

The Politics of Anti-Poverty Policy in Russia 1998-2007

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- 1. Macro background**
- 2. Poverty and anti-poverty policy: a regional perspective**
- 3. Approach/model**
- 4. Empirical strategy and tests**
- 5. Conclusions**

1. Macro background

During the 1990s, Russia passed through one of the most harrowing macro-adjustment processes of modern times, involving the loss of several million jobs, severe reductions in the real value of social welfare benefits, and wage arrears that, at their peak in 1997, affected around two-thirds of the workforce (Mussurov 2007). In the process, the Gini index of inequality rose from one of the lowest in the world to a level higher than that of the United States (Brainerd 1998)², and material deprivation, on several indicators, grew to frightening levels. Between 1992 and 1998, the headcount index of poverty grew, although measures of this vary, by a factor of about three (Klugman and Braithwaite 1998); there was a general deterioration in health, extensively surveyed by Stillman (2005); overall mortality, which in other countries afflicted by adjustment continued on a declining trend, rose continuously through the decade³; and even suicide rates experienced a sharp upward trend (Brainerd, 2001). Thus the process of macro-economic stabilisation, which imposed severe social costs around the world, in Russia took on the nature of a catastrophe. As

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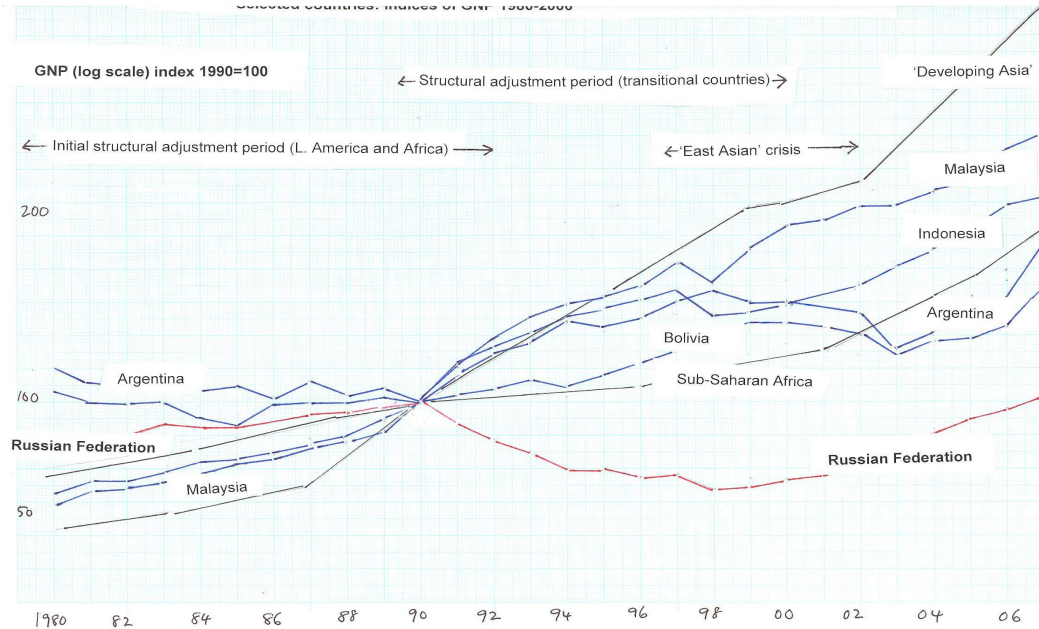
² The coefficient of variation of per capita income between 79 of the Russian regions is given by Hanson as 0.61, by comparison with 0.27 for the 15 states of the European Union prior to 2004 and 0.15 for the 50 states of the US. Hanson(2007b), Table 1.

³ The crude death rate rose from 12 to 15 per thousand between 1990 and 2001 (Stillman 2006: 114) One survivor who survived on eating shoe-leather during the Leningrad blockade and famine of 1941, in which a million people died, was willing to claim to the BBC '1991 was worse' (Bridget Kendall, Radio 4, 26 August 2007)

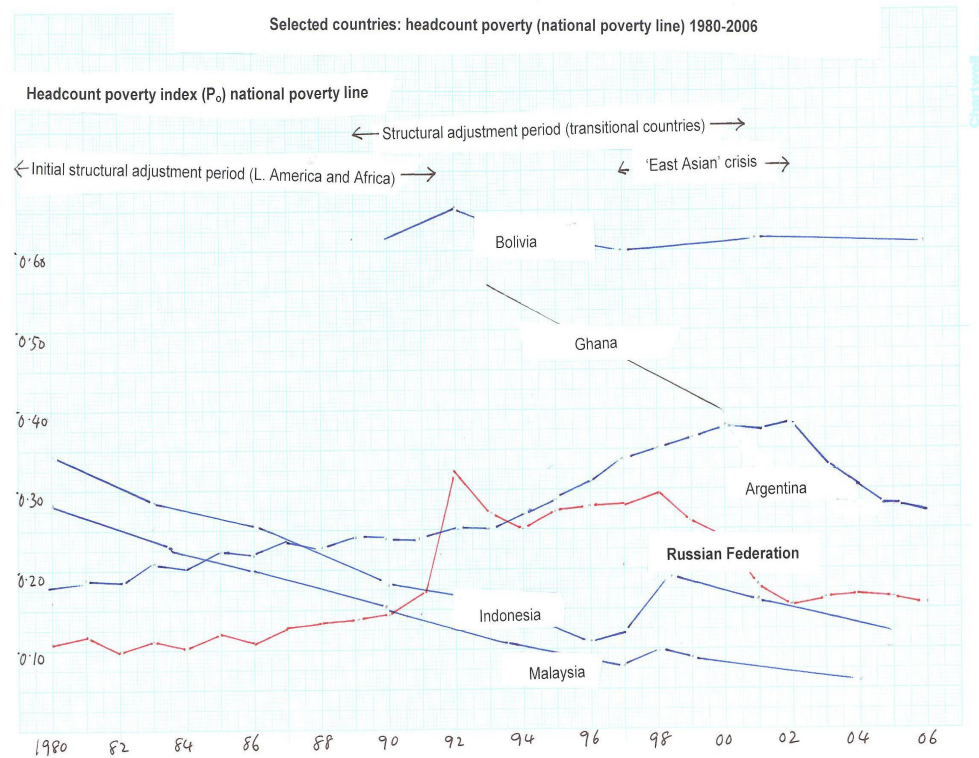
illustrated by Figure 1, no other adjusting country experienced such an extended fall in GNP or such a sharp rise in poverty.

Figure 1. Russia and Comparator Countries: Evolution of GNP Growth and Poverty 1980-2005

(a) GNP growth rates



(b) Headcount poverty



In the process of this adjustment, the traditionally powerful and centralised Russian state underwent extreme stresses, and through much of its early transition to democratic forms of government stood 'on the precipice of state failure' (Giuliano 2006: 276). Of the 89 constituent political entities, or 'federal subjects'⁴, of which the Russian Federation has consisted since the break-up of the Soviet Union, more than a dozen, mostly on the southern and eastern edges of the federation (see figure 1 below) have rebelled against federal authority⁵ in ways which vary from refusing to comply with requirements to execute elections, to defying federal laws, to refusing to deliver tax revenues or statistics or in the limit threatening to secede from the federation, with Chechnya simply the most dramatic and widely-publicised case of the articulation of this threat. This 'fragility at the edges' provided, during the 1990s, a window of opportunity for external actors, such as the IMF, to seek to intervene in determining the direction of Russia's macro-economic and public expenditure policies. The extent to which this intervention was successful is disputed (Mosley, 2003); but the weakness which gave rise to it was resented, and much of the thrust behind subsequent Russian economic policy consists of an attempt to protect against a recurrence of that weakness.

Both politically and economically, there has since 2000 been a perceptible drawing-back from the precipice: economic growth has been substantial and uninterrupted over the years 2000-2006, the headcount measure of poverty has fallen, President (now Prime Minister) Putin's United Russia Party won the December 2007 elections with a majority of over 40% over their nearest rivals the Communists; and there has been some diminution in the level of dissent within the regions⁶. But what is the role of economic, and specifically of distributional, factors in this process? This paper considers that question. Its approach is disaggregated: it explicitly considers and analyses the massive variations in degree of recovery from the distress of the 1990s across the regions of the world's biggest country, and uses these variations to try and understand political outcomes. We shall show, first, that anti-poverty policy -perhaps more than in other countries - can be seen as an attempt to buy off the threat of political instability; in particular the instability associated with threats of regional dissidence and rebellion. Second, the chosen instrument of anti-poverty policy varied across time, with alternations between social expenditure, minimum wages and pensions , according to the salience of particular influence groups in government and of particular interest groups in civil society. In conclusion, we use these findings to shed light on current debates about the scope for making policy pro-poor in different environments.

⁴ These comprise 55 *oblasti* (regions) and *kraya* (federal territories), 20 autonomous republics and 10 other autonomous districts.

⁵ During the late 80s and early 90s, Boris Yeltsin encouraged the autonomous republics to do this as part of his campaign against President Gorbachev (Service 2003:)

⁶

2. Poverty and anti-poverty policy: a regional perspective

We begin by looking in a little more detail at the trend of poverty levels depicted in Figure 1. As shown in Table 1, aggregate poverty levels for the Russian Federation as a whole rose dramatically across the country in the early 90s, remained on that higher level throughout the decade as economic growth rates continued negative, and then fell gradually through the growth phase of the early 2000s.

Table 1. Russia :Selective Poverty Indicators based on official estimates, 1992-1999¹

Year	Headcount Index	Gini	Real Wage	Nominal Wage/Poverty Line	Nominal Pension/Poverty Line
1980	0.113	0.276			
1992	0.335	0.289	67	281	119
1993	0.315	0.398	100.4	254	138
1994	0.224	0.409	92	226	129
1995	0.248	0.381	72	159	101
1996	0.220	0.375	106	190	116
1997	0.207	0.381	105	206	113
1998	0.233	0.398	87	189	115
1999	0.284	0.399	78	152	70
2003					
2006					

Source: Mussurov and Mosley(2007), Table 1.

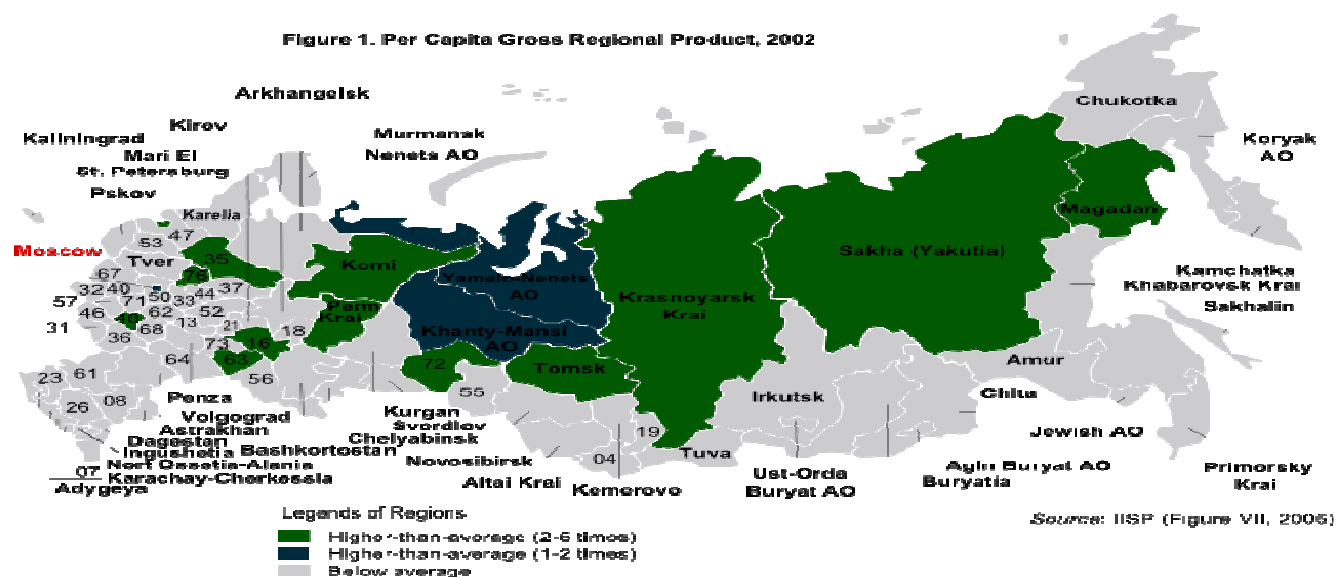
Notes: ¹Definition: Headcount Index of poverty = share of individuals with incomes below the official poverty line; Gini Index = income inequality measure. Real wage = inflation- adjusted wage relative to the previous year; Nominal Wage/Poverty Line = ratio of nominal monthly wage to the poverty line; Pension/Poverty Line = ratio of nominal monthly pension to the poverty line.

We now wish to disaggregate this picture between regions, which becomes possible with the publication after 1995 of data on the GDP ('gross regional product'), fiscal expenditures and social conditions of all of the 89 'federal subjects'⁷. The first thing which we notice (figure 2) is that, in essence, the rich regions (two to five times per capita GNP) are of two types – in the west, the city-states of Moscow and St Petersburg and, in the east, the resource-rich states of northern and central Siberia. By the same token, the

⁷ These data are published as *Regiony Rossii....*) The only study which to our knowledge examines regional GDP trends is Yemtsov (2007). This study, however, examines only the period 1995-2000 and is almost entirely concerned with issues of GDP convergence among regions, and does not discuss issues of living standards or poverty levels.

poor regions are also of two types – ‘always poor’ regions with a mainly agrarian economy and poor infrastructure on the southern periphery (Chechnya, Dagestan, Ossetia, Bashkortostan AR, Ingushetia, Chechnya) – the last two of these also recently afflicted by conflict - , and ‘newly poor’ regions in the south-east, often along the line of the Trans-Siberian railway (Chita, Tuva, Kemerovo, ? Novosibirsk) – mainly industrial regions decimated by the decline of the state heavy industry sector after 1991 and lacking the political, therefore the financial, resources to diversify in the reconstruction period.

The regional distribution of poverty across the federation is as shown in Figure 2.

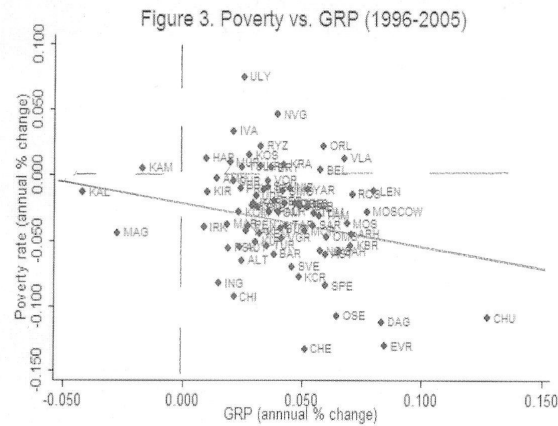


We now examine the dynamics of poverty across the regions of Russia during the period of perestroika and after. As originally argued by Dollar and Kraay (2003) there is a tendency across the countries of the globe for poverty to fall with increasing rates of economic growth, and we wish to see whether this tendency is also evident across the regions of Russia. As illustrated by figure 3, there was *in general*, across the 89 federal subjects, a tendency for poverty (between 1998 and 2005) to decline as growth rates increased; however the proportionate rate of decline (the ‘poverty elasticity’) is only -0.53 – half the level estimated by Dollar and Kraay in the late 1990s and one-fifth of the central cross-section estimate of poverty elasticity presented in the 2006 *World Development Report*. Moreover, in thirty of the 89 federal subjects in the 1996-1999 period, and in a smaller number in the 2000s, positive growth rates of GDP in particular regions were accompanied not by reductions in poverty but rather by increases: growth was of a type which was actually inimical to escape from poverty. These regions are catalogued in Table 2.

Figure 3. Poverty and growth experience, Russia versus global

(a) Russia; poverty versus GRP 1996-2005

Source: Regiony Rossii (2007 edition)

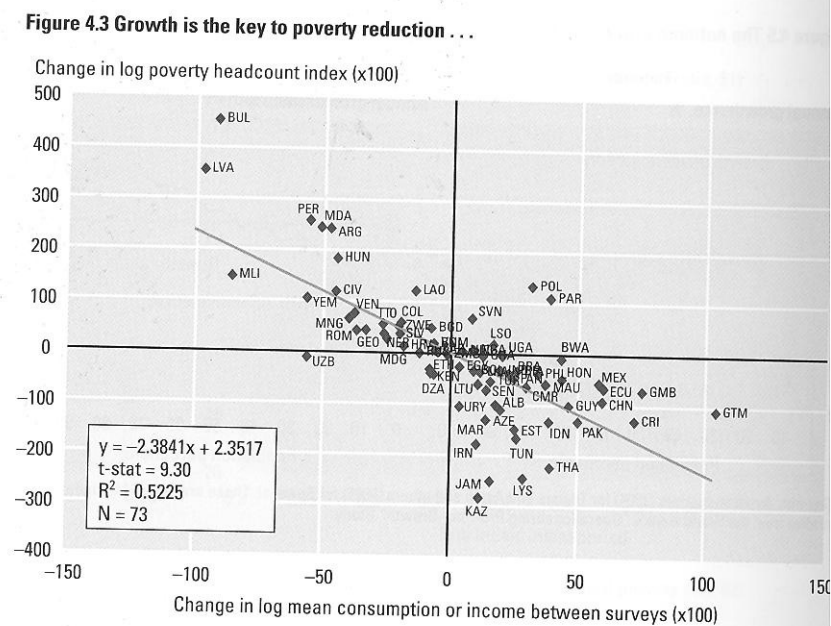


Regression: $\text{Log poverty} = -0.009 - 0.533^{**} \text{ log gross regional product (GRP)}$
(-3.30)

Adjusted R = 0.112 F = 10.89 N = 79

(b) Global cross-section: poverty(log headcount index) vs change in log mean consumption or income 1990-2005(between-survey calculations)

(Source: World Bank, World Development Report 2006, Figure 4.3)



Source: Authors' calculations.

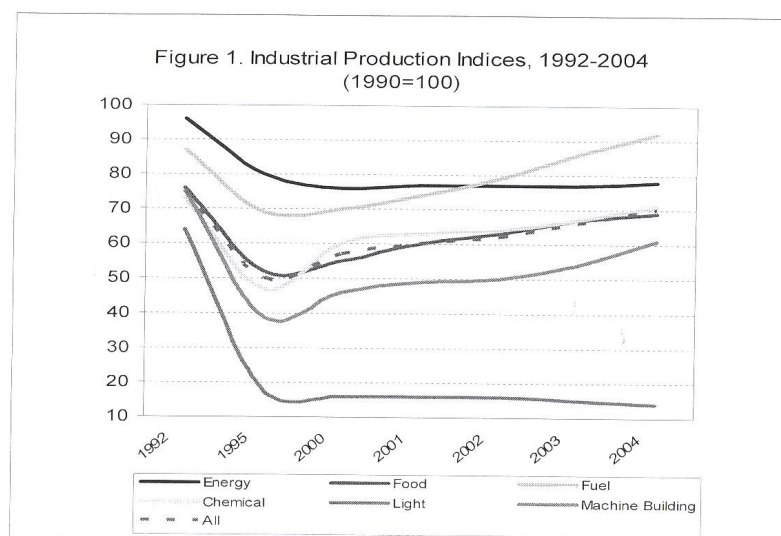
Table 2. Patterns of growth and poverty, 1996-99 and 2000-2005

1996-99		2000-05	
Positive growth, fall in poverty <i>Southern:</i> North Ossetia/Alania Republic	Positive growth, increase in poverty <i>Central:</i> Belgorod, Vladimir, Voronezh, Kostroma, Kursk, Moscow (oblast and city), Oryol, Smolensk, Tambov, Yaroslavl <i>Northwestern:</i> Archangelsk, Vologda, Leningrad, Murmansk, Novgorod), <i>Southern</i> (Kabardino-Balkans Republic, Krasnodar Krai, Astrakhan, Rostov); <i>Volga</i> (Mordovia Republic, Nizhny Novgorod, Penza, Perm, Samara, Saratov); <i>Siberian</i> (Buryatia Republic, Tuva Republic); <i>Far Eastern</i> (Khabarovsk Krai, Sakhalin)	Positive growth, fall in poverty <i>Central, Northwestern federal, Volga, Ural and Siberian:</i> all territories. <i>Southern:</i> all territories except Kalmykia. <i>Far Eastern:</i> Yakutia, Primorsky Krai, Khabarovsk, Amur, Sakhalin, Jewish AO, Chukotka AO	Positive growth, increase in poverty <i>Southern:</i> Kalmykia Republic
Negative growth, decline in poverty <i>Southern:</i> Adygeya republic, Dagestan Republic <i>Siberian:</i> Irkutsk	Negative growth, increase in poverty <i>Central:</i> Bryansk, Ivanovo, Kaluga, Lipetsk, Ryazan, Tver, Tula). <i>Northwestern:</i> Karelia Republic, Komi Republic, Kaliningrad, Pskov, St Petersburg <i>Southern:</i> Ingushetia Republic, Karachay-Cherkessia Republic, Stavropol Krai, Volgograd). <i>Volga:</i> Baskortostan Mari El, Tatarstan, Udmurtia, Chuvashia, Kirov, Orenburg, Ulyanovsk). <i>Ural:</i> Kurgan, Sverdlovsk, Tyumen, Chelyabinsk). <i>Siberian:</i> Altay Republic, Khakassia Republic, Altai Krai, Krasnoyarsk Krai, Kemerovo, Novosibirsk, Omsk,	Negative growth, decline in poverty <i>Far Eastern:</i> Magadan	Negative growth, increase in poverty <i>Far Eastern:</i> Kamchatka

	Tomsk, Chita. Far Eastern: Yakutia Republic, Primorsky Krai, Amur, Kamchatka, Magadan		
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One important reason for the low overall poverty elasticity is embedded in the characteristics of structural adjustment itself. Adjustment to global market forces involved a shift (Figure 3) from non-tradables to tradables – involving, in Russia and a number of other countries, the substitution of unprofitable state manufacturing activities in both heavy and light engineering industry , mostly labour-intensive , by oil, gas and minerals exports, which currently account for a quarter of GNP and over 80% of exports⁸, but are highly capital-intensive⁹ and unable to convert any significant part of the growth to which they give rise into livelihoods for poor households with limited skills.

Figure 3. Patterns of industrial development 1998-2007



Source: Federal State Statistics Service (2007).

The nature of this structural shift both explains a large part of the low overall poverty elasticity, and defines the nature of the gainers and losers from the adjustment process. The gainers were people with skills adapted to the requirements of the 'new economy' and regions intensive in natural resources; the losers (the 'perverse cases' with increasing poverty levels shaded in the shaded top right-hand corners of Table 3) were individuals with low levels of skill and regions on the eastern and southern periphery

⁸ Hanson 2007: Figure 4.

⁹ A similar evolution towards a capital-intensive pattern of production – and once again, increases in poverty in many districts - is visible, with even more dramatic political consequences, in our Bolivia case study (Mosley 2007)

which, as previously described, either never had any labour-intensive tradable activities or lost them with the onset of perestroika.

The map of winning and losing regions is reflected in the map of political protest.

Who were the losers in the late 90s, continuing into the early 00s, and to what extent were they able to articulate their grievances?

*****Will be Table 3*****

The opening up of the regional Pandora's box, therefore, provides an insight both into economic performance and into political behaviour that is not available from the aggregate data. A number of the regions and groups which did not gain from the renewed onset of economic growth after 2000 – including in January 2005 pensioners, previously thought of as a politically weak group, - sought to achieve by political action what the newly established market was unable to deliver to them. Did this political action achieve any kind of influence on patterns of public action (expenditure, legislation protective of the poor, and price controls) at the regional level, and did this public action in turn achieve any kind of influence on the regional pattern of poverty and well-being? The following two sections consider these questions.

3. Approach and model

The general argument so far, then, is that in Russia since 2000 economic growth has indeed been important in helping the Putin government re-entrench its grip on power¹⁰, but that the quality of that growth leaves it still vulnerable. The degree of political stability in Russia after 2000, we argue, depends as in any country not only on the rate of economic growth, but also on the benefits which the growth process is able to deliver to particular interest groups with the ability to disrupt that stability – which do to some extent, we shall argue, overlap with the benefits which it delivers to the poor. Our particular concern is to assess the extent of this overlap.

We now seek to model this process. The point of departure is that the low overall poverty elasticity of growth in Russia represents a potential political liability for the government, as it is symptomatic of the emergence of an underemployed underclass lacking the skills to hold down jobs in the new, albeit rapidly-growing, economy, and constituting a political threat especially if this poverty combines with other grievances. In those regions (depicted in table 2) where a perverse poverty elasticity combined with ethnic or other demands for autonomy, the federal state was vulnerable, and might be expected to pump resources into such regions to pre-empt politically destabilising action. The resources which it injected might come in various forms – subsidies on the prices of 'sensitive' items such as food and heating

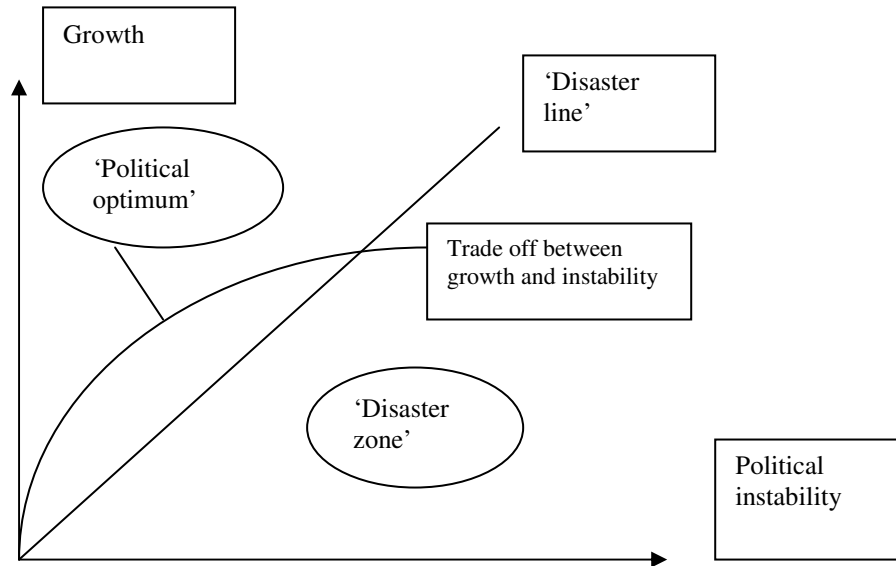
¹⁰ 'The general sense of rising prosperity has been one of the bases – perhaps the most fundamental of all – of Putin's popularity' Hanson (2007a) p. 872.

fuel, pensions, variations in the mix of public expenditures, and variations in the minimum wage, Collectively we refer to these alternative channels for injecting public resources into the economy as the *social efficiency wage* – an increase in the social wage designed to achieve greater economic stability, by analogy with the private efficiency wage of labour economics, in which increases in the private wage achieve increases in the stability and productivity of the labour force.

Our model (Figure 4) visualises a government determined, in whatever way it can, to maximise its chances of retaining its hold on power¹¹, and using the social efficiency wage as an instrument to enable it to do this. We assume that the government's hold on power will be improved by economic success (e.g. high rates of economic growth) but damaged by political instability. A high level of civil disruption combined with poor economic performance is a calamity for any government, and defines a 'disaster zone' in which the likelihood of holding on to power is very poor, as in Figure 4. We visualise that any rational government will wish, as an absolute priority, to keep away from this disaster zone – that is, it will choose the point, on the trade-off between these two objectives, which takes it the furthest possible distance away from the abyss.

¹¹ Appropriate behavioural assumptions for governments depend on decision-making mechanisms within government – see Drazen (2002) chapters 2 and 3.

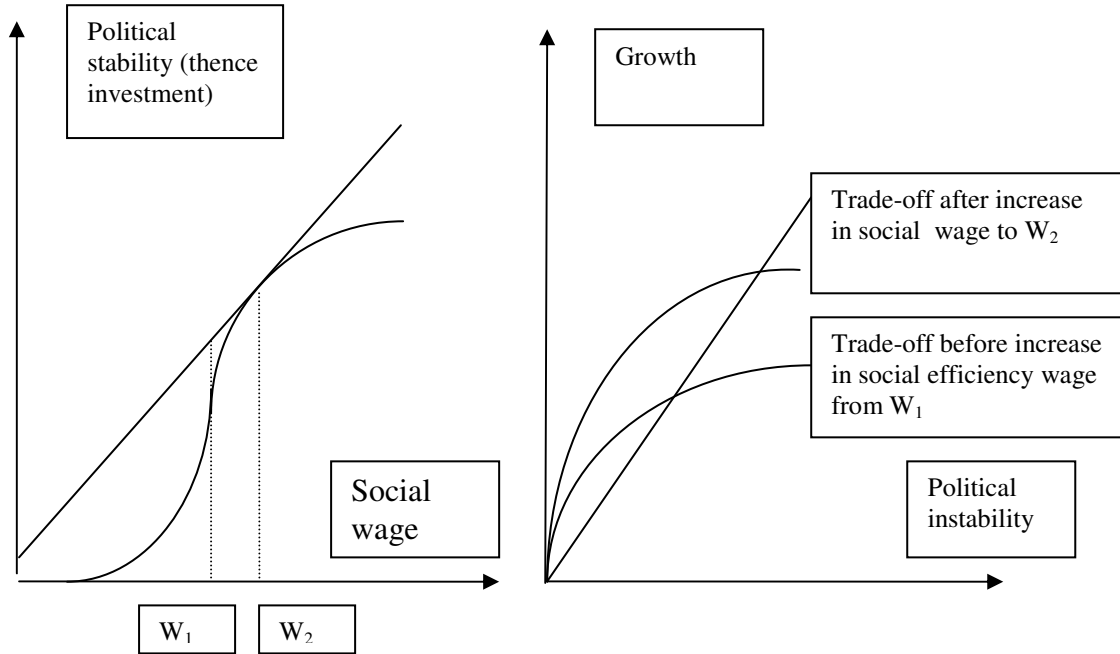
Figure 4. Economic performance and political stability – the trade-off and the disaster zone



The significance of the social efficiency wage instrument, in this context, is that if correctly chosen it will increase the incumbent government's chances of keeping away from the cliff-edge. We reason that up to a certain point, increases in the social efficiency wage (from W_1 to W_2 in the diagram of Figure 5), mediated through any of the instruments previously described¹², will move the trade-off so as to give it a better change of holding on to power. How effectively a government is able to do this depends on how well it is able to gauge the impact of changes in expenditure, through the channels of influence identified earlier, on the sensitivities of local interest groups.

¹² Changes in the expenditure mix, changes in the level of social expenditures, variations in pensions, and variations in subsidies/price controls seem to be the alternative formulations of this instrument most practised in Russia (see page above)

Figure 5. The ‘social efficiency wage’ and the government’s survival prospects



The government, therefore, as in Figure 4, maximises a utility function consisting of two elements: the size of the investible surplus, hence the growth rate (X) and risks to political stability (R). The notation of the model is in Table 4.

$$U = f_1(X, R) \quad (1)$$

In (1) the investible surplus X is simply the difference between the marginal product of labour (L) and its cost, which consists of the wage (w) plus any social efficiency wage premium (p) that is paid:

$$X = g(L) - w - p \quad (2)$$

The growth rate of labour productivity, $\partial g(L)/\partial t$, depends fundamentally on the standard factors of production of the new growth theory literature (capital K , skills H , initial income Y_0 , etc); but also on the risks of political instability, R .

$$\partial g(L)/\partial t = f_2(Y_0, K, H; R) \quad (3)$$

Table 4. Notation

Symbol	Meaning
X	Investible surplus
Y	National income
I	Investment
K	Physical capital
H	Human capital
L	Labour force
R	(Risk of) political instability
P	Poverty index (e.g. P_0)
p	Social efficiency wage (index of level and intersectoral allocation of social expenditure)
p^*	Optimal level of social efficiency wage
U(p)	'Universality of appeal' of policy instrument = coverage (in millions of persons) of instrument
A	External aid flows
S	External shocks
W	Wage rate
T	Transparency index (World Bank governance indicator)
C	Conflict history (level of conflict in previous periods)
σ	Index of income inequality

The risks to political stability , including the associated risk of conflict, depend on initial conditions (social capital, inequality σ , history of conflict C, etc), and on incidental shocks (S). But they also, and this is the main novelty of our approach, depend on the size of the social efficiency wage premium (p) which is paid:

$$R = f_3 (I(\sigma, C), S, p) \quad (4)$$

Within this expression, the impact of the social efficiency wage, p, on political instability, R, is the aggregate of its impact on specific social and occupational groups. Thus for social groups 1, 2...n,

$$dR/dp = ((\partial R_1/\partial p_1)dp_1 + (\partial R_2/\partial p_2)dp_2 + \dots + \partial R_n/\partial p_n)dp_n \quad (5)$$

and the key element in the setting of p consists in its allocation between different interest-groups. It will already be clear that the determination of the social efficiency wage depends on the relative perceptions, militancy and social leverage of different groups and specifically, in this context, on the ability of government to reduce the risk of blockage or rebellion by specific social groups, $\partial R_i/\partial p_i$, by varying the element of the social efficiency wage

which pertains to each of them.,.In the limiting case, if only one group is able to exercise influence, its preferences will dominate in determining the social efficiency wage; but typically its value will be determined by a process of coalition formation between different social groups (de Janvry, Fargeix and Sadoulet (1993)).

Thus, as in Figure 3, the recipient government maximises (1) subject to the requirement that the risk of conflict, which we see as proportional to the *ratio* of expected gain to expected loss, not fall below some disaster level¹³:

$$R < R^* \quad (6)$$

Thus, maximising government utility ((1)) subject to the constraint (6) and incorporating expressions (2) through (5), the optimal level of the social efficiency wage premium, p^* , is the value of p which solves

$$\frac{\partial(X-R)}{\partial p} - \lambda[(R - R^*)] = 0 \quad (7)$$

This solution condition reduces to:

$$(\partial/\partial p)[f_1(f_2(Y_0, K, H; R(p)) - w - p) - f_2(I(\sigma, C), S, p) - \lambda[f_2(I, S, p) - R^*]] = 0 \quad (7')$$

In other words, the optimal level of the social efficiency wage depends on initial conditions (inequality, social capital and past conflict history), the parameters of the aggregate production function (initial income, physical and human capital) and the impact-coefficients of social expenditure in favour of particular interest groups, p , on the risk of political instability, R :

$$p^* = f(I(\sigma, C), S; Y_0, K, H; \partial R_1/\partial p_1, \partial R_2/\partial p_2, \dots, \partial R_n/\partial p_n) \quad (8)$$

Further, from (3) the reduced form for the growth of productivity is:

$$\partial g(L)/\partial t = f_2(Y_0, K, H; f_3(I, S, p^*)) \quad (3')$$

where p^* is the value of p which solves (7')

An issue of particular interest is whether, in particular environments, the social efficiency wage reflects the preferences of the poor, so that it becomes good politics to practise expenditure policies which benefit low-income people. In the stabilisation and adjustment literature, there is a tradition of arguing that since the poor are not the most militant, and lack political leverage and

¹³ This is exactly the same approach as that taken in chapter 7 of Mosley et al(2003), where the farm household maximises utility subject to the requirement that income (or assets) not fall below some 'disaster' level.

resources, this is unlikely to be the case¹⁴. However, this tradition may now be incorrect: if the nonpoor see it as in their interest to form coalitions in support of policies which will promote the interests of the poor as well as theirs (such as universal primary education, in developing countries), or if there are powerful pro-poor external actors (such as non-governmental organisations and aid donors in developing countries) willing to exercise leverage in support of pro-poor expenditure patterns, then the adoption of a pro-poor expenditure mix will be politically attractive and will reduce instability.

What is the likelihood that the adoption of 'politically efficient' social efficiency wage policies, p^* , will result in a pro-poor outcome? We see the poverty leverage of the social efficiency wage, which we shall refer to by the symbol Φ , as being determined by four factors:

- (1) *the type of policy instrument chosen* – social policy instruments applicable to the entire population, such as the minimum wage and universal education and healthcare, are more likely to attract widespread political support and secure the formation of coalitions in their support than particularistic instruments focussed on poor people only (de Janvry and Sadoulet 1993);
- (2) *the distribution of post-tax income* – which we take as an indication of the representation of poor people in the power-structure (Alesina and Rodrik, 1994), and hence their ability to exercise control over the allocation of the social wage;
- (3) *the representativeness (degree of transparency) of the prevailing political regime* – the more willing the regime is to allow all voices to be heard, the more likely it is to allow a voice to poor people;
- (4) and finally, *the nature of external influence* – a variable reflecting, in particular, the influence of international financial agencies and aid donors. Where donors with a strong poverty-reduction ethos have influence on the mechanisms of internal policy-making – and this, as we have seen, occurred even in Russia during the 1990s – that is likely to bias the internal allocation of resources in a pro-poor direction, and when their influence recedes, then to an extent determined by the preferences and openness of the prevailing regime (factors 1 and 3) this bias may be corrected as the government breaks free of the need to defer to external forces.

Thus, in the notation of Table 4 above,

$$\text{poverty leverage } \Phi = f(U(p), \sigma, T, A/Y) \quad (9)$$

Thus the pro-poor impact of the prevailing growth pattern will be determined by, first, the representation of the poor in the setting of the social efficiency wage, as determined by (9), and second, the ability of the (private-sector)

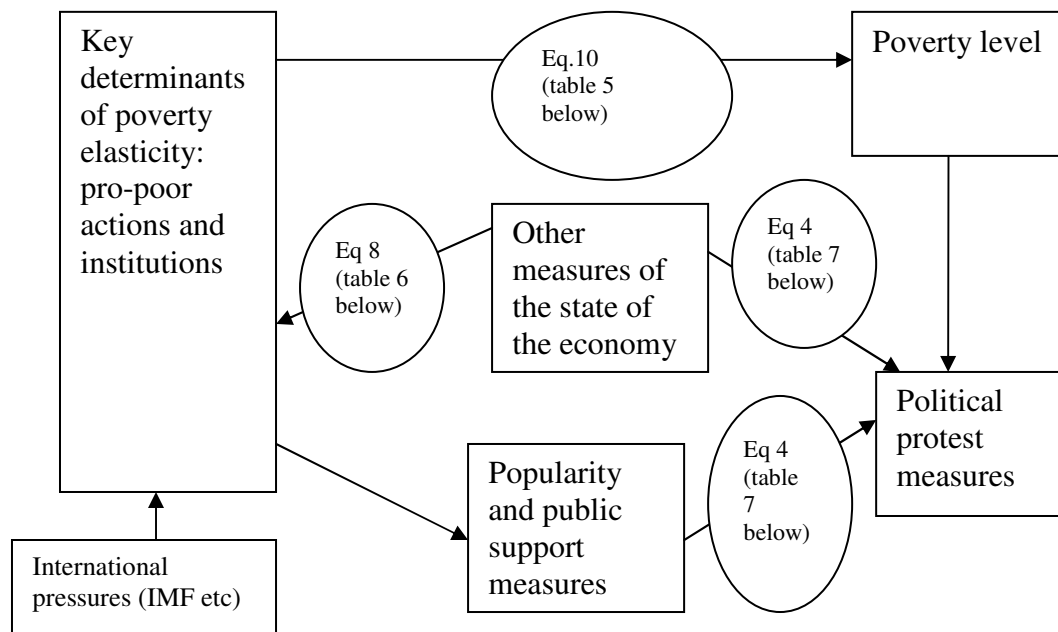
¹⁴ 'A focus on social equity is not necessarily relevant to understanding the politics of adjustment, because the politically most active groups are not usually the poorest' Haggard, Lafay and Morrisson(1995), p. 120.

growth process to reduce poverty, which we treat as related to capital-intensity, for reasons discussed earlier ()

$$dP = f[(\Phi(U(p), \sigma, T, \text{strategy variable})p^*), (K/L)Y] \quad (10)$$

Our main empirical and policy interest in what follows will be to establish the drivers underlying expression (4), the level of political instability, and in particular the influence of the social efficiency wage on it. However, the level of the social efficiency wage is endogenous, in particular to the distribution of power within society, as per (8), and it is also fundamental for us to understand the driving forces behind the level of poverty, as in (10). The interaction of these three causal relationships, as in Figure 5, constitutes the essential story which we wish to investigate.

Figure 5. Causal model



The model which we seek to estimate in the next section (figure 5) is, therefore, a model of circular causation linking these three core relationships: public policies and other factors determine the level of poverty; revenue, political structure, political violence and other factors determine public policies; and poverty and other factors determine the level of political violence. The model reduces, under certain parameter values, to a 'vicious circle of poverty' model in which lack of resources constrain the ability to buy off protest which weakens the state, and one dilemma for weak governments

is how to escape from this vicious circle¹⁵. Russia is not ordinarily thought of as a weak state, but the duration and severity of economic crisis transitorily made it one during the 1990s, and a major priority for the Putin administration, as discussed above has been to shield the federal administration against any risk of being re-enmeshed in the vulnerabilities experienced at that time.

4. Empirical strategy and tests

Altay - Table of descriptives wanted here.

In this section we estimate the reduced forms of the three basic linkages in the model – the poverty equation (10), the equation for the social efficiency wage (8) and the equation for conflict (4), against data for each of the 89 ‘federal subject’ territories of Russia, with a view to understanding the determinants of regional variations in poverty levels and in the elasticity of poverty with respect to the renewed growth of the years 2000-07. We operate with a number of alternative specifications of our key variables: the social efficiency wage is alternatively defined as social spending, social spending plus housing, pensions expenditure and the level of the minimum wage; and ‘the threat of conflict’ is variously defined as indicated willingness to protest against the government (as expressed in VTsIOM opinion polls¹⁶) and as votes for the Communist party (the principal opposition party). Our estimates are displayed in tables 5 through 7.

Determinants of poverty and deprivation

Our poverty equation (equation (10)) expresses poverty as a function of the propensity to take on low-income labour (the capital intensity) of the regional economy, and of the level of the social efficiency wage. Our estimates (table 5) suggest that both of these factors are significant in determining poverty elasticity: poverty is significantly responsive to social expenditure (only at the 10% level in equation (2), to the level of regional infrastructure, and to the salience of the energy sector. We take this as a proxy for capital-intensity: the oil and gas sectors, which accounted for 27% of output and 60% of the country’s exports in 2006, employ fewer people than the Russian railways, and employ only 2 per cent of the employed workforce (Hanson 2007: 873-874).

¹⁵ For an application of this approach to Bolivia – which remained mired in a state of economic and political crisis for much longer after the global economic disturbances of 1997-2000 than any other country involved in them – see the paper by Mosley (2007).

¹⁶ VTsIOM () is the (nationalised) opinion-polling and survey agency.

**Table 5. Regression equations: dependent variable poverty (P)
(equation 10))**

Russian Federation: data for 89 'federal subject' regions 1995-2006

Estimation method: XT fixed-effects regression			
Regression coefficients on independent variables:			
Constant	0.52 (8.47)	2.09** (2.11)	-0.29 (0.17)
Log(per capita gross regional product)	-0.22*** (4.60)		
' <i>Social efficiency wage 1</i> ' Log (social expenditure)	0.18*** (2.82)	0.26* (1.67)	
' <i>Social efficiency wage 2</i> ' Log (social expenditure with housing)			0.71** (2.30)
Road expenditure	0.003*** (3.05)	0.038 (0.19)	
Energy sector	-0.0008 (0.46)	0.09** (2.02)	0.118* (0.91)
Year dummy 4	-0.12*** (2.62)		
Year dummy 5	0.054 (1.16)		
Year dummy 6	0.41*** (6.43)	0.19** (2.46)	0.31** (5.83)
Year dummy 7	0.50*** (6.55)		
Year dummy 8	0.46*** (5.22)		
Year dummy 9	0.35*** (3.54)		
Year dummy 10	0.35** (2.45)	-0.19** (2.41)	
Year dummy 11	0.18 (1.53)		
Number of observations	671	222	151
R ² (within group)	0.6036	0.5287	0.7102
R ² (between groups)	0.0882	0.0782	0.0687
R ² (overall)	0.1729	0.2574	0.2722

Source: *Regiony Rossii*, 2007 edition.

Notes: Figures in parentheses underneath coefficients are Student's t-statistics.

Row 4 - Energy sector = salience of energy sector within region (*Altay*-please check this)

Social expenditure and the 'social efficiency wage'

Only recently have attempts been made to explain social expenditure endogenously in developing and transitional economies, as a response to trends in the surrounding economy and society. The most significant recent contribution to this literature is the book by Haggard (2006), which lays particular emphasis on fiscal constraints on welfare spending – indeed, explains the differential evolution of welfare spending in the transitional, Latin American and Asian economies in these terms – and also sees the degree of democracy – the World Bank's so-called 'polity' variable – as being an important determinant of social spending. As indicated by Table xx {table of descriptives - not yet included - social expenditure has expanded substantially in real terms since 2000, as part of the expanded role of the state which is apparent both in Russia¹⁷ and in other post-crisis countries since 2000 (Hanson, 2007a; Grugel and Ruggirozzi (2007 for Argentina) *add extra examples if possible*. We see this, specifically in the Russian context, as a variable whose role is not only to redistribute resources equitably but explicitly to pre-empt the possibility of conflict, and thus as related to the threat of conflict. We find that indeed this is the case: even controlling for the 'Haggard factors', revenue and local democracy indicators, our measures of political threat (expressed intention to protest and votes for the communist party at the regional level) are, at the 10% level, significant influences on the level of all indicators of the social efficiency wage, and local social expenditures have in particular been higher in areas where the local separatist threat is more significant (Ossetia, Dagestan, Tuva Republic, and of course Chechnya)¹⁸. There is also a progressive' response, not always significant, to the level of headcount poverty. Other likely underlying factors contributing to the rise in the social efficiency wage (the Φ coefficient, in the notation of equations (8) through (10)) are the improvement in the Gini coefficient of inequality since 2000 (Mussurov and Mosley 2007) and, paradoxically, the *reduction* in the degree of external pressure to make expenditure policy poverty-focussed. Once external pressure diminished, internal policy was free to respond purely to domestic imperatives – and as these increasing came from groups with an interest in speaking up for those disenfranchised by reform, this dictated an increasingly progressive use of fiscal instruments.

Altay - Check that this holds good with all alternative indicators of the SEW. Eventually, add section on which SEW indicators are chosen at

¹⁷ . Private sector share of Russian GDP 70 per cent in 2000-2004, down to 65% in 2005 and 2006 – Hanson(2007a) p877

¹⁸ The government has made disparaging remarks on the (political and otherwise) productivity of this expenditure; refer to Putin's(?) remarks on this theme (*Altay source please*)

which time, according to relative perceptions of which group most needs to be placated (esp pensioners – Jan 05, min wages – late 90s, according to Treisman and Gimpelson]

Table 6. Regression equations – dependent variable social efficiency wage (as specified in top row of table equation 10))

Russian Federation: data for 89 'federal subject' regions 1995-2006

Estimation Method	Random-effects GLS	XT fixed-effects OLS	XT fixed-effects OLS
<i>Specification of 'social efficiency wage'</i>	Social expenditure only	Social expenditure only	Social expenditure with housing
<i>Regression coefficients on independent variables:</i>			
Constant	3.72*** (24.39)	2.70*** (5.61)	4.71*** (13.45)
Social expenditure(one-year lag)		0.43*** (6.01)	
Poverty headcount		0.063 (1.45)	0.057 (1.28)
Revenue		-0.064** (2.42)	-0.064** (2.44)
Regional democracy			
Log (political protest – participation in demonstrations)	0.05* (1.91)		
Log (political protest – vote for Communist party)		-0.051 (1.09)	-0.075* (1.85)
Year dummy 6		-0.028 (0.63)	0.069* (1.56)
Number of observations	82	156	151
R ² (within group)	0.4044	0.4842	0.6212
R ² (between groups)	0.0769	0.2787	0.0019
R ² (overall)	0.2164	0.3905	0.0750

Political militancy and the threat of violence (equation (4)). We have argued that pro-poor action, and thus the poverty elasticity, is driven by the threat of violence, as well as by underlying fiscal capacities and political characteristics. The equation in which we seek to explain this political instability ((4) above) is an offshoot of the ‘economics of conflict’ literature, which visualises conflict not as an ethnically- or politically-based irrationality, but rather as a course of action which may be rational if there is sufficient to gain (ie the state becomes weak enough at local level for the strategy of seeking to take it over to have rational prospects of success) or little to lose (ie they become sufficiently desperate to have few alternative strategies to taking up arms) (Collier and Hoeffler 1998, 2004). Our own spin on this literature (Fiess et al 2007) adapts the ‘rational conflict’ approach to the case of riot-type conflict, which certainly in Russia, and indeed in the many transitional and developing countries, is more characteristic of the kind of conflict feared by the authorities than the outright civil war analysed by Collier and Hoeffler, as in the Kuzbas miners’ strikes of 1997, 1999 and 2001? (*Altay help!, can we fit in the specifics*) and the pensioners’ protest of January 2005¹⁹. We see (the threat of) conflict of this type as something which is indeed motivated by individual and collective rationalities, and is increased by random shocks and increases in volatility and by increases in the militancy of the opposition, but importantly as a threat which can be offset, as in equation (4), by appropriate adjustments of the social efficiency wage, as well as by improvements in the perceived fairness of the income distribution.

In table 7, we estimate the level of both individual and collective political protest (in the shape of the vote for the principal opposition party, the Communists) to these economic variables. We find (column 5 of the table) that the level of protest is indeed responsive to the level of local social expenditure, in the definition which includes housing. It is also responsive (columns 3 through 5) to local levels of unemployment and (much more significantly) to local levels of inflation, which probably provides part of the key to the issue just discussed – what instrument of pro-poor action to use (*connect with discussion on page 20/21*). There is a possibility, not yet tested, that at the federal level the decline in the level of militancy may have a connection with the increase in the equality of the post-tax income distribution (the decline of the Gini coefficient of inequality). At the individual level, the threat of militancy is responsive to the level of wage arrears, as also to local economic conditions and to one of our other indicators of militancy, the vote for the Communist party leader Zyuganov. It is also higher, following our earlier argument, in rural areas which suffered very badly in the slump and have not recovered in the subsequent boom.

¹⁹ The one place where the threat of conflict does border on civil war is of course Chechnya

Table 7. Regressions – dependent variable political protest

<i>Estimation Method</i>	XT fixed effects OLS		XT fixed-effects OLS	XT fixed-effects OLS	
<i>Specification of dependent variable</i>	Individual-level- likelihood of protest against the local authorities		Regional-level : likelihood of protest against the local authorities	Regional level: vote fro Communist party	
	NB these are STANDARD ERRORS in parentheses	NB these are STANDARD ERRORS in parentheses	NB t-stats in parentheses	NB t-stats in parentheses	
<i>Regression coefficients on independent variables:</i>	Autumn 1998	Autumn 2000	Panel 1998-2006	Panel 1998-2006	
Constant	-1.491*** (0.151)	-1.507*** (0.161)	0.300 (0.21)	-1.05 (0.58)	0.20 (0.01)
Wage arrears	0.255*** (0.099)	-0.061 (0.085)			
Poverty within region				-0.05 (0.67)	0.012 (0.12)
Unemployment within region			0.132 (1.08)	0.032 (0.52)	-0.050 (0.57)
Inflation within region			0.54** (1.88)	0.77** (2.33)	0.91* (1.66)
Social expenditure (with housing) in region					-0.43* (1.62)
Female	-0.056 (0.074)	0.162** (0.084)			
Rural	0.193** (0.093)	-0.024 (0.114)			
Siberia	-0.067 (0.099)	-0.135 (0.111)			
University	0.077 (0.104)	0.031 (0.083)			
Family's welfare	0.038 (0.098)	0.008 (0.090)			
Stop reforms	0.186** (0.082)	0.221** (0.108)			
Age below 30	0.047 (0.083)	-0.048 (0.093)			
Big city	-0.392** (0.114)	-0.379** (0.099)			
Voted Yeltsin	-0.080				

	(0.093)				
Voted Putin		0.058 (0.088)			
Voted Zyuganov (Communist)	0.315*** (0.109)	-0.160 (0.152)			
Local economy	0.358*** (0.094)	0.454*** (0.090)			
Dissatisfied	0.191** (0.091)	0.124 (0.090)			
Future welfare	0.178** (0.078)	-0.061 (0.100)			
Dependency ratio	-0.180 (0.156)	-0.037 (0.45)			
Year dummy 5			0.20 (1.38)		
Year dummy 6			0.10 (1.16)	0.51** (2.83)	0.53** (4.16)
Year dummy 7			0.40*** (5.50)		
Year dummy 9			-0.24** (2.90)		
Year dummy 10				0.01 (0.04)	
Year dummy 11			-0.14 (1.56)		
Number of observations	3292	3235	239	231	156
P-value	0.000	0.000	0.000	0.0000	0.0000
R ² (within group)			0.2778	0.8056	0.9037
R ² (between groups)			0.0094	0.1595	0.0280
R ² (overall)			0.1254	0.3504	0.3434

Sources: cols 1 and 2: Mussurov and Mosley (2007) cols 3 through 5, *Regiony Rossii*, give further details.

4. Conclusions

In this paper we have sought to understand and analyse the experience of Russia since the crisis of 1998, which is an experience of slow and gradual reduction of poverty since the millennium following a long-drawn -out and severe recession during the 1990s. Underlying the slowness of the reduction in poverty, we have argued, is a fundamental characteristic of the Russian structural adjustment process – a shift away from labour-intensive and previously heavily protected manufacturing towards the more tradable, but more capital-intensive, oil, gas and minerals sectors, which are only to a very limited extent capable of providing livelihoods for the millions shaken out of the non-traded sector by the process of adjustment. As a consequence, the growth which has taken place has produced only very limited reductions in poverty, and in some places poverty has actually increased. Where these locations coincide with existing ethnic and other resentments, the Russian state is

still vulnerable, we argue, in spite of its resounding success in the recent elections.

We analyse the local response of poverty to growth (the ‘poverty elasticity’), which we interpret as determined by political forces –in particular the willingness and skill of the authorities in buying off local resentments by fiscal means as well as the economic factors previously described. We do this within a theoretical framework which visualises the mix of social policy instruments as a ‘social efficiency wage’, analogous to the efficiency wage of labour economics. In Russia, our estimations suggest that the social efficiency wage is a significant determinant of local poverty levels and poverty elasticities, and various incarnations of the social efficiency wage are responsive to the level of political protest, holding constant the levels of local revenue and local democracy. The level of local protest, in turn, is capable simultaneously of being contained by the level of the social efficiency wage, and responds also to local economic conditions – in particular the level of the consumer price index. Thus both at local and national level, pro-poor policies have been used to hold in check the continuing fragilities in the apparatus of government – contrary to a conventional wisdom which insists²⁰ that, especially in strong and centralised states like that of Russia, the poor are unlikely to have political leverage.

²⁰ Cf. passage keyed by footnote 14 above.

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To sort (for interviews 21/1 if they can't be sorted)

pp 7/8 – economic gainers and losers and their political attitudes (communist or otherwise)

pp 9/10 - quotes if possible on where the government saw itself as being vulnerable (regions, interest groups) and why it saw particular instruments as the right ones to head off protest.

p15 – equation 3 - ? reestimate with autonomous republic dummy to link with RES paper.

p17 – table of descriptives wanted.

p17 – 'equation 1', table 5 - (Altay please check definition of social expenditure)

Notes: row 4 - Energy sector = salience of energy sector within region (Altay-please check this)

p19 – 'equation 2', table 6, Altay you said this became significant if the vote for United Russia was included – include this.

p20 – footnote 18 – source for Putin's disparaging remarks (was it Putin's?) needed here.

p22 – specifics needed for miners' strikes and pensioners' protest – maybe these can be formalised as an additional indicator of protest.

Econometrics section – simultaneous equations approach – either try, or give good econometric reasons for taking this approach.