-resort social assistance programs and other programs*, such as labor market activation services and other social support services, could enhance the effectiveness of the safety nets in the Western Balkan countries. Guiding social assistance beneficiaries toward other support services could make them more employable (through education and training), connect the poor with available jobs (through job information, job search help, and matching services), and remove other obstacles to work (by providing them with access to other social services or productivity-enhancing schemes). This would also make social policy more coherent, taking it beyond cash handouts and toward providing integrated and proactive support.

The reform of social assistance in the Western Balkan countries is far from over. In keeping with the objective of increasing the efficiency and effectiveness of social protection while staying within a smaller fiscal envelope in the postcrisis environment, the new legislative agenda involves both parametric design changes and more radical steps toward making the safety net proactive and incentive compatible.

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Chapter 14
The Political Economy of Welfare Reform in the Western Balkans

Will Bartlett

Introduction

Various theories have been advanced to explain the emergence and growth of the welfare state in advanced industrial societies. While the context is very different, the perspectives behind these theories can help to inform our understanding of the welfare state in the Western Balkans. One of the most broadly adopted explanation for the rise of the welfare state in the nineteenth and twentieth centuries is the industrialism thesis. Industrial development undermined previous social relations and social capital based on the family and the local community. Industrial workers who migrated from rural communities to anonymous industrial cities became alienated from their communities and lacked social security in the face of social risks such as sickness and unemployment. This provided a rationale for the state to step in to provide social assistance to workers who had fallen on hard times so as to preserve the quality of the labour force during periods of cyclical downturns. The rationale applied both to the advanced capitalist countries of the west and in the industrialising socialist economies behind the iron curtain (Quadagno 1987).

Potential factors who played an important role the spreading electoral franchise and the widening of democracy changed the political culture in the advanced economies. New social groups were able to influence the redistribution of income and wealth through political representation. Democratisation led to the growth of political support for social transfers to lower income groups such as pensioners, the disabled, the sick and lone parents. A general political imperative for greater equality emerged alongside support for measures to reduce extreme poverty and thus correct the inequalising and impoverishing tendencies of the institutions of market-based capitalism, especially in its more liberal form.

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In addition to particular explaining the growth of the welfare state, scholars have addressed the variation of the welfare state accross the advanced capitalist countries. Esping-Andersen (1990) identified three ideal-type models of the welfare state: the Scandinavian, the Anglo-Saxon and the continental European. He explained the variety of welfare regimes on the basis of both historical path dependency and political coalition through the creation of alliances between different social groups.[1] The political factor was seen as crucial in explaining variation in welfare regimes – Some welfare systems were supported by political alliances between the workers' movement and the middle class, others by alliances between workers and peasants. Both have provided the basis for progressive social reforms of different types. The Scandinavian type of welfare regime provides universal flat-rate benefits combined with a second-tier earnings-related social insurance scheme which supports middle-class standards, although it has recently been reformed to provide less generous benefits. The continental European "corporatist" model was also shaped by middle-class interests, but in a rather different way; it provided occupationally segregated social insurance linked to work and employment status with the aim of ensuring middle-class participation and support for welfare reform. In contrast, the Anglo-Saxon welfare state provided services essentially focused on the poor through means-tested social assistance for the poorest social groups combined with modest universal transfers and social insurance plans, with the middle classes covered separately against social risks through private insurance and occupational fringe benefits (Esping-Andersen 1990: 31–32). In practice, real-life welfare regimes display elements of all three ideal types, although in most cases one or other of them is dominant.

An emerging literature on welfare systems in post-communist transition countries has identified a distinct form of welfare regime conditioned by the experience of transition (Aidukaite 2009; Hacker 2009). Aidukaite characterises post-communist welfare regime, as those in which "insurance-based schemes play a major part in the social protection system …; high take up of social security; relatively low social security benefits; increasing signs of liberalisation of social policy …[and] …still deeply embedded signs of solidarity and universalism" (Aidukaite 2011: 218).

Despite this interest in exploring the post-communist model, surprisingly little attention has been paid to the analysis of welfare regimes in the Western Balkans. While reflecting some aspects of the welfare regimes identified in the post-Soviet countries, significant differences have also emerged. Elsewhere large gaps in social insurance, privatisation in some countries of the provision of health and education services and the liberalisation of social policy. The latter is true for Albania and Kosovo. Elsewhere former social insurance systems have been retained alongside relatively high levels of social expenditure in other countries in the region.

[1] Esping-Andersen (1990: 30) contrasted his political coalition model with the "power-resources" model developed by Korpi (1983) and others which focused on the strength of organised labour movements in forcing concessions from the dominant elite of advanced capitalist economies in the form of welfare benefits and poverty reduction outside the sphere of market economic relation.

The Welfare State in Socialist Economies – The Former Yugloslavia

In developing the thesis of industrialisation as a driver of the welfare state, theorists have drawn little distinction between capitalist and socialist forms of industrial society. In reality, the socialist countries which followed the Soviet model of central planning and state ownership developed more comprehensive welfare states than did the capitalist countries, with welfare grounded in a strong commitment to full employment. The type of welfare state that emerged in former Yugoslavia was different again, since it did not make a commitment to full employment even though employment rights were just as strong as in the other socialist countries, and many social benefits were linked to employment status. Titoist socialism also emphasised industrial development and had a strong commitment to social welfare based on social insurance principles, combined with universal health and education systems, the inclusion of minorities and the provision of generous pensions and family benefits.

The origins of the social protection systems in Yugoslavia can be traced back to the pre-communist period of the former Kingdom of Yugoslavia during which a Bismarckian system of social insurance was established. The system covered a range of social risks but excluded the participation of many social groups including individual craftsmen, agricultural workers and peasants. Under the communist regime established after WWII, the system of social insurance was gradually extended as the industrial working class expanded. By 1965, almost half (48%) of the population was covered by social insurance compared to just over one-sixth (17%) before WWII (Vaughan 1965). The system was supplemented by a range of non-contributory cash benefits and benefits in kind mostly available on a universal basis (Posarac 1993). It covered health insurance, disability insurance, pension entitlements and child allowances and was organised on a decentralised basis. With the exception of health insurance, which covered the entire population, the social insurance programmes covered only employees, while professionals such as lawyers, engineers and clergymen could access a voluntary social insurance scheme. Self-employed persons including farmers were eligible to join one of the three voluntary social insurance schemes.

The main contributory benefit was the pension, provided on the basis of age, invalidity or widowhood, at a level related to the contribution record of the beneficiary at the pension insurance fund. The pension scheme was relatively generous. In the mid-1960s, male workers were eligible for a full pension at the age of 55 on condition of having worked for 35 years, while for women the retirement age was 50 on condition of having worked for 30 years. Partial pensions were available depending on conditions of service. Replacement rates were close to 80% for workers in low-income groups and 70% for those in higher income groups. Health care was also provided on a social insurance basis. Almost all the population was covered since workers' health contributions covered family members, and unemployed workers' health insurance contributions were paid by the employment bureau. Owners and employees in the crafts sector and in private agriculture had inferior benefit entitlements, while uninsured people were entitled to a reduced package of health-care entitlements.

Non-contributory cash benefits included child benefit, family benefit, maternity benefit, disablement benefit, war veteran's benefit and housing benefit, while education was provided on a universal basis (Posarac 1993). A generous child allowance was available to families, employees and the unemployed with children under 15 years of age. Skilled workers were entitled to the payment from the first day of employment, while unskilled workers became entitled after having completed one year's employment. The allowance was paid at a reduced rate for professionals and self-employed farmers. The benefits were inversely related to family income. The system was financed on the basis of social security contributions paid by employers and by the self-employed. The overall level of contributions in the mid-1960s was set at a rate of about 36% of payroll, with the decentralised nature of the system allowing different rates to be established in different republics and districts.

Workers had extensive employment rights, and job protection meant that dismissal from employment was rare so relatively few were eligible for unemployment benefit. Subsidised low-cost housing, subsidised holidays and subsidised transport were provided by socially owned enterprises to their full-time employees. Larger enterprises in some republics also provided privileged access to health-care services. Utilities such as heating and running water were provided to households at subsidised prices. The maintenance of jobs during the crisis period in the 1980s (real wages in Yugoslavia fell by 30% between 1978 and 1987) was a main element of social welfare.

By the beginning of the 1990s, the cost of providing such an extensive social-welfare regime had become unaffordable, and new legislation was introduced to reform the system. Funding was transferred from local "self-management communities of interest" (an institution which might today be seen as local stakeholder partnerships) to centralised republican funds for family social welfare (Arandarenko 2003: 27). Owing to the growing awareness of poverty, entitlement to social assistance was extended to any family whose income fell below a minimum subsistence level. With the break-up of Yugoslavia, each of the successor states inherited these republic-based welfare systems.

The Drivers of Welfare State Reforms in the Western Balkans

The collapse of the socialist systems brought the issue of welfare system reform to the center of the policy agenda. Yugoslavia's successor states inherited strong welfare regimes based on social insurance combined with in-kind benefits provided by enterprises in which employment rights were protected. Social assistance was provided through a range of family benefits, while universal health and education systems provided comprehensive services mainly free at the point of delivery.[2] In the early years of transition, this system of social welfare remained largely in place in each of the successor states.

[2] In Yugoslavia, prescription charges had been introduced in the health sector in 1966.

Since the welfare system had been decentralised following the changes embodied in the Yugoslav constitution of 1974, its preservation in the successor states did not entail many radical changes other than a centralisation to the level of the newly created states.

Despite the continuity, some changes did occur quickly. One example was the privatisation of social housing which accompanied the enterprise privatisation programmes in the early reformers such as Croatia and Macedonia in the early 1990s. In most of the Yugoslav republics, tenants were given the right to buy socially owned housing at discounted prices. In Croatia almost three quarters of the stock was sold under the Law on the Sale of Apartments, with protection for tenants who could not afford to buy their own apartments. In Macedonia in the early 1990s, almost all the social housing stock was privatised at hefty discounts under the Law on the Sale of Socially Owned Housing. In Albania 98% of the housing stock was privatised following the 1993 Law on Privatisation. Most state-owned apartments within high-rise blocks had been poorly built, and many were in serious need of repair or replacement (CEDB 2004). The maintenance problem became even worse after they were privatised, and many apartments continued to deteriorate (UNECE 2002). In Serbia a Housing Relations Law was passed in 1990, and by the end of 1992, about one-fifth of the stock had been sold. According to one analysis, the properties were sold mainly to "elite members who bought the largest and most desirable housing" (Petrovic 2001: 222). A Residence Law was passed in 1992 which restricted the sales to current tenants, and further discounts were offered. By the end of 1993, almost all social housing had been privatised. Housing privatisation had two political purposes. The first was to ensure a transfer of property to the elite, and the second was to provide a means to build support for the Socialist Party.

Health provision also underwent change. Croatia and Macedonia were the first to introduce reforms in the health sector. At the primary care level, governments in both countries encouraged private sector providers to deliver health services. Similar reforms were subsequently introduced in Bosnia and Herzegovina, Serbia and Kosovo (Simic et al. 2010). At the secondary care level, hospital ownership was transformed from social to state ownership, while privately owned hospitals were established in some countries. The process has gone furthest in Macedonia, where private entrepreneurs have invested in new health facilities and in advanced medical equipment and technology in private hospitals. This has created a two-tiered hospital system, composed of an over-politicised and inefficient public hospital system alongside a modern private hospital system that relies on out-of-pocket payments (Lazarevic and Donev 2012).

Differences between the welfare regimes in the different successor states and Albania have became more pronounced over time. In the advanced capitalist countries, variations in welfare regimes have been explained by a combination of (1) path dependency implied by different historical experiences, (2) differences in the transition to industrial societies and (3) the nature of the political coalitions which were established to manage the transitions, typically dominated by a strong middle

class (Esping-Andersen 1990: 32). Similar factors define differences in the paths of transition from socialism to capitalism in the Western Balkans and can be seen to account for differences in welfare regimes in this region.

Path Dependency

Esping-Andersen argued that the historical legacy of a welfare regime is difficult to overturn due to the existence of path dependency; accumulated rights in a welfare system develop over time and cannot simply be abolished (Esping-Andersen 1990). This is probably the reason why Kosovo is the only example from former Yugoslavia in which the dominant model of welfare is based on a universal entitlement to social assistance and flat-rate non-contributory pensions: the records of entitlement were simply destroyed or disappeared during the 1999 war, and the welfare system had to be built from scratch. In the other successor states of Yugoslavia, many of the pre-existing entitlements to social insurance and other aspects of the social welfare systems have been maintained, although their form has been modified over time. For example, radical reforms have been introduced to pension systems in Croatia and Macedonia, but not in Bosnia and Herzegovina, Montenegro or Serbia (Bartlett and Xhumari 2007). Albania is another case of rupture with the previous system (although in a different direction to that in Kosovo) the country having experienced the wholescale replacement of universal social welfare provision based on full employment under centralised state socialism by a system of comprehensive social insurance for those employed in the formal sector. The social insurance system in Albania was established for the first time in 1991 together with a residual means-tested and targeted system of social assistance for those not covered by social insurance.

Social insurance schemes have thus been preserved or newly established although the specific nature of their effects and benefits has changed over time. Pension rights have been altered through parametric changes. Retirement ages have been increased, especially in the aftermath of the global economic crisis, and the generosity of pension schemes has been reduced. New private pension pillars have been established in Croatia, Macedonia and Kosovo. Health insurance has been made more restrictive through periodic changes in entitlements. Meanwhile a new private health sector has emerged in some countries, catering to the elite higher income earners and successful entrepreneurs and professionals, as well as to highly placed public sector bureaucrats and politicians. Sickness insurance benefits have been preserved, but eligibility conditions and medical authorisation regimes have been adjusted in some countries. Unemployment insurance benefits remain pitifully low, and their scope has even been reduced in terms of eligibility and generosity in the face of moves to encourage and develop active employment policies. Employment protection legislation has been reformed in an attempt to reduce even further the rights of workers to stable employment, and to any residual welfare benefits attached to employment status.

Transition to Capitalism and Deindustrialisation

Wars and conflicts, as well as transitional recessions, have led to a process of deindustrialisation in several Yugoslav successor states. To some extent this has thrown the development of the welfare state in these countries into reverse. Unemployment has increased and employment rates have fallen even more dramatically with low levels of economic activity. Reduced rates of labour force participation reflect not only discouraged worker effects but also the reversion to more patriarchal cultural patterns of social interaction and the return to a more traditional role for women in the family. During the transition, therefore, some welfare measures were abandoned as deindustrialisation took hold. One early casualty was the provision of family benefits such as free kindergartens which had often been linked to enterprises and which disappeared when the enterprises were privatised. As indicated above, another early reform in almost all the successor states of former Yugoslavia was the privatisation of public housing. Migration has also played a role. Unemployment, especially high youth unemployment, encouraged migration which became a widely used means of avoiding poverty in both the Yugoslav successor states, where it had been widespread in the former socialist system, and for the first time in Albania. The large inflow of remittances which these emigrants sent home often exceeded formal social assistance transfers to the poorest sections of the community.

The structure of the economy and the social and class composition of the society also changed as transition progressed. Large-scale structural change and privatisation, combined with wars and conflicts led to the collapse and physical destruction of much of the old industrial base and with it the loss of employment attachment to protected jobs. New jobs were created mainly in the emerging service sector, in small- and medium-sized firms in which workers were unable to defend their employment rights (and in which job-related welfare entitlements were unheard of), and in the informal sector locking even the traditional social insurance provisions. The residual public sector remained the sole source of protected permanent employment, but became increasingly politicised. High turnover of personnel in response to changes in government and political affiliation became a common feature of the public sector employment landscape. Eventually, even a public sector job was not entirely secure. As in the former socialist system, trade unions were weak or absent and failed to organise strongly to defend inherited welfare rights. Unemployment increased in a system in which unemployment benefits were minimal, even though unemployment was not a new phenomenon. As unemployment increased, the social basis of the old welfare system was gradually undermined.

Democratisation

At the same time as deindustrialisation undermined much of the basis of the socialist welfare state based around strong employment rights, the political transition to democratic societies worked in the opposite direction by enfranchising social groups who previously had little voice in the one-party socialist systems.

Democratization meant that new political constituencies had to be taken into account for the first time, obliging politicians to pay attention to the demands of specific social groups. War veterans and their families figured prominently in the new political calculus. Other newly enfranchised political constituencies included the unemployed, pensioners and the urban professional elite. The welfare of refugees and IDPs became an important issue, although these groups have been less successful in exerting political influence. The situation and living conditions of ethnic minority groups such as the Roma also dramatically deteriorated in some countries. Under the transition, the position of the middle class declined and policies such as education and life-long learning took a back seat leading to a decline in education expenditure and performance. Migration also led to a brain drain of the most highly educated, reducing the political support of the middle class for universal benefits. In social assistance programmes, categorical benefits have tended to dominate, reflecting the political power of the more powerful sectional interest groups such as war veterans, pensioners and the politicised public sector where access to a formal public sector job often depends on political affiliation. Public sector jobs become an instrument of social policy and a means of redistributing wealth.

Despite the introduction of democracy, there were few political forces motivated to protect or preserve the former welfare system. Often it seemed that only the force of inertia held the system together in the face of the development of new social risks and new pressures for change. The forces which promoted change included prominently the various international donor organisations which assumed a powerful role in policy formation in most countries. However, their influence was limited by a relative lack of coordination and different approaches to policy transfer leading to a relatively inconsistent reform agenda. Since multiple strategies were developed with conflicting aims and objectives, it is hardly surprising that implementation proved to be a major weakness. This led to the appearance of weak administrative capacity which in many cases reflected more the proliferation of conflicting advice and policy inconsistency as much as lack of technical skills and experience. Thus, international advisors everywhere became a prime influence on the nature of welfare state reform (Deacon and Stubbs 2007).

Another prime influence was the nature of political alliances formed in the aftermath of different patterns of transition and conflict which beset the various countries of the region. In several countries, the middle class was either underdeveloped (Albania, Kosovo, Macedonia) or much reduced in size (Serbia, Bosnia, Montenegro) due to migration of skilled professionals and to economic collapse and inflation during the 1990s. Perhaps only in Croatia was sizeable middle class preserved which could form a political coalition with other forces (workers,

peasants and pensioners). In Serbia, the Minister of Labour and Social Policy, Rasim Ljajic, commented that "most people who were not rich in Serbia today were in some way poor" and that "the entire middle class category is gone".[3]

Political support for any welfare systems under transition may come from either winners or losers reflecting the relative strength of new political constituencies for reform. Institutional reforms in transition economies can be seen as the outcome of a policy process which involves a political struggle between pro-reform and anti-reform elite groups and the emergence of political coalitions which have specific interests. There has been a long debate, in the transition literature, about the relative influence of "winners" and "losers" on the transition process. According to one account, the potential losers from the transition process are likely to resist reform and confront reformers with severe political constraints (Roland 2000). The losers, including workers thrown out of their jobs as a consequence of privatisation and restructuring, may be mobilised into opposition to reform by members of the old elites, including managers of state-owned enterprises and the top echelons of the security establishment who prefer the status quo to radical reform. In order to minimise this opposition to reform, pro-reform leaders should ensure that economic reforms are accompanied by appropriate social measures. The creation of a social safety net to compensate vulnerable groups for their losses is one of such measures (Kramer 1997).

Another view holds that it is the winners who are the most dangerous opponents of reform progress (Hellman 1998). The winners are the new elites who gain from the early stages of reform. They include managers of large privatised enterprises, politically well-connected tycoons who gained privatised assets at bargain prices, media barons and directors of public institutions who owe their positions to political connections and political leaders who represent these groups. According to this view, in a partially reformed economy, new elites establish monopoly positions that provide opportunities for rent seeking, and they strive to prevent further reforms that would undermine their new privileges.

Another source of political support for welfare regime change emerged with the rise in some countries of coalition parties (Serbia, the Federation of Bosnia and Herzegovina) and the creation in others of de facto a two-party system (Croatia, Macedonia, Albania). Two-party systems with dominant parties in power for extended periods of time were in position to pursue more consistent changes to the welfare regimes. For example, pension reforms were pushed through in Croatia and Macedonia, while welfare state reforms proved far more difficult in Serbia and Bosnia. In Albania, an entirely new social insurance system was introduced early on in the transition.

What, then, were the sources of support for new non-contributory social assistance schemes in the Western Balkans? Despite the growth of mass unemployment and poverty, no countries have introduced social assistance schemes that have been

[3] Bojana Barlovic, "Serbia's 'social map' reveals extent of poverty", Balkan Insight, 22/4/2011.

anything other than residual means-tested arrangements with little impact on poverty reduction. In Albania, a means-tested social assistance programme known as *Ndihme Ekonomika* was introduced in 1993 for urban families with no independent source of income and rural families with only small plots of land. In 2005 only one-third of poor households were reached by the programme (World Bank 2007: 59). The scheme is decentralised to local authorities, and the benefit is often distributed on a political basis.[4] In Bosnia and Herzegovina, the poverty impacts of non-contributory social assistance benefits are small, accounting for just a 6% reduction in the poverty headcount (World Bank 2009a: 45). Moreover, the benefits are targeted predominantly to veterans of the 1990s civil war. Veteran-related benefits, amounting to 4% of GDP, are highly unequal and regressive, with just one quarter of transfers going to people in the richest quintile compared to less than 15% for poorest quintile (World Bank 2009a). Despite the high expenditure on non-contributory transfers, the coverage of these benefits is low. The share of the population receiving non-contributory social assistance transfers is 15.1% among the poorest quintile, compared to 10% among the richest quintile (World Bank 2009a: 42). These outcomes reflect the fact that the coverage of categorical war veterans' benefits is greater than for means-tested civilian benefits. Moreover, the targeting is regressive.

In Kosovo, the non-means-tested social assistance scheme is rather more successful in targeting the most vulnerable with 78% of the funds going to the poor, and 50% to the poorest quintile. Social assistance is provided to categories of households with no employed members or with a child under 5 years old and one unemployed member. However, coverage is low due to budget constraints, with only 23% of the poor in receipt of social assistance benefits. This is part of a wider pattern across the Western Balkan countries. Although there are variations in targeting efficiency, coverage tends to be low and the provision of benefits to people other than war veterans and their families is limited. Political influence helps to explain the pattern of social welfare payment. While the poor have little political influence. Pensioners have formed their own political parties in Croatia and Serbia. These parties have defended pensioner interests as ageing increases the size of the elderly population and creates pressures to downsize their benefits.

The veterans' infuence has also been a driving force for a particular model of social benefits in post-conflict countries such as Bosnia and Herzegovina and Croatia. In both cases, the strong political voice of veterans' associations has encouraged the development of social assistance in the form of categorical benefits, creating a regime that is only weakly targeted towards the poor. In other countries, social assistance has tended to be quite well targeted towards the poorest income groups, although coverage has been narrow allowing many poor people to slip through the residual social safety nets (World Bank 2009b).

[4] Interview, UNDP, Tirana, 1 June 2010.

Varieties of Welfare State in the Western Balkan Transition

Social expenditure varies in extent throughout the region (Table 14.1).[5] Broadly, the countries divide into a group with relatively high social benefits (Croatia and Serbia), and a group of relatively low spenders (Albania and Bosnia and Herzegovina). Albania has the lowest share of expenditure on social benefits in the region among countries for which this data is available.

Government expenditure on social benefits is complemented by private expenditure, and in some countries, this makes a substantial difference to the consumption of public services such as health and education. Private expenditure on health services is especially high in Albania and Bosnia and Herzegovina, while public health expenditure is correspondingly low. Such private expenditure is not included in reported social benefits. Total government expenditure as a share of GDP as well as social benefit expenditure as a share of GDP is significantly below the corresponding expenditure shares in the EU-27. Table 14.1 also presents data on absolute poverty measured at a level of $5 per day World Bank poverty line. This shows the wide

Table 14.1 Social expenditure and poverty in the Western Balkans (2008–2009)

	General government expenditure as % GDP (2009)[a]	Social benefits as % of GDP (2009)[b]	Private expenditure on health as % of total expenditure on health, 2008[c]	Absolute poverty at $5 per day (latest data)[d]
EU-27	51.0	29.5	–	–
Croatia	41.8	17.0	15.1	2.0
Bosnia and Herzegovina	43.4	14.2	41.8	8.0
Serbia	43.6	19.7	37.5	17.1
Macedonia	33.7	–	31.8	37.0
Montenegro	49.4	–	33.0	49.2
Albania	33.4	10.2	60.6	60.0
Kosovo	29.0	–	–	82.0

Sources: [a]EBRD online data; 2011 and Eurostat online data; Kosovo Medium Term Expenditure Framework, 2011, [b]IMF "Government Financial Statistics", online data and Eurostat online data, [c]WHO (2011) "World Health Statistics", Geneva: World Health Organization, [d]World Bank (2010) The Crisis Hits Home, Washington DC: The World Bank

[5] Here I refer to the concept of social expenditure used by the IMF which refers to social benefits as the sum of all expenditures on social insurance and social assistance, whether in cash or in kind. Government expenditure on social benefits covers health expenditure, family assistance including child allowances, pensions, unemployment benefits, housing benefits and other social transfers. Individual insurance against social risks and individual accounts in private pension funds, whether compulsory or voluntary, are not included in this definition. Social benefits are within the scope of the "economic" classification of government expenditure, whereas social protection falls within the "functional" classification.

range of poverty and, by implication, incomes in the region. Poverty rates measured in this way range from 2% in Croatia to 82% in Kosovo. There is little relation between the level of social benefits as a share of GDP and the poverty rate, although it is notable that the low share of social spending in Albania corresponds to a very high poverty rate.

These expenditure patterns are typical of post-communist welfare regimes with relatively low social spending, despite their adoption of social insurance schemes which characterise the corporatist continental model of welfare. Albania and Kosovo stand apart with extremely low levels of public expenditure and social benefits, relatively high levels of private expenditure on health care, and high rates of absolute poverty.

Among the Western Balkan countries, the level of social spending is highest in Serbia at 20% of GDP reflecting the lack of reforms and the adherence to the former social insurance-based welfare system. Montenegro has a similarly high share of government spending although data on social spending are not available. Croatia also has a largely unreformed system of social welfare based on social insurance principles, and while the reform of the pension system has removed some social spending towards the private sector, the impact on public spending is as yet rather marginal: social spending still represents 17% of GDP. Macedonia exhibits similar characteristics, although data on social spending are insufficient to provide an adequate account. While Bosnia and Herzegovina also provide an example of unreformed social welfare, the level of social spending – 14.0% of GDP – is relatively low. This reflects the limited budget capacity of many of the poorer municipalities in the Federation of Bosnia and Herzegovina and the high level of expenditure on administration in the complex governance system that was set up after the Dayton Agreement. All of these countries could be said to fall into the group of post-communist welfare regimes, characterised by a basis in social insurance and a complementary social assistance scheme.

Albania presents a rather different model of a welfare state regime with significant gaps in welfare provision. Although it has a social insurance system accompanied by a system of residual social assistance, its social spending share is very low at just 10% of GDP reflecting the fact that social insurance covers only a small proportion of the population. According to a recent demographic and health survey, around 70% of the population are not covered by health insurance. Private expenditure on health service is correspondingly high at 60% of total health expenditure (see Table 14.1). In this respect, the welfare state in Albania is essentially based on a residual model of welfare, despite being formally a system based on social insurance. Kosovo is different again, having abandoned social insurance principles in favour of universal social benefits delivered through the flat-rate pension scheme and the non-means-tested social assistance. However, since the level of benefits is extremely low, it has the highest rate of absolute poverty in the region. Both of these states differ in important respects from the standard models of welfare regimes in either Western or Eastern Europe and could perhaps be classified as uniquely Balkan in their approach.

Conclusions: Implications for Welfare Policies

The welfare systems in Western Balkan countries appear to follow the pattern of other post-communist welfare state regimes which have been identified in the literature, although both Albania and Kosovo stand outside this framework. The characterisation of post-communist welfare regime does not fit the latter two cases very well due to the large gaps in the coverage of social insurance and social assistance. Moreover, all the countries of the Western Balkans have adopted hybrid welfare regimes driven by a mixture of the legacy of the previous socialist systems, transition changes and associated deindustrialisation; the specific style of democratisation which has characterised the countries of the Western Balkans; and advice from international organisations accompanied by sometimes coercive policy transfer subject to conditionality clauses (Deacon and Stubbs 2007). This has often given a degree of apparent incoherence to social reforms. The most notable example is pension reform, which has differed depending on the influence of domestic political coalitions and international donor organisations with Croatia, Kosovo and Macedonia adopting partial privatisation and other countries avoiding this step (Bartlett and Xhumari 2007).

In sum, the welfare systems in Western Balkan welfare regimes reflect different driving factors from those which propelled the development of the welfare states in Western Europe or the new EU member states of Eastern Europe. Attempts to impose policy solutions which do not take those factors into account and which do not work with the grain of domestic institutional, structural and political trends and influences are unlikely to be successful.

This chapter has provided a complementary perspective to the other chapters in the book by focusing on the political economy of welfare reform. Understanding the drivers of welfare state reform and the sources of reform resistance can inform realistic strategies to improve the effectiveness of social protection policies. The main message that emerges is that, despite widespread poverty in several countries, there is little political support for social assistance programmes that would increase transfers to the poorest members of society.

The middle class which might have provided the political support for such measures has been reduced by the impact of transition, war and conflict. In industrialised countries, as shown by the work of Esping-Andersen and others, welfare regimes of different types – from Scandinavian to continental corporatist – were driven by the interests of the middle class, as much as by a concern to assist the poorest members of society. In the absence of a politically significant middle class, the political alliances necessary to generate support for comprehensive welfare states are weak or absent. Thus, proposals to scale up the well-targeted social assistance programmes which currently exist in order to improve their coverage and generosity are likely to fall foul of political constraints in the region. The poor have little electoral clout and are vulnerable to nationalist manipulation. In the absence of a supportive middle or entrepreneurial class with an interest in ensuring a wide income base for consumption and growth, the poor have few political allies to press

their case. Arguments in favour of scaling up existing social assistance programmes by improving coverage may seem plausible in theory, but in practice there may be little political support for such measures, nor for transferring expenditure from captured categorical benefits such as those benefitting war veterans towards wider social assistance for the poorest. Instead, a strategy of replacing categorical benefits by some form of universal benefits may have more traction. These could include the provision of improved child allowances[6] and more inclusive vocational and adult education which might be attractive to a relatively wide range of voters encompassing both winners and losers from reform, as well as being at the same time potentially quite effective in supporting poverty reduction in the region.

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Chapter 15
Simulating Policy Reform: Distributional and Poverty Outcomes of the New Social Welfare Law in Serbia

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Introduction

Between 2006 and 2008, Serbia's poverty rate declined by 2.5 percentage points, with the proportion of people living below the absolute poverty line dropping from 8.8% of the population in 2006 to 6.3% in 2008.[1] However, with economic activity declining by 3% in 2009, the number of poor increased to 6.9%, thus reversing the trend. Protecting poor and vulnerable households from the effects of the crisis requires measures to improve access to social benefits and stronger targeting. Improved monitoring and tracking of the demand for social assistance to meet the needs of the new poor emerging with the unfolding economic crisis is also vital. The last-resort social assistance programme (referred to as MOP[2] in further text) has already started, albeit slowly and somewhat inadequately, to act as an "automatic stabiliser" in time of crisis.

In the short term, the government is ensuring that social assistance transfers are not affected by the fiscal spending cuts needed to combat its increasing budget deficit. It managed to protect social spending on programmes from the quite heavy cuts that affected other sectors in 2009 and to pay fully all benefits despite an increasing uptake of the MOP. Over the medium term, the government plans to increase coverage and

[1] These figures are based on a new methodology for poverty calculations from Household Budget Survey (HBS) which now calculates a nutritional basket for 2006 and adjusts it by consumer price index for each consecutive year.

[2] MOP stands for "materijalno obezbedjenje porodice" and translates into English as "material support for low-income households".

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improve the design of the MOP while limiting spending on less efficiently targeted programmes.

The new social welfare law introduced a number of changes into the eligibility criteria for MOP and its implicit equivalence scale. The purpose of the new law is to make MOP more equitable and to link the "passive" cash support to social care and employment services for the poor and vulnerable. As a result, the government expects to increase budget expenditures on social assistance by some 70% (albeit starting from a low base).

This chapter assesses the impact of proposal social welfare law changes on income distribution and poverty outcomes across Serbian households.[3] Estimates are based on micro-simulations conducted using SRMOD, a tax and benefit micro-simulation model for Serbia. The results suggest that the proposed changes in legislation will improve the targeting of social assistance and support for the most deprived members of the society.

This chapter is structured as follow. The next two sections provide an overview of the social assistance policy debate in Serbia and more detailed information on the methodology used to conduct the micro-simulations. We then present simulation results for the effect of all envisaged changes to the social welfare law, associated with the new eligibility criteria, presenting the disaggregated results of micro-simulations by number of children in household, household size and age of individuals. The final section discusses the issue of benefit non-take-up and overpayment.

Policy Background

The MOP is a last-resort poverty gap programme activated only when all other social protection mechanisms are exhausted but the individual or household remains poor. In this sense it is a typical minimum-income benefit programme of the type found in most European countries. Eligibility is determined by a means test that takes into consideration all earnings of the household except those from other social benefit programmes. The MOP eligibility threshold is determined as a percentage of the average wage and adjusted for household size with a steeply declining equivalence scale.

Public outlays on social assistance programmes for Serbia increased from 1.3% of GDP in 2006 to 1.8% in 2008. However, allocation for the MOP programme from 0.16 to 0.14% of GDP over the same period. As can be seen from Table 15.1, the outlay on MOP is lower than for similar programs in new EU member states.

[3] This chapter presents part of a larger research endeavour financed by the World Bank. FREN's research team was commissioned by the bank to simulate the impact of the new social welfare law on income distribution and poverty outcomes before its adoption by the Serbian parliament. The law was adopted in March 2011.

Table 15.1 Spending on social protection in Serbia and EU new member states (% of GDP)

Country	Total social protection	Pensions	Family and child benefits	Targeted social assistance	Disability benefits
Latvia	12.6	6.1	1.3	0.2	1.2
Lithuania	13.3	6.1	1.1	0.3	1.3
Serbia (2008)	**13.4**	**11.4**	**1.0**	**0.14**	**0.8**[a]
Estonia	13.4	5.8	1.7	0.2	1.2
Romania	14.9	5.6	1.6	0.6	1.0
Slovakia	17.2	6.6	1.8	0.5	1.6
Czech Republic	19.6	7.8	1.6	0.6	1.5
Poland	20.0	11.6	0.9	0.2	2.3
Hungary	20.7	8.6	2.5	0.5	2.1
Slovenia	24.3	10.6	2.0	0.7	1.9

Source: World Bank (2009, p. 57)
[a]War veterans benefits and caregiver allowance

Although underfunded, there is a general consensus (in both academic and policy circles), that the MOP programme is well designed. Targeting compares favourably with other means-tested benefits in the region, and with other targeted cash benefits in Serbia, especially the child allowance. The main shortcomings are low coverage, and low levels of benefits, which limit the poverty alleviation impact of the programme. In a policy note from 2006, the World Bank stressed that reforms are needed to increase the MOP programme within the existing budget envelope for social protection. The analysis showed that there was more room to improve the targeting of the MOP benefit through concentrated outreach by social workers to poor households and better dissemination to potential beneficiaries. Additionally, the policy note warned that targeting based on income was likely to underestimate household welfare when there was high informal employment.

In their analysis of the impact of the current social welfare law, Matkovic and Mijatovic (2009) found extremely low MOP benefit coverage. They argued that, apart from budgetary reasons, the government had opted for social assistance programme because more generous benefits could provide disincentives for work. Additionally, the study pointed out that the then existing rule of limiting MOP receipt for beneficiaries capable of working to 9 months in a year was not achieving its objective of increasing work incentives. During the summer, when there are more opportunities for seasonal work, the number of MOP beneficiaries fall only to rise again as beneficiaries returned to the program. The World Bank (2006) proposed the elimination of the 9-month rule and the introduction of work incentives, including closer links with active labour programmes.

Another drawback of the current MOP programme is an equivalence scale that discriminates against larger households (Matkovic 2010). The equivalence scale is implicit in that benefit amount is determined in nominal terms per household depending on the number of its members. The scale does not differentiate between children and adults, and the presence of every additional member in the household

is valued at steeply declining coefficients. In 2009, a two-member household was receiving 1.37 of the MOP amount for one-member household; a three-member household, 1.75; and a four-member household, 1.87. Families with five and *even more* members are entitled to two times the MOP amount for single-member family (World Bank 2009).

The new draft law introduced a number of changes. First of all, a new implicit equivalence scale was introduced which accounted for children and adults within a household differently, assigning 100% of the basic MOP amount to the first household member, 50% for each additional adult and 30% for each child under 18. Moreover, MOP eligibility criteria was relaxed for large families, so that households would be entitled to social assistance for a larger number of their members. The old law allowed social assistance to be paid out to a maximum of five household members, while the change lifted the threshold to six members. The access of families (households) from rural areas to MOP will be improved by a provision relaxing the land ownership eligibility condition from 0.5 to 1 ha per unit of assistance. Finally, single-parent households and households in which all members are incapable of work will be entitled to higher amounts of social assistance.

Data and Methodology

During the last decades, public economics literature has developed very useful tools to analyse and evaluate the equity and efficiency effects of tax and social benefit reforms. Theoretical analysis has experienced substantial progress with the appearance of the Mirrlees model of optimum taxation. This model provides a framework for identifying the elements that determine the effects of direct taxes and cash benefits on equity and efficiency. At the same time, development of the tax and benefit micro-simulation models and the labour supply models has facilitated high-quality empirical research (Atkinson 2009).

To evaluate the effects of social assistance benefit reform on poverty and inequality, we use the tax and benefit micro-simulation model for Serbia (SRMOD), which is based on the EUROMOD platform.[4] Like other tax-benefit models, SRMOD operates on micro-data for a representative sample of household, within the population to be observed. The Living Standards Measurement Survey (LSMS) from 2007 is currently used as the SRMOD dataset. This dataset was chosen since it includes detailed

[4] EUROMOD is the tax and benefit micro-simulation model for the European Union, developed and maintained by the micro-simulation unit of the Institute for Social and Economic Research (ISER), University of Essex. More details are available at http://www.iser.essex.ac.uk/research/euromod. For more details about SRMOD construction, see Žarković-Rakić (2010).

Table 15.2 Main income concepts in EUROMOD

Original income (employment and self-employment income, income from agriculture, income from capital, income from property (rent))
+ *Social benefits* (family benefits, pensions, unemployment benefit, social assistance benefits, housing benefits)
– *Social insurance contributions* (employee, self-employed)
– *Personal taxes* (income and other direct taxes)
= Disposable income

Source: Paulus et al. (2009)

information both on various sources of income and on paid taxes and claimed benefits.[5] This allows micro-validation (comparison of simulated and real values of benefits at the household level) to be conducted with greater accuracy, thus enabling a more reliable estimate of the model's conformity with the actual tax system and benefit policy. Using elements of income from the survey data and combining them with simulated taxes and benefits, the model calculates disposable income for each household (see Table 15.2).

The basic SRMOD output therefore consists of information on changes in disposable income of households after specified policy reforms are introduced. The model shows the distribution of the household disposable income and the tax-benefit component income by deciles.[6] Additional statistics provided in the model include the percentage of people below the poverty line (headcount ratio) for the overall population and for selected groups and the Gini coefficient for equivalent initial income and disposable income.

As well as calculating the effects of actual policies, SRMOD, like other microsimulation models, is also used to evaluate the effects of tax and benefit policy reforms on poverty, inequality, incentives and government budgets. The model can be used to analyse the distributional and poverty effects of the social assistance benefit reform, envisaged in the new social welfare law before its adoption by the Serbian parliament.

Since the baseline tax-benefit policy year (2007) and income data reference period are the same, there was no need for income uprating in the database. The only modification to the original dataset was net-to-gross imputations. Since the original dataset recorded incomes net of taxes, we performed tax-benefit calculations in order to compute gross incomes. Additionally, it was important to distinguish in the database those persons working in the formal economy from those working in the informal labour market. This avoided any overestimation in the simulated values for income tax and social security contributions, while capturing the earnings of those working in the informal economy.

[5] For example, in the LSMS, the receipt of social assistance, unemployment benefit and maternity leave benefit is reported separately, whereas in the Household Budget Survey, there is only one question regarding the receipt of these three benefits.

[6] Decile groups are formed by ranking according to equalised household disposable income using the modified OECD equivalence scale and weighted by household size.

Simulating Changes to Social Assistance (MOP) Rules

In this section, we focus on how the disposable income of households in the two bottom income deciles is theoretically affected when they become eligible for MOP, under the new rules by comparison with the situation under the old rules. This comparison is conducted under the assumption that each household fulfils the eligibility criteria, fully recovers the cost of obtaining it[7], and actually receives MOP transfers. Therefore, we present results on the theoretical maximum of MOP beneficiaries, without fully accounting for non-take-up. Determining the full extent of non-take-up, which frequently depends on other unobservable household characteristics-such as the stigma of being poor, inability to understand complicated administrative procedures, or lack of information on the programme- is difficult to model and simulate as we show below.

The following changes to MOP rules in the social welfare law were simulated in SRMOD:

- Introduction of the new equivalence scale
- Increased ceiling for eligible household members from 5 to 6
- Increased MOP payments for single-parent households with one or two underage children
- Increased MOP payments for households in which all members are incapable to work
- Raised ceiling on land ownership for those households in which all members are incapable to work from 50 to 100 ares
- Increased number of incapable of work for those in education from 19 to 26 and those on maternity leave

The baseline household disposable income used in simulations includes all sources of income but MOP, so we refer to it as pre-MOP disposable household income. Disposable household income is calculated as shown in Table 15.2.

The first part of this section presents the overall distribution of those households and individuals eligible for MOP across income deciles as well as the amounts of MOP they should receive. It also throws light on some of the fiscal impacts of the new law on social welfare. The second section assesses the impact of the changes in the legal framework to the income and poverty outcomes of eligible households. Subsequent sections provide disaggregated data accounting for the number of children in households, household size, and age of household members.

[7] We estimate the cost of claiming MOP at 1,000 RSD (Serbian national currency). See section "Issues of MOP Non-take-up and Overpayment" of this chapter for explanation.

Table 15.3 Main results of SRMOD simulation analysis

	Number of eligible HHs	Total fiscal expenditures on MOP, in RSD
Old MOP criteria	53,444	274,347,719
New MOP criteria	65,272	369,404,612
Percentage increase	22.1%	34.6%

Note: RSD is the national currency; exchange rate amounts to around RSD 100 for EUR 1
Source: Authors' calculations in SRMOD

Distributional Aspects of Changes to MOP Rules

Based on SRMOD simulations, changes to the MOP eligibility criteria envisaged in the law on social welfare lead to an increase in theoretical MOP coverage by 22.1% (approximately 12,000 households). Total fiscal expenditures on MOP increased by 34.6%, (around 0.05% of GDP), which is equivalent to an increase in the total consolidated government expenditures of 0.1% (see Table 15.3).

These estimates represent a lower bound of the total population in Serbia eligible for MOP. Since the LSMS sample is based on census data, it does not provide information on people living in shanty towns (mostly Roma). Moreover, these data show the theoretical maximum of MOP beneficiaries (which are covered by the census), and do not fully account for benefit non-take-up issues.[8] This is why the number of eligible households (presented in Table 15.3) does not refer to MOP recipients from the LSMS database but instead to the number of households who fulfil all eligibility criteria in the simulation, regardless of whether they take up the benefit or not.

Most of the changes to eligibility criteria in the law affect the minimum income level, or the threshold a household needs to be under in order to become eligible. Most of the households that are eligible under the new rules and were not eligible under the old rules will receive a low level of social assistance. This is because they became eligible mainly as a result of the jump over the threshold level (the law envisages that they receive social assistance only the difference between their disposable income and the minimum income threshold). On the other hand, the changes in the law affect those who were already eligible for MOP to a greater extent by changing the level of social assistance they receive (again as a consequence of changes in the income threshold).

Viewed in aggregate, the changes in eligibility criteria has increased the amount received by most households (36,186 or 55.4%) which were eligible under both old and new rules. There has been a negative change in the amount of MOP received by

[8] See Chap. 6 for a more detailed discussion on the original recipients of MOP from the LSMS database and their comparison to administrative records of the Ministry for Labour and Social Policy.

Table 15.4 Main results of SRMOD simulation analysis, detailed

		Number of HHs	Distribution of total eligible HHs—new rules	Average increase in amount of MOP per ae. (in RSD)	Average MOP amount per ae.—new rules (in RSD)
HHs eligible for MOP under both old and new rules	Negative change in amount received	7,724	11.8%	−162	2,253
	No change in amount received	9,138	14.0%	0	2,340
	Positive change in amount received	36,186	55.4%	769	3,563
Newly eligible households		12,224	18.7%	–	1,622
Total number of eligible HHs under new rules		65,272	100%	–	2,873

Source: Authors' calculations in SRMOD

7,724 households (11.8%), while there was no change in the amount received for 14% of households. The newly eligible households represented 18.7% of all eligible households under the rules from the new law (see Table 15.4).

We next observe how the simulated changes to MOP rules affect the distribution of eligible households across income deciles. Decile cut-offs are based on pre-MOP disposable household income per adult equivalent (based on the new equivalence scale).

Since the number of recipient households in all income deciles, except the first one, is too low, we cannot make statistically reliable conclusions about the distribution of recipient households in deciles 2–10. The results presented in Table 15.5 represent a condensed and a more statistically reliable version of distribution of MOP recipients across deciles. Of the total number of eligible households according to old MOP eligibility criteria (53,444 households), 43,468 belong to the first income decile, while 9,976 households belong to other deciles. According to the simulation scenario which includes new MOP rules, there is an increase of 8,021 recipient households in the first decile, whereas there are 3,807 new eligible households in deciles 2–10 (see Table 15.5).

The 2007 LSMS results show the incidence of poverty in Serbia at 6.6%. We look beyond those below the poverty line to the poorest 10% of the population. For this purpose, we split the poorest decile into two parts: the poorest 5% of the population, households between the 5th and the 10th percentile of the income distribution.

How does MOP coverage vary across the income distribution? We address this question in the light of eligibility criteria.

Out of total 241,477 households which belong to the first income decile, only 18% fulfil all criteria to receive MOP under the old law, while 21.3% of them meet

Table 15.5 Distribution of HHs eligible for MOP across deciles

Income deciles	Total HHs in population	Eligible HHs under old MOP rules	Eligible HHs under new MOP rules	Increase in eligible HHs
1	241,477	43,468	51,489	8,021
2–10	2,161,317	9,976	13,783	3,807
Total	2,402,794	53,444	65,272	11,828

Note: Decile cut-offs are based on pre-MOP disposable HH income per adult equivalent, based on the new equivalence scale
Source: Authors' calculations in SRMOD

Table 15.6 Distribution of eligible HHs, within the 1st income decile

	Total number of HHs in population	Eligible HHs under old MOP rules	Eligible HHs under new MOP rules	Increase in eligible HHs
1st–5th percentile (1st ventile)	119,814	28,724	31,406	2,682
5th–10th percentile (2nd ventile)	120,394	14,744	20,082	5,339

Note: Decile cut-offs are based on pre-MOP disposable HH income per adult equivalent, based on the new equivalence scale
Source: Authors' calculations in SRMOD

Table 15.7 MOP coverage across deciles

Income deciles	Total number of HHs in population	HH coverage by old MOP rules	HH coverage by new MOP rules
1	241,477	18.0%	21.3%
2–10	2,161,317	0.5%	0.6%

Note: Decile cut-offs are based on pre-MOP disposable HH income per adult equivalent, based on the new equivalence scale
Source: Authors' calculations in SRMOD

the new criteria (see Table 15.7). Therefore, the change in MOP rules which we simulate leads to a 3.3% increase in MOP coverage for the poorest income decile.

Further analysis of the first income decile indicates that the share of households eligible for MOP who are in the lowest income ventile is double compared those in the second ventile. With the change of MOP rules, coverage increases by around 2.2 percentage points for the first ventile and 4.5 percentage points for the second ventile.

The new law on social welfare also increases the average amount of MOP assigned to eligible households. We observe an increase of 10.6% in the average monthly amount of MOP per adult equivalent paid out to the first income decile and a 15.1% increase for other deciles, albeit both from a low base (see Table 15.8).

For comparative purposes, the net minimum wage in May 2007 (when LSMS was conducted) amounted to the 12,133 RSD. The minimum wage averaged around 40% of the average wage between 2001 and 2008.

Table 15.8 Average MOP payments across deciles

Income deciles	Old MOP rules		New MOP rules		Increase in average MOP payments
	Number of individuals in eligible HHs	Average MOP payment	Number of individuals in eligible HHs	Average MOP payment	
1	158,177	2,684	18,694	2,969	10.6%
2–10	38,337	2,186	49,699	2,515	15.1%
Total	196,514	2,591	23,664	2,873	10.9%

Note: Average MOP payments represent monthly payments per adult equivalent (new equivalence scale) in RSD
Source: Authors' calculations in SRMOD

Observed in greater detail, within the first income decile, an increase of 13.3% in the average amount received per adult equivalent can be expected among the lowest 5% of income earners, while there is an increase of 6.3% for those in the second ventile. When we apply new MOP rules, the difference between the average nominal amount per adult equivalent paid out to individuals in the first and second ventile increases, in favour of the first ventile. This indicates better calibration of MOP under the new rules.

Income and Poverty Outcomes of Changes to MOP Rules

This section discusses income and poverty outcomes related to changes in MOP rules, focusing on for average disposable income per adult equivalent for each income decile. As expected, MOP represents a significant source of income only for the poorest decile of the population. The share rises further for the bottom 5% of the income distribution. The new rules do increase the overall average significance of MOP in household disposable income.

When the poverty line is set at the 5th percentile of the income distribution introduction of new rules triggers a relative decrease in the number of poor, by almost 3.4% in comparison to the scenario for the old rules. However, the poverty index and poverty gap do not change (see Table 15.10).[9]

Setting the poverty line at the 10th percentile of the income distribution, the new MOP rules decrease the number of poor by approximately 15,000 or 2.15% (see Table 15.11).

[9] Since the analysis undertaken here represents the theoretical maximum of the beneficiaries, i.e. non-take-up is not entirely accounted for, it is more relevant to observe the relative changes in the percentage of poor when new eligibility criteria are introduced, rather than the absolute numbers.

Table 15.9 Average disposable income

Income deciles	Average disposable income per adult equivalent			Percentage change in disposable income, old MOP vs. new MOP
	Before MOP	After MOP (old rules)	After MOP (new rules)	
1	3,849	4,333	4,482	3.46%
2	8,855	891	8,939	0.32%
3	11,787	11,797	11,813	0.13%
4	14,645	14,664	14,673	0.06%
5	17,393	17,393	17,393	0.00%
6	2,028	20,286	20,286	0.00%
7	23,349	23,349	23,349	0.00%
8	27,825	27,825	27,825	0.00%
9	34,324	34,324	34,324	0.00%
10	56,832	56,832	56,832	0.00%

Note: Average disposable income is expressed per adult equivalent (new equivalence scale) in RSD
Source: Authors' calculations in SRMOD

Table 15.10 Basic poverty indicators, poverty line at 5%

	Before MOP	After MOP (old rules)	After MOP (new rules)
Number of poor	37,055	285,118	275,431
Poverty index	5.0%	3.8%	3.7%
Poverty gap	2.1%	1.4%	1.4%

Note: Poverty line is set at the 5th percentile of the income distribution, where income is disposable income per adult equivalent before MOP
Source: Authors' calculations in SRMOD

Table 15.11 Basic poverty indicators, poverty line at 10%

	Before MOP	After MOP (old rules)	After MOP (new rules)
Number of poor	74,078	714,826	699,442
Poverty index	10.0%	9.6%	9.4%
Poverty gap	4.5%	3.8%	3.6%

Note: Poverty line is set at the 10th percentile of the income distribution, where income is disposable income per adult equivalent before MOP
Source: Authors' calculations in SRMOD

Simulation Results Disaggregated by Number of Children in Household

This section endeavours to throw more light on the distributional and poverty outcomes of changes in MOP rules, when some specific household characteristics are taken into account.

Table 15.12 HHs eligible for MOP, by number of children

Number of children in HH	Eligible HHs		Percentage increase in eligible HHs
	Old MOP rules	New MOP rules	
0	21,489	2,818	31.1%
1	11,771	13,775	17.0%
2	9,892	11,922	20.5%
3+	10,292	11,395	10.7%
Total	53,444	65,272	22.1%

Source: Authors' calculations in SRMOD

Table 15.13 Average MOP payments, by children in HH

Number of children in HH	Average MOP payments per ae. (in RSD)		Percentage change in amount received
	Old MOP rules	New MOP rules	
0	2,790	3,197	14.6%
1	2,464	2,698	9.5%
2	2,656	2,538	–4.4%
3+	2,260	2,634	16.6%
Total	2,591	2,873	10.9%

Source: Authors' calculations in SRMOD

The introduction of new MOP criteria favours households without children (Table 15.12). These households mostly consist of elderly members . It seems likely that the increase in their coverage was influenced by the loosening of eligibility conditions for households in which all members are incapable to work (see Table 15.12).

Households with three or more children as well as those without children, receive the highest increase in MOP payments under the new rules, while those with two children experience a decline (see Table 15.13).

The new equivalence scale reduced the average amount of MOP received by households with children because a smaller weight is assigned to each child (although this decrease is not that significant on average). However, the average amount received by households with three or more children still increases with new MOP rules because more children become eligible for MOP. The new rules increase the number of eligible household members from five to six. Moreover, it is likely that average amounts received by households with one child have increased with the increase in entitlements of single-parent households.

When the poverty line is set at the lowest 10th percentile of the income distribution, the most vulnerable are households with three or more children. Poverty numbers in this category also decreased the most with changes in MOP rules, by 7.1%, when poverty line is set at the 10th percentile (see Table 15.14).

Table 15.14 Poverty index by children in HH

Number of children in HH	Poverty index			Decrease in the number of poor, old MOP vs. new MOP
	Before MOP	After MOP (old rules)	After MOP (new rules)	
0	8.8%	8.4%	8.2%	2.1%
1	10.8%	10.9%	10.8%	0.9%
2	9.6%	9.1%	9.0%	1.1%
3+	18.1%	16.8%	15.6%	7.1%
Total	10.0%	9.6%	9.4%	2.2%

Note: Poverty line is set at the 10th percentile of the income distribution, where income is disposable income per adult equivalent before MOP. The percentages in the table represent the ratio of total number of poor living in these households and the total number of people living in these households
Source: Authors' calculations in SRMOD

Simulation Results by Household Size and Age Categories

Households with one and six and more members are over-represented within the first two deciles of the income distribution, compared with the general population. In absolute terms, most poor households have one, two and four members. The new MOP rules lead to by far the greatest increase in eligibility for households with three members (40.2%), followed by those with two members (24.8%) (Table 15.15).

The largest increase in the average MOP amount received per adult equivalent when new criteria are introduced takes place in two-member households (22.4%), followed by households with six or more members (16.6%) (see Table 15.16). The reduced average amount of MOP for three-member households is the result of a larger than average increase in eligibility of these households (see Table 15.16). Newly eligible households, in this category, were closer to the minimum income threshold, so, the difference between their disposable income and the income threshold, which determines the size of the transfer, is lower than average.

Household numbers influence the risk of being in poverty. Most vulnerable to poverty are those households with seven or more members, followed by one-person households. After new MOP rules are introduced, we observe the largest percentage point decrease in poverty among households with two members (6%) and those with seven or more members (6.6%). Note that these results relate to a simulation that sets the poverty line at the 10th percentile of the income distribution (see Table 15.17).

Finally, we present the results of our simulations factoring in the age of MOP recipients. When we observe the distribution of individuals by their age in the entire population, the highest incidence of poverty by age groups occurs among children (under 18 years of age).

Table 15.15 HHs eligible for MOP, by HH size

Number of HH members	Eligible HHs		Percentage increase in eligible HHs
	Old MOP rules	New MOP rules	
1	8,580	10,017	16.8%
2	9,209	11,494	24.8%
3	8,493	11,906	40.2%
4	10,859	12,839	18.2%
5	7,515	8,707	15.9%
6+	8,789	10,309	17.3%
Total	53,444	65,272	22.1%

Source: Authors' calculations in SRMOD

Table 15.16 Average MOP payments, by HH size

Number of HH members	Average MOP payments per ae. (in RSD)		Percentage change in amount received
	Old MOP rules	New MOP rules	
1	3,378	3,896	15.3%
2	2,944	3,604	22.4%
3	2,264	2,107	–6.9%
4	2,542	2,700	6.2%
5	2,316	2,584	11.6%
6+	2,067	2,409	16.6%
Total	2,591	2,873	10.9%

Source: Authors' calculations in SRMOD

Table 15.17 Poverty index by HH size

Number of children in HH	Poverty index			Decrease in the number of poor, old MOP vs. new MOP
	Before MOP	After MOP (old rules)	After MOP (new rules)	
1	11.9%	11.2%	11.1%	0.7%
2	9.5%	8.9%	8.4%	6.0%
3	7.4%	7.2%	7.2%	0.0%
4	11.7%	11.4%	11.3%	0.7%
5	8.9%	8.5%	8.3%	2.9%
6	8.8%	8.8%	8.8%	0.0%
7+	14.2%	14.2%	13.3%	6.6%
Total	10.0%	9.6%	9.4%	2.2%

Note: Poverty line is set at the 10th percentile of the income distribution, where income is disposable income per adult equivalent before MOP. The percentages in the table represent the ratio of total number of poor living in these households and the total number of people living in these households. Source: Authors' calculations in SRMOD

Source: Authors' calculations in SRMOD

Table 15.18 Number of MOP recipients, by age

Age category	Number of eligible individuals		Percentage change in eligible individuals
	Old MOP rules	New MOP rules	
Children (0–17)	71,185	81,436	14.4%
Working age (18–64)	109,095	129,083	18.3%
Elderly (65+)	16,235	2,612	60.9%
Total	196,514	23,664	20.4%

Note: The total number of eligible individuals represents the total number of people in households which receive MOP
Source: Authors' calculations in SRMOD

When we look at the changes in the number of MOP beneficiaries by age, the largest increase in number of eligible individuals is among the 65+ age group (60.9%) (see Table 15.18).

Under the new rules, the largest increase in the average amount received per adult equivalent is among the working age population (12%) (see Table 15.19).

A more detailed account of "losers" and "winners" from the changes in eligibility criteria by age groups shows that, the biggest beneficiaries are the children with 61.8% of eligible children receiving more MOP. However children are also the most adversely impacted, due to the changes in the equivalence scale (20.7% of children receive less MOP). The largest increase in eligibility (39.4%) occurred among elderly most likely due to the relaxation of the ceiling on land ownership for those incapable of work.

Age-related poverty outcomes of changes in MOP rules, when poverty line is set, at the 10th percentile of the income distribution, are significant. The largest positive impact was observed among the elderly (4% decrease) and children (3.4% decrease), while the smallest impact is on the working age population (1.4%) (see Table 15.20).

Issues of MOP Non-take-up and Overpayment

Database Caveats and Non-take-up of MOP

The baseline dataset used for SRMOD was the 2007 LSMS.[10] As we can see from Table 15.21, receipt of MOP is under-reported in the LSMS. In June 2007, according to official administrative records, 48,954 households received MOP, which is 29.3% higher than the number of households which were MOP beneficiaries in LSMS.

[10] Year of collection: 2007. Income reference period: 2007. Sample size: 17,375 individuals in 5,557 households.

Table 15.19 Average MOP payments, by age

Age category	Average amount of MOP per ae. (in RSD)		Percentage change in amount received
	Old MOP rules	New MOP rules	
Children (0–17)	2,389	2,599	8.8%
Working age (18–64)	2,271	2,545	12.0%
Elderly (65+)	2,953	3,092	4.7%
Total	2,591	2,873	10.9%

Source: Authors' calculations in SRMOD

Table 15.20 Poverty index by age

Age category	Poverty index			Decrease in the number of poor, old MOP vs. new MOP
	Before MOP	After MOP (old rules)	After MOP (new rules)	
Children (0–17)	12.1%	11.6%	11.2%	3.4%
Working age (18–64)	10.0%	9.7%	9.6%	1.4%
Elderly (65+)	7.8%	7.4%	7.1%	4.0%
Total	10.0%	9.6%	9.4%	2.2%

Note: Poverty line is set at the 10th percentile of the income distribution, where income is disposable income per adult equivalent before MOP
Source: Authors' calculations in SRMOD

Table 15.21 Number of MOP recipient HHs/amounts paid out

	Number of recipient HHs (admin. records)	Number of recipient HHs (LSMS)	Total amount of MOP paid, in RSD (admin. records)	Total amount of MOP paid, in RSD (LSMS)
June 2007	48,954	34,608	253,897,376	176,921,584

Sources: LSMS, RSO and Ministry of Labour and Social Policy

The discrepancy is explained by the fact that certain vulnerable groups, such as Roma, refugees and IDPs, are underepresented in the LSMS (Krstić 2008). The dataset sample was mainly comprised of households residing at their registered address or not registered addresses.

Results presented in the first three sections of this report show that the number of people eligible for MOP according to SRMOD simulations (75,220 households according to old, i.e. currently used MOP rules) is significantly greater than the number of those that report receiving MOP in the administrative records (48,954 households). This disparity can be traced to the so-called non-take-up phenomenon, a crucial drawback in any system of means-tested benefits. Studies show that non-take-up is a widespread problem across Europe and beyond. For most European countries, non take-up rates are over 50%, rising to 67% for Germany and 70% for Austria (Fuch 2007). According to our simulation, the *non-take-up ratio*[11] for Serbia is even higher, at 76.9%.

[11] The ratio between the number of households which are not receiving the benefit but are eligible and the total number of households which are potentially eligible.

Levels of take-up in Serbia can be traced by several different factors:

1. Time inconsistency in the application of the means test. The data reports "current" (previous month) income. However, it may be that the MOP means tests referred to income from another period (e.g. last year or the time the household applied for the benefit). This points to the need to simulate household eligibility for MOP, irrespective of how well it fits with the cases reported in the data. SRMOD does not replicate "actual receipt" of the benefit when the data was collected but the "potential entitlement" given the circumstances "currently" described in the data.
2. Unobserved income, one of the assumptions of our simulation is that social workers can fully observe income from informal employment.[12] If we assume that social workers are completely oblivious to income from unregistered activity, the level of non-take-up would be 77.1%.
3. Group representation, as we already mentioned, of certain vulnerable groups- such as Roma, refugees and IDPs- is questionable in the LSMS. Considering the fact that these groups are at high risk of poverty and thus highly likely eligible for MOP, better representation of these groups in the sample would probably further decrease the level of non-take-up.

According to Matsaganis et al. (2010), we may group determinants of non-take-up into four main categories: (a) the expected level and duration of entitlement to benefit, subject to uncertainty about the outcome of application; (b) information costs, i.e. time and effort required for understanding entitlement rules and mastering application procedures; (c) transaction costs associated with gathering proof of eligibility, administrative delays and errors; and (d) psychological costs including stigma.

In the literature (Fuch 2009; Matsaganis et al. 2010), the focus on costs and benefits of claiming assistance has proved influential as well. Therefore, the way we control for non-take-up is to estimate a threshold below which it is not profitable for a household/individual to apply for MOP, since the amount he is entitled to is lower than the cost he needs to undertake in order to obtain it (e.g. costs such as regular travels into town to collect MOP from remote areas, obtaining certificates). We estimated the threshold at the amount of RSD 1,000. Namely, after removing the outliers in the distribution, the minimum level of the social assistance that household reports in the LSMS was 1,000 RSD. Hence, our assumption was that the cost of applying for social assistance equals to the minimum level of social assistance the households declare to be receiving in the database and that nobody would make the effort to apply for social assistance if they are entitled to below this amount.

The LSMS questionnaire included a question about the reasons for not receiving/applying for MOP. Analysis of households which are entitled to MOP according to

[12] The law on social welfare allows social worker to impute income from informal employment (in the lump sum amount) in the means test of an applicant if he/she suspects that applicant has incomes from unregistered activity.

the SRMOD simulation but do not report receiving it in the database shows that 2/3 of them lack information about the programme. More precisely, 21% of non-take-up households were unaware of the programme; 25% were ignorant of the administrative procedures, i.e. they did not know how to apply for MOP, while 17% of them believed that procedures are too complicated. Finally, 13% of non-take-up households believed that they did not qualify for social assistance. Only a small number of households have applied for MOP but were rejected by the Center for Social Welfare.

Overpayment of MOP

Targeting benefits is not only subject to errors in the form of non-take-up. It can also take the form of overpayment of benefits to individuals/households who are not eligible for them.

Further to our SRMOD simulations, only 37.5% of households which reported to receive MOP (according to LSMS) meet all eligibility criteria to receive MOP, whereas 62.5% of households which reported to receive MOP do not meet at least one (out of six) eligibility criteria.

According to the micro-simulation results, the non-eligible households which receive MOP are mostly not eligible because they failed to meet one or more of the following criteria:

- Income test—78% of households which reported to receive MOP
  Sixty-eight percent of households which do not pass the income test (but nevertheless receive MOP) fail to pass it due to income from informal activity. In our simulations, it is assumed that the social worker is able to observe such income and take into it into account when testing eligibility.

  Besides that, part of the difference between the data and simulations arose due to time inconsistency in the application of the income test. The data reports "current" (previous month) income. However, it is possible that the MOP income test refers to income from another period (e.g. last year or the time the households have applied for the benefit).
- Socio-economic and demographic characteristics (criteria related to unemployment, age and disability)—10% of households which reported to receive MOP
- Number of persons in the tax unit is lower than the number of rooms in the main residence of the household—8% of households which reported to receive MOP
- Household owns land greater than 0.5 ha—2% of households which reported to receive MOP
- Household has other immovable property—2% of households which reported to receive MOP

Our analysis suggests that non-take-up of monetary social assistance is very high in Serbia. Even though we offer a rough estimate of non-take-up phenomena (as more sophisticated statistical methods are needed to determine the real size of this indicator), preliminary results are alarming. Low participation rates may distort the intended welfare impact of the MOP programme. Also, non-participation results in unjustified disparities among eligible persons, if only those who are better informed claim the benefits rather than those who would benefit most.

Empirical findings show that non-take-up is also quite high in Western European countries with a better functioning social welfare system than in Serbia. Following this line of research, factors that lie behind high non-participation rates in Serbia need to be determined in future research. Then, policies to improve participation in programmes like MOP could be introduced.

Our analysis also suggests that overpayment is as important a problem as non-take-up of MOP is. Both types of targeting errors are problematic, although, from the fiscal perspective, overpayment of benefits is costly to the government, while non-take-up actually saves public money. This asymmetry may partly explain why the latter often receives less attention than the former (Matsaganis et al. 2010).

Concluding Remarks

As expected, results of the SRMOD micro-simulation show that the changes to eligibility criteria for last-resort social assistance (MOP), envisaged by the new law on social welfare, increase the number of eligible households and individuals and that the average amount of MOP received per adult equivalent increases as well. While the number of eligible households increases by 22.1%, the average amount received per adult equivalent increases by 10.9% (albeit from a low base).

Furthermore, although households in the first 5% of the income distribution appropriate a significantly larger share of MOP than those households whose incomes belong to the second ventile (5%), new eligibility criteria assign MOP to a larger number of new households from the second ventile. This occurs because the new criteria are more lax in terms of the income threshold. Therefore, the new criteria complement the existing subset of recipients by a subset of better-off households and individuals (although they are still from the lowest deciles of the income distribution).

At the same time, out of the total of 241,477 households which belong to the first income decile, only 18% of them fulfil all criteria to receive MOP according to the old law, while 21.3% of them fulfil the new eligibility criteria. Therefore, although MOP coverage increases, it remains low, since a significant portion of households and individuals from the lowest income decile remain ineligible. Even when we

only look at the household from the lowest 5% of the income distribution, their coverage increases from 24 to 26.2%, i.e. it remains low.

With the introduction of new criteria, we observe the highest percentage increase in eligibility of households without children. Since these households mostly consist of elderly members, we can conclude that the increase in their coverage was influenced by loosening the eligibility condition for those households in which all members are incapable to work.

Although the amounts received by children are most positively impacted by the changes in the law (61.8% of eligible children receive more MOP than they used to), children are also the most adversely impacted, due to the changes in the equivalence scale (20.7% of children receive less MOP than they used to).

Some of the most important reasons for ineligibility, when we look beyond income, are criteria related to (not) being registered as unemployed, having a larger number of persons in the tax unit than the number of rooms in the main residence of the household, owning land greater than the 0.5 ha or having other immovable property. These types of criteria which are closely linked to the administrative burden, such as having to renew one's registration with the unemployment service or gathering other proofs of eligibility, have not been changed in the new law, i.e. none of the changes to the law were related to the reduction of information and transactions costs linked to exercising one's right to social assistance. It is therefore expected that those households and individuals that were ineligible for administrative reasons will remain ineligible with adoption of the new law, even when they fulfil the income criterion.

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Chapter 16
Improving the Targeting of Social Assistance in Albania: Evidence from Micro-simulations

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Introduction and Motivation

Albania has registered significant poverty reduction over the last decade, with poverty incidence halving between 2002 and 2008, when it stood at 12%. Extreme poverty (defined as not being able to cover the basic nutritional needs) has all but been eradicated. Growth accounted for most of the reduction in the poverty rate over the period, and inequality decreased between 2005 and 2008. Increases in pensions and social assistance have been seen to contribute to these positive changes. No data are available on the evolution of poverty since 2008, and while there is consensus that Albania has been spared much of the hardship that the global crisis inflicted on many of the economies in Eastern Europe, the present context is one of high vulnerability.

The government's ongoing efforts to improve the efficiency and effectiveness of social benefits programs appear all the more important in this context. According to the latest assessment of the country's largest social assistance program, Ndihma Ekonomike (NE), 56% of the program's resources reach the poorest quintile (World Bank 2011). NE's performance compares favorably with other mean-tested social assistance programs in the region and has also been improving over time (Fig. 16.1; see also Chap. 13).

The findings, interpretations, and conclusions expressed in this chapter are those of the authors and do not necessarily reflect the views of the International Bank for Reconstruction and Development/ the World Bank and its affiliated organizations or those of the executive directors of the World Bank or the governments they represent. The World Bank does not guarantee the accuracy of the data included in this chapter.

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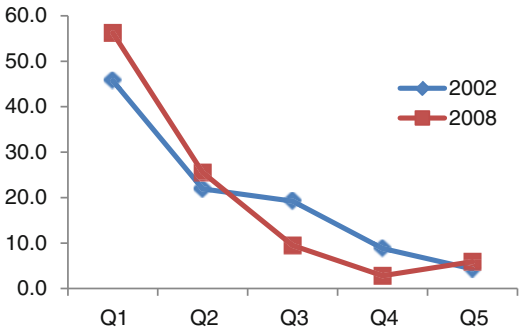

Fig. 16.1 Share of benefits by quintile, 2002 and 2008. *Source*: LSMS (2008)

The program's performance could be improved, however, particularly in terms of the coverage of the poor,[1] strengthening benefit administration and introducing the indexation of benefits and eligibility thresholds to inflation. The generosity of the program could also be improved, as it currently accounts only for 14% of pre-transfer consumption of the bottom quintile.

Since 2010, the government has been working to strengthen the poverty-targeting mechanism for the allocation of NE. This chapter tests how improving the informational basis used to target the program could improve the two steps that constitute such targeting mechanisms—the allocation of block grants to the municipalities and the application of the eligibility criteria by local officials. In particular, we focus on the impact of linking more clearly the allocation of block grants to the poverty map and the impact of replacing the current system of binary eligibility criteria, designed so that failing any of them disqualifies the potential recipient, with a formula where different characteristics of households are weighted in a continuous scoring (using a so-called proxy means test). Both suggestions, and particularly the first one, represent a way of leveraging poverty information to improve the targeting performance of the program.

The interest in improving the performance of this social assistance program might come as a surprise to those familiar with the literature on targeting, as the Albania social assistance of last resort program has often been given as a good example of community level targeting (e.g. Alatas et al. 2010). An influential analysis by Alderman (2002) concluded that "social assistance in Albania is targeted to the poor as effectively as many of the best programs in other developing countries" and that the involvement of local officials in the targeting of Ndihma had a positive impact on program's performance so that "whatever the information that local officials are using, the fact that they use it to further the poverty alleviation objectives of the program is supportive of the use of block grants or other forms of financing that promote more local discretion in allocation" (pp. 398–399). A subsequent

[1] NE provides the highest coverage in the mountainous areas with 30% coverage; 40% of the Roma population is covered by the program against 7% of the general population.

meta-analysis (Coady et al. 2003) referring to the Alderman's findings ranked NE 5th in terms of targeting performance among the 122 programs drawn from 48 countries that it analyzed.

Today, NE is a much smaller program than it was in the mid-1990s. According to administrative data in 2008, the program covered about 100,000 families, having been significantly cut from the 150,000 it reached in 2002 (and the 145,000 reported by Alderman for 1996).[2] More importantly, only 22% of those in the bottom quintile (25% of those in the bottom decile) are covered by the program, a coverage which looks low particularly compared to an estimated 40% for 1996. Other aspects of the program remain comparable to those found by Alderman—for example, the share of total benefits received by those in the bottom quintile was 56%,[3] with a further 25% of total received by those in the second lowest quintile of the distribution.

Another difference with respect to the 1990s is that, while resources are mostly targeted to those at the bottom of the distribution, in the current more constrained resource environment, the program appears to be lacking in transparency and at risk of reaching "undeserving" groups. Far from being perceived as the international star performer the literature suggests it, in the country, the program seems to have acquired a negative image with some of its constituents (including potential recipients). The very feature praised by the literature—that is, the discretionality that is added by the involvement of local council—together with the very burdensome application process[4] appears to be playing a major role in driving this perception. Indeed, anecdotal evidence suggests that the role of the local councils in vetting the lists of eligible households prepared by the local social worker might have contributed to this ill repute, giving rise to suspicions of political interference and rent-seeking behavior. This seems to have been reflected also in the central government emphasis on cutting the programs' reach in terms of both recipients (by enforcing the eligibility criteria dictated by the law) and in terms of generosity, at least since 2002.[5] More rigorous sources such as extensive qualitative work e.g. IDRA 2011 also documented how the eligibility criteria left space for arbitrary exclusion and tended to be discriminatory toward women and female-headed households in need.

These considerations do not amount to an explanation of why the informational advantage of community involvement documented by Alderman is not prominent in current policy discussions—something which seems to require a whole separate enquiry. It is worth underscoring, however, that as Alderman (2002) narrates NE

[2] According to the 2008 Living Standard Measurement Survey, NE benefited 7.3% of the population (or 6% of household) during the 12 months preceding the survey.

[3] This performance in terms of coverage of the bottom quintile is about the mean for targeted social assistance projects in the region.

[4] Applicants for NE benefits have to meet 28 different eligibility criteria and are required to present at least 9 different documents (World Bank 2011).

[5] In 2008, eligibility criteria were also more stringent than those presented by Alderman (2002) and used to design his regressions. In particular, having other income sources from employment or pension payments or owning land would disqualify households in urban areas.

had not originally been designed as a community-based program but rather as an entitlement-based one. Funding pressures transformed the available budget in block grants for communities to allocate on the basis of an original set of eligibility criteria. Whatever the potential benefits of the current hybrid arrangement with externally selected eligibility criteria and the possibility of modifying them at the local level,[6] it seems that the potential offered by new technologies to move toward a more transparent, needs-based, easier to manage, and centralized system is shaping the new wave of reforms. These reforms should hopefully contribute to raise the institutional credibility and sustainability of the program.

Given this background, this chapter presents simulations on two different ways in which NE's performance could be improved. A first section will present the data and the key variables the next section will look at how the geographic element of the targeting could be strengthened by using the information from the updated poverty map and adding a new emphasis on the areas where poverty is most severe. The following one will focus on how targeting at the household level could be improved by adopting a proxy means test rather than the current set of binary criteria. A final section will conclude.

Data and Key Variables

The microeconomic analysis in this chapter is based on data from the 2008 Albania Living Standard Measurement Survey (LSMS 2008), unless indicated otherwise. The survey is an extensive multi-topic household survey including the core LSMS modules (metadata, household roster, dwelling and utilities, education, health, employment, transfers and social assistance, other income sources, and consumption) plus additional modules on migration, fertility, subjective poverty, agriculture, nonfarm enterprises, and social capital. The survey provides a nationally representative sample of 3,599 households. The survey is also representative for urban and rural areas and for three large regions, the coast, the central area, and the mountain, plus Tirana.

The welfare aggregate constructed from LSMS data is annual per capita consumption, which is the total of the following expenditure categories (1) food expenditures, (2) nonfood expenditures, (3) education expenditures, (4) utilities, and (5) durables. The per capita expenditures are then deflated using the Paasche price index. Based on this consumption measure and the national poverty line,[7] the average poverty headcount in 2008 was 12.5%, but there is considerable variability across regions and urban/rural areas, poverty incidence being particularly high in the mountainous region and in rural areas.

[6] Alatas et al. (2010) highlight, for example, the advantages of community-based targeting in identifying the impacts of transitory or recent shocks which would not be captured by eligibility criteria focused on assets.

[7] The national poverty line used is 4,891 New Lek in 2002 prices, updated to 2008.

The centiles used for this analysis are derived from the pre-transfer distribution (measured as total expenditures, minus the amount of the transfers). This implicitly assumes that program receipts do not affect other sources of income, such as labor income (through changes in labor market behavior) or private transfers.

The main indicators we adopted to evaluate the targeting performance of different allocation mechanisms are the following: coverage, defined as the percentage of households where at least one member receives benefits from the program, and generosity, defined as the percentage of total (post-transfer) household expenditure constituted by the transfer through the social assistance program.

Using Better Information to Improve Ndihma Ekonomike's Geographic Targeting

As already mentioned, the first step in the allocation of NE is the identification of a block grant by officials in the Ministry of Labor, Social Assistance, and Equal Opportunities (MOLSAEO), which is then submitted to Parliament for approval. Current procedures for this first phase of geographical targeting are largely based on the number of NE beneficiaries at the municipal level in the previous year. Since 2010, the allocation also takes into consideration a poverty estimate obtained using population data at municipality level from the 2001 Census and regional poverty estimates from the 2008 LSMS survey.

Two main issues arise with respect to this allocation mechanism. First, the poverty information that is considered in the allocation is a regional headcount applied to an estimate of the local population. Regional poverty estimates can be ineffective proxies for municipal level poverty estimates to the extent that different regions are characterized by significant variation across municipalities. Taking as a benchmark the estimates of the updated poverty map (Betti et al. 2012), Fig. 16.2 contrasts the spread of poverty estimates by municipality[8] as compared to regional level estimates of poverty incidence. The loss of valuable local variation in the allocation process appears to be particularly an issue for the mountain region, which is also the poorest region in the country.

Secondly, inspection of the data shows that there is not a systematic way in which the number of poor people and the existing number of beneficiaries at the municipal level are combined. In-depth interviews with government officials highlighted that this combination is based on the experience, knowledge, and judgment of the limited number of ministry officials involved in identifying the allocations.

Could better information, particularly the updated poverty map produced by Betti and coauthors, result in a more effective and transparent geographical allocation

[8] For the sake of simplicity in this chapter, we call the lower level of the administration "municipality" without distinctions between urban and rural areas (where they are known as communes).

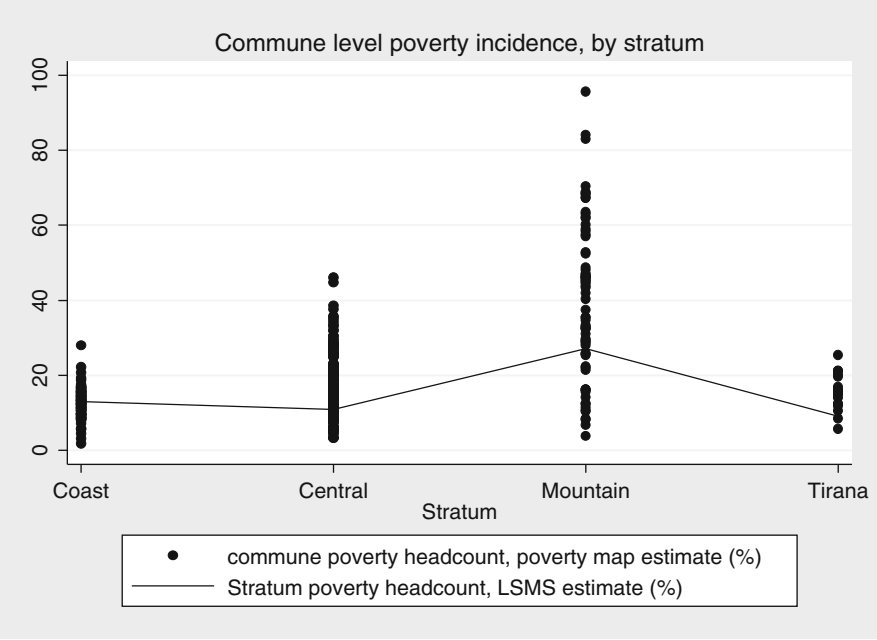

Fig.16.2 Poverty estimates by municipality from the poverty map versus regional estimates of poverty from LSMS 2008

mechanism? We consider two different simulations aimed at exploring the specific impact of changing the geographic targeting mechanism based on the poverty map. Both adopt a geographical allocation scheme which Elbers et al. (2004) call "the naïve poverty share scheme," based on allocating the budget to each municipality in proportion to the share of poor people who live in that municipality.[9] We consider two different versions of this simulation as the naïve poverty share can be based not only on poverty incidence but also to other poverty indexes more sensitive to the distribution of the poor (i.e., how poor the poor are). The second simulation adopts therefore the severity of poverty index at the municipal level as the basis for the allocation. Note that among the many possible ways of using the poverty map information to simulate alternative geographic targeting mechanisms, the naïve poverty share seemed the closest to the logic currently adopted by the ministry in its allocations and therefore the easiest to implement in practice. In addition, this allocation mechanism, even if very stylized, addresses two important concerns that characterize MOLSAEO allocations, namely, that all municipalities receive some resources[10] and

[9] Note that unlike other academic studies such as Elbers et al. (2004), for our analysis we have information on the budget available (we use the cumulated NE benefits from the LSMS survey 2008).

[10] Alternative schemes could include targeting resources to the poorest communes, either exclusively, or giving them some extra weight in the allocation.

that the allocation itself does not create an entitlement on the part of the municipalities to certain resources.[11]

As the focus of this first set of simulations is to evaluate improvements in the geographical allocation mechanisms only, our simulations simplify the complex nature of the program by presenting per capita allocations with no equivalence scales adjustments and by not differentiating between rural and urban areas in the amounts distributed to households. To evaluate the performance of these alternative geographical allocations, we construct a counterfactual which similarly simplifies program design and neutralizes the effects of the second stage of the targeting mechanism by local authorities (i.e., the household level targeting). By adopting a counterfactual, we remove the bias that errors in implementation and non-take-up which characterize the observed distribution would bring to the comparison. Based on these considerations, we compare the following three simulations:

Baseline simulation. This simulation is based on the current targeting of NE but eliminates the effects of the community level identification of the beneficiaries by distributing the benefits to all members of a given municipality.

Poverty map—naïve poverty share. The overall budget is allocated based on the share of overall poverty in each municipality. In parallel to what is done for the baseline, benefits are then distributed to all household members of a given municipality.

Poverty map—naïve severity of poverty index. This simulation is a variation on the previous one, but the weights assigned to each municipality are proportional to their contribution to the overall severity of poverty index.

A first check on the possible improvements that the "true" poverty distribution obtained from the Betti et al. poverty map could bring about is provided by Figs. 16.3 and 16.4 below. In Fig. 16.3, for each municipality represented in the figure, one can read on the *x*-axis the estimated share of poor people that live in the municipality, while on the *y*-axis one can see the share of resources that were allocated for 2010 by MOLSAEO. All points above the 45° line represent communities that receive an allocation greater than their share of overall poverty, with the reverse being true for the points below the line. Figure 16.4 is similarly constructed and contrasts existing allocations (on the *y*-axis) and those that would be obtained based on the severity of poverty in each municipality (on the *x*-axis).

[11] As this mechanism provides a rule for sharing the total budget, there is not an entitlement to a given level of resources for any municipality. Note also that a third concern, arguably conflicting with the previous but nevertheless present in policy discussions, is the need to ensure that allocations do not vary abruptly. In current practice, this is typically taken into consideration by considering information on the number of NE recipient the previous year. The move to allocations based on poverty map information would have to be phased in to ensure that municipalities can adjust to changing allocations. In addition, additional variables to take into account localized shocks could become part of the allocation formula.

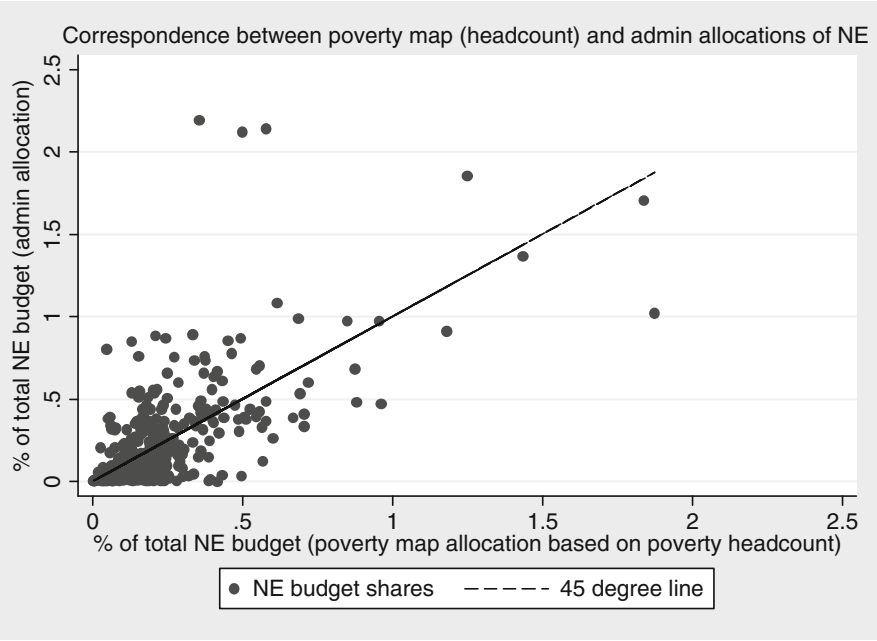

Fig.16.3 Linear correlation between budget shares based on poverty headcount = 0.79 ($p = 0.0000$). *Note*: the figure omits a limited number of municipalities with either share >2.5%: Durres, Elbasan, Shkoder, and Tirana

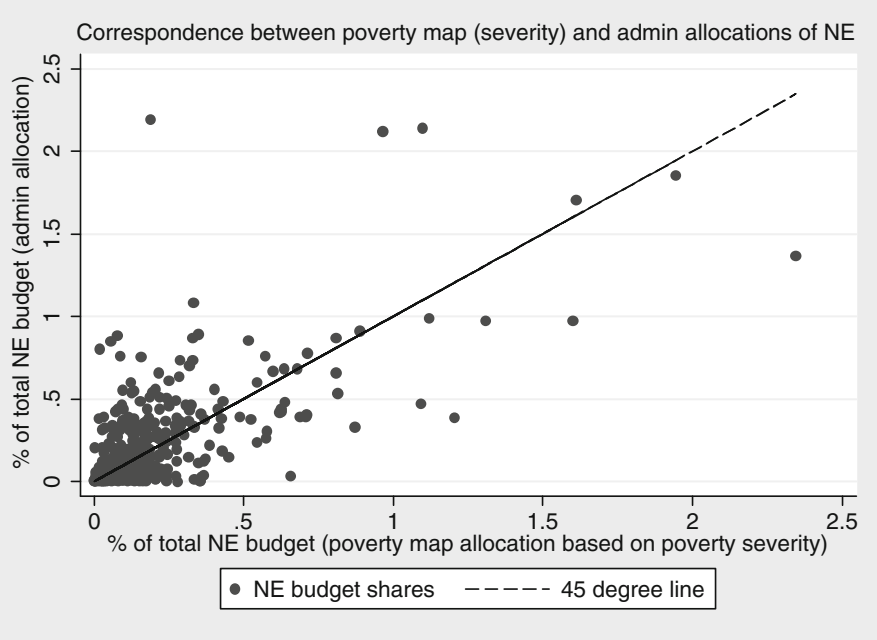

Fig. 16.4 Linear correlation between budget shares based on poverty headcount = 0.69 ($p = 0.0000$). *Note*: municipalities with either share >2.5%: Durres, Elbasan, Shkoder, Tirana, and Vlore

Figure 16.4 shows that the current allocation process, even if not rigorously based on the share of poverty in each municipality, is very consistent with the incidence of poverty in different municipalities. While a few municipalities appear to be very far from the line,[12] the two variables are strongly correlated (the coefficient of correlation is 0.79). The correlation is weaker in the case of allocations based on the severity of poverty, even though this is a more sensitive indicator for the policy objective of giving priority to the poorest of the poor. Part of the success of the current allocation method in allocating more to poorer municipalities seems to be due to the informational content of the past number of beneficiaries (the key variable used in the current MOLSAEO allocation before it is subject to ad hoc adjustments). This same variable, however, seems to introduce an element of rigidity into the system. The data from the updated poverty map, for example, show that urban poverty rates are now higher in the coastal areas than they were in 2002, while urban NE allocations still reflect a higher concentration of urban poverty in the mountain region. This suggests that allocation of NE based on an updated poverty map could potentially improve targeting since recent poverty data would have be a better guide to allocation than the information on previous beneficiaries.

This hypothesis seems to be confirmed by the results of our simulations presented in Table 16.1. The share of resources allocated to the bottom quintile or to the poor in general would significantly increase if geographic targeting adopted weights proportional to the share of poverty incidence, or poverty severity accounted for by each municipality.[13] Interestingly, because of the nature of our simulations, the improvement in the degree of progressivity of the distribution of the benefits is not monotonic. As we consider uniform allocations to all inhabitants of a given municipality, this seems to be driven by the fact that some of the areas where the severity of poverty is higher are also those where relatively more wealthy groups live. This appears to be the case mostly for urban areas. Combining a geographical allocation with household level targeting would eliminate this feature and potentially result in more resources being allocated to lower income groups. From this point of view, the findings of our simulations can be seen as lower bound estimates of the improvements in the targeting performance that would be possible by adopting geographical allocations proportional to the most common poverty indices.

[12] Note that Elbasan, Shkoder, and Tirana have the largest shares of the transfer (and they appear off the graph because their share is more than 2.5% of the total) under the current allocation. Tirana houses a higher proportion of the poor than its already high share of the allocation, while the reverse is true for Shkoder and Elbasan. Durres, which receives a grant allocation which is below 1% of the total, according to the poverty map, is home to more than 3% of the total number of poor in the country and accounts for an even greater share of the poverty severity index.

[13] Note that we present only indicators of targeting accuracy as the simplifying assumptions made to bring into relief only the geographical element of this allocation mechanism would result in universal coverage and very unrealistic monetary values (hence generosity) of these transfers.

Table 16.1 Distribution of NE benefits across income groups according to different geographic allocation criteria, by quintile and poverty status

	Baseline	Simulations	
	Targeting accuracy with *actual* weights	Targeting accuracy with *poverty headcount* weights	Targeting accuracy with *poverty severity* weights
Q1	54.6	61.2	63.8
Q2	24.5	18.6	17
Q3	12	8.4	11.6
Q4	4.9	3.9	3.9
Q5	4	3.3	3.7
Poor	39.8	39.9	46.5
Nonpoor	60.2	60.1	53.5

Note: In 2008 12.5% of Albanians were estimated to be living in poverty

Combining Household Level Information in New Ways to Improve Individual Level Targeting

As discussed in the introduction the allocation of NE takes place in two steps. Once communities receive their block grants, local offices allocate them according to beneficiary identification rules identified at the central level. These identification rules include a series of steps. The first is means testing, which involves checking formal income sources and carrying out household visits. This process excludes participants who fail eligibility criteria, for example by refusing employment when offered. Ownership of capital is another source of ineligibility. Special rules apply for rural areas where income from agriculture is imputed. Once the first screening test is completed, social administrators can still deny benefits based on a household's "good economic conditions." There are no clear criteria to determine what this means. As mentioned in the introduction, when approving the list of NE beneficiaries, local councils can introduce subsequent modifications and anecdotal evidence suggests that they tend to add members rather than deny benefits to households who have already qualified. The overall process appears to be long and complex, with claimants being required to present an extensive set of documents.

As Chap. 13 discusses the binary nature of the eligibility criteria significantly constrain the potential coverage of NE. It has been estimated that only 8% of the poor living in urban areas could potentially be covered by NE if the requirement that no household member has a job is interpreted include informal sector jobs (something which local communities might be able to ascertain). Even with a less restrictive interpretation, including only formal jobs, would result in only 41% of the poor being eligible for the program. The same logic holds for the quality of NE in rural areas, though the eligibility criteria are different.

It is possible that the flexibility in the determination of the eligibility process might allow local authorities to mitigate the effects of the selection criteria adopted by NE and ensure coverage of needy households that would otherwise be excluded. While this might well be the case, it has been suggested that objective weighting of

different household characteristics would provide for a more effective and transparent process of assessing household need (World Bank 2010). This can be achieved through a proxy means test (PMT), by using an indicator which combines a number of household characteristics as proxies for income for purposes of determining the welfare of a household. The alternative approach, adopting an explicit means test by collecting and verifying income data, would face acute difficulties in implementation given a context characterized by high levels of informal employment and a high dependence on private transfers such as remittances.

As detailed in the Annex, we constructed a PMT by regressing the natural logarithm of per capita expenditures on a set of household characteristics. These estimates were used to predict household expenditure levels based on observed characteristics, much in the same way that offices administering NE would assess eligibility in the event of such a system being implemented.

To evaluate the performance of the PMT as a mechanism for selecting beneficiaries, we contrast two simulations, which, as in previous case, simplify the complex administration of the program to bring into relief key issues in household level targeting:

Baseline simulation. This simulates the choice of NE beneficiaries by using the program household eligibility criteria as stated in the law.[14] This simulation abstracts from issues of non-take-up of the program (according to our simulations, a total of 7.8% of the population is found to be eligible for NE, against an effective coverage of 7.3% of the population in the LSMS 2008 data). This simulation also uses a simplified rule to determine allocations. The total NE budget derived from the survey is divided equally in per capita terms across the total pool of NE recipient households in the survey.[15]

PMT simulation. This simulation changes the identification of NE recipient by identifying the bottom 7.8% of the population as ranked by the PMT. The overall NE budget is then distributed on an equal per capita basis to all the recipients.

Table 16.2 presents the main findings of the simulations. The PMT simulation improves targeting considerably compared to the baseline with 58% of benefits accruing to the bottom decile against 15% in the baseline. Less than 1% of benefits[16]

[14] Due to lack of data, a number of disqualifying conditions cannot be simulated, such as whether a household member (1) owns stakes/shares of any kind other than agricultural land or dwelling; (2) is abroad for reasons other than education, medical treatment, or diplomatic work; (3) is not working but not a registered unemployed; and (4) is not working but does not participate in community work.

[15] Note that this simulation does not take into account two separate features of NE, such as the very steep discount for additional family members implied by the current equivalence scales and the rural-urban differences in the level of benefits.

[16] Note also that in our simulations as we are simulating a constant per capita allocation, the distribution of benefits (targeting) is equivalent to the distribution of beneficiaries.

Table 16.2 Performance of NE across income groups according to different simulated eligibility criteria, by quintile and poverty status, percentages

	Baseline		Simulation	
	Coverage	Targeting	Coverage	Targeting
D1	11.9	15.3	45.2	57.9
D2	12.0	15.3	11.6	14.8
D3	8.0	10.2	11.7	15.0
D4	12.6	16.3	6.5	8.3
D5	4.6	5.8	2.1	2.7
D6	5.0	6.4	0.3	0.4
D7	6.5	8.3	0.4	0.5
D8	6.1	7.8	0.1	0.1
D9	7.5	9.7	0.1	0.2
D10	4.1	5.1	0.0	0.0
Poor	12.4	20.4	36.9	60.8
Nonpoor	7.2	79.6	3.5	39.2
Total	7.8	100.0	7.8	100.0

Source: LSMS (2008)

would be obtained by each of the four top deciles. Overall, 61% of the poor (as opposed to 20% in the baseline) would be reached by the scheme. The coverage of the first decile also improves dramatically (from 11.9 to 45.2), though there is a slight dip for the second decile.

Discussion and Conclusions

The government of Albania has made a commitment to strengthen the link between social assistance allocations and poverty indicators. This chapter has presented two scenarios under which the current allocation mechanism could be strengthened by taking advantage of new statistical indicators that capture different aspects of poverty. The practical application of either of these scenarios or of a combination of the two, would require more in-depth work. Combining the predictability of transparent and predetermined allocations with the flexibility to respond to idiosyncratic shocks that is required by any program of social assistance of last resort would require careful design.

Notwithstanding the need to refine the methodological innovations and approaches considered in this chapter, the evidence that we present demonstrates that leveraging poverty information, an area in which Albania and its development partners have invested significantly, can contribute to improved program design.

Appendix A. Annex: Deriving a Proxy Means Test

Following the literature, a PMT was constructed by regressing the natural logarithm of per capita expenditures on a set of household characteristics. Rather than forcing model parameters to be equal for the entire sample, we allow for different slopes across strata and urban/rural areas. Note that PMT models commonly include location variables (such as geographic stratum or urban/rural variables), which would allow for different intercepts across groups defined by these variables, whereas estimating separate regressions for the above subregions allows for a less restrictive specification.

These estimates were used to predict expenditures for households with observed characteristics. As the basic idea behind PMT is to rely on household characteristics as proxies for income, household welfare relevant characteristics were chosen, trying to ensure that they respected the principles identified in the literature (Coady et al. 2004): high correlation with poverty; parsimony, in order to ensure feasibility of implementation for a large share of the population; observability and ease of measurement; and difficulty of manipulation by the household.

In selecting the variables to be included in the consumption regressions, we follow Grosh and Baker (1995) and choose variables from three broad categories (1) household composition characteristics, (2) housing/dwelling characteristics, and (3) ownership of assets.

A.1. Family Characteristics

We use a standard set of family composition variables, which includes (log of) the household size; the share of household members who are employed, unemployed, or inactive, whether the head of household is a woman; the age and gender composition of the household; and the highest education level in the household. Most of these variables are readily verifiable (or at least not commonly misreported) and have been shown to be significant predictors of consumption levels in the region.[17]

A.2. Housing/Dwelling Characteristics

The LSMS provides a number of housing characteristics that could be included in the set of explanatory variables. The important consideration here is that characteristics that are chosen are easily observable and/or measurable. For instance, one of the questions in the survey asks whether the condition of the dwelling unit is very

[17] See World Bank (2009) on Bosnia and Herzegovina, and Betti 2003) on Albania using 2002 LSMS.

good, appropriate, or inappropriate for living. While this variable can be shown to be a strong predictor of welfare, Coady et al. (2004) note that chosen characteristics should be such that different staff members or the same staff member on a different day or in a different mood would make the same evaluation. It is unclear whether including a variable of this kind could potentially result in manipulation; hence, we do not include this variable among housing characteristics.

The chosen variables include the type of dwelling (whether residing in an apartment building or not); type of dwelling ownership (whether owned by HH or not), whether the household is connected to the public water supply system; type of heating used; distance to nearest hospital; as well as whether the dwelling has any of the following: kitchen, garage, terrace, or pantry. The distance to the nearest hospital is also included as a measure of access to health services.

A.3. Ownership of Assets

A number of assets that have been previously used in PMT analysis are chosen, including the following: color TV, refrigerator, computer, car, motorcycle, video/DVD system, washing machine, dishwasher, air conditioner, water boiler, TV cable/satellite dish, wood stove, and gas/electric stove. Whether a household owns a phone is not included since only a fixed phone is observed in the survey, and lack of a phone could certainly be due to reliance on cellular phones, but we cannot distinguish between this situation, and lack of any phone in HH.

The main findings of the models are described in Table 16.3, which presents the signs of the coefficients significant at more than 10%.

Alternative specifications of the PMT model were run, checking for the sources of error of inclusion and exclusions that different models would result in to identify the model that performed best. This analysis was conducted with reference to the bottom quintile of the consumption distribution. As expected, the correspondence between the distribution of actual expenditures and of the predicted expenditures improves considerably as additional household characteristics are accounted for. Using the final specification of the PMT model, 63% of the observations in the bottom quintile of the "true" consumption distribution are found also in the bottom quintile of the predicted expenditure distribution. At 37%, the error of exclusion is comparable to estimates by Grosh and Baker (1995) who report an undercoverage rate of 41% and by Hentschel et al. (2000) at 39%. While also the error of inclusion is at 37%, it should be noted that of those erroneously categorized as belonging to bottom quintile of the distribution, the majority is in the second quintile from the bottom, such that they are just above the cutoff and not at the top of the expenditure distribution.[18]

[18] The accuracy of targeting decreases focusing on smaller groups of the population. For instance, if instead of the bottom quintile, the target group is constituted by those in the bottom decile of the distribution, the correspondence between the bottom deciles of the actual and predicted distributions of consumption based on the full model drops from 63 to 53%. Nevertheless, the correspondence level is still rather high for this level of disaggregation.

Table 16.3 PMT regional models: sign of variables significant at more than 10% significance level

	Coast urban	Coast rural	Central urban	Central rural	Mount urban	Mount rural	Tirana
Apartment							
WC inside		+		+			−
Kitchen			+		+	+	
Terrace	+	+			+	+	
Garage				+			+
Pantry		+				−	+
Dwelling owned				+	+		
Public water supply	+						
HH uses gas	+	+	+	+		+	
Electric/gas/central heat	+	−				−	
Electricity meter					+	−	
Rooms per person	+		+	+			
Distance to hosp. <21 min							
Female head					−		−
Ln (HH size)	−	−	−	−	−	−	−
Share of employed in HH	+	+	+	+	+		+
Share of children in HH		−		−		−	
Share of elderly in HH							
Share of women in HH				−		−	
No education					+		
Secondary education	+				+		+
Vocational education	+			+	+	+	+
University education	+			+	+	+	+
Color TV			+	+			
Refrigerator					+		
Video/DVD system	+	+	+			+	+
Washing machine		−		+		+	
Dishwasher	+	−			+		
Electric/gas stove			+	+			+
Wood stove			−		−		
Air conditioner		+	+	+		−	+
Water boiler	+		+		+		
Computer	+		+			+	+
Cable/satellite dish	+				+	+	+
Car	+	+	+	+	+	+	+
Motorcycle		+	+				

Note: +/− indicate the sign of the coefficient for variables significant at the 10% level or less

Following Hentschel et al. (2000), a further test of the accuracy of the PMT model was performed by randomly dividing the survey sample in half and estimating the same models as above for one half of the sample. The estimates from these regressions are then used for an out-of-sample prediction for the remaining half of

the survey data. As sample sizes were too small to reestimate over rural/urban regional subsample, overall regressions were estimated with dummies for each of the subregion (coastal urban, coastal rural, etc.) to allow for differences in intercepts. The fit of the regression was quite good, with an adjusted R^2 of 0.57. The sign of the coefficients in the model was generally similar to those of estimates from subregional regressions. Furthermore, based on the half of the sample over which the model was estimated, the correspondence of distribution quintiles is only marginally lower than in the case of subregional regressions—60% of those in the bottom quintile of the distribution of actual expenditures are also in the bottom quintile of the distribution of predicted expenditures and vice versa.

As could be expected, the out-of-sample prediction was not as good with the correspondence between the bottom quintiles of actual and predicted distributions being only 55%. Nevertheless, the leakage and undercoverage rates are still comparable to those reported above.

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