



European Bank  
for Reconstruction and Development

# TRANSITION REPORT 2016-17



[tr-ebrd.com](http://tr-ebrd.com)

Transition for all:  
equal opportunities  
in an unequal world



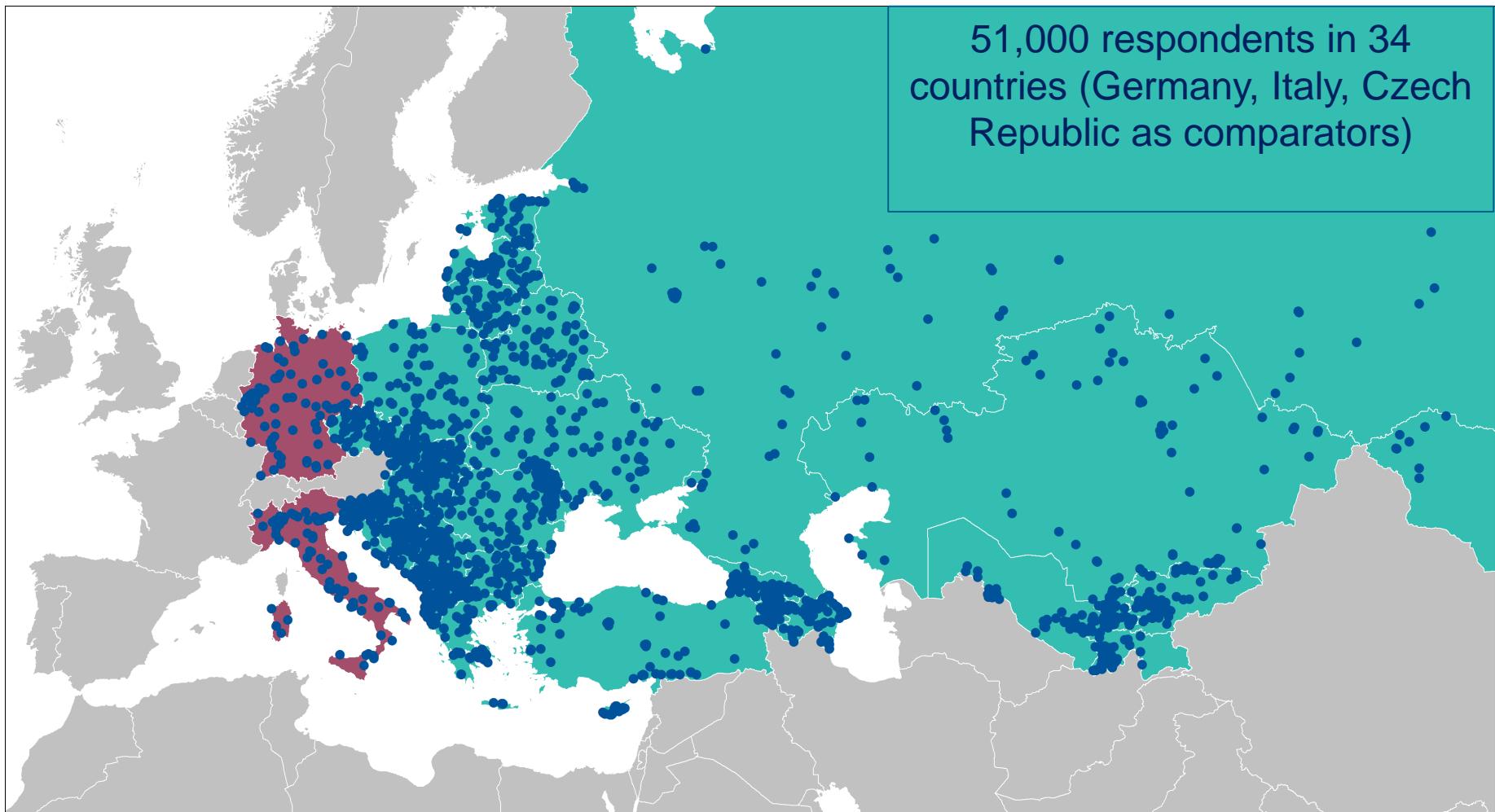
## A look beyond average growth

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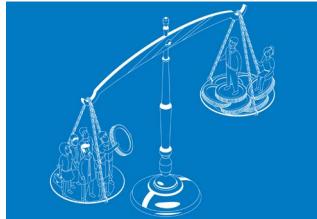
- What have individual experiences of transition been like in terms of income, happiness and health?
- Who benefited from transition and globalisation? Who did not?
- Who currently lacks economic opportunities?
- How can equality of opportunity be improved?

For the first time, a Transition Report focused on *inequality*

# A unique survey: Life in Transition III



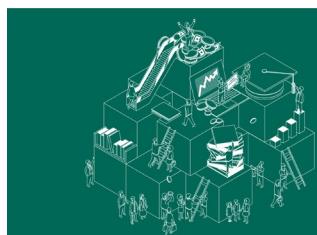
# A look beyond average growth



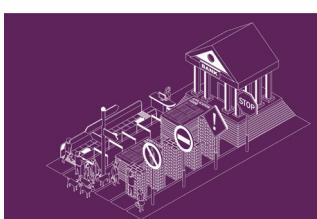
- I. Income convergence – how did individual experiences vary?



- II. The impact of transition on people's well being



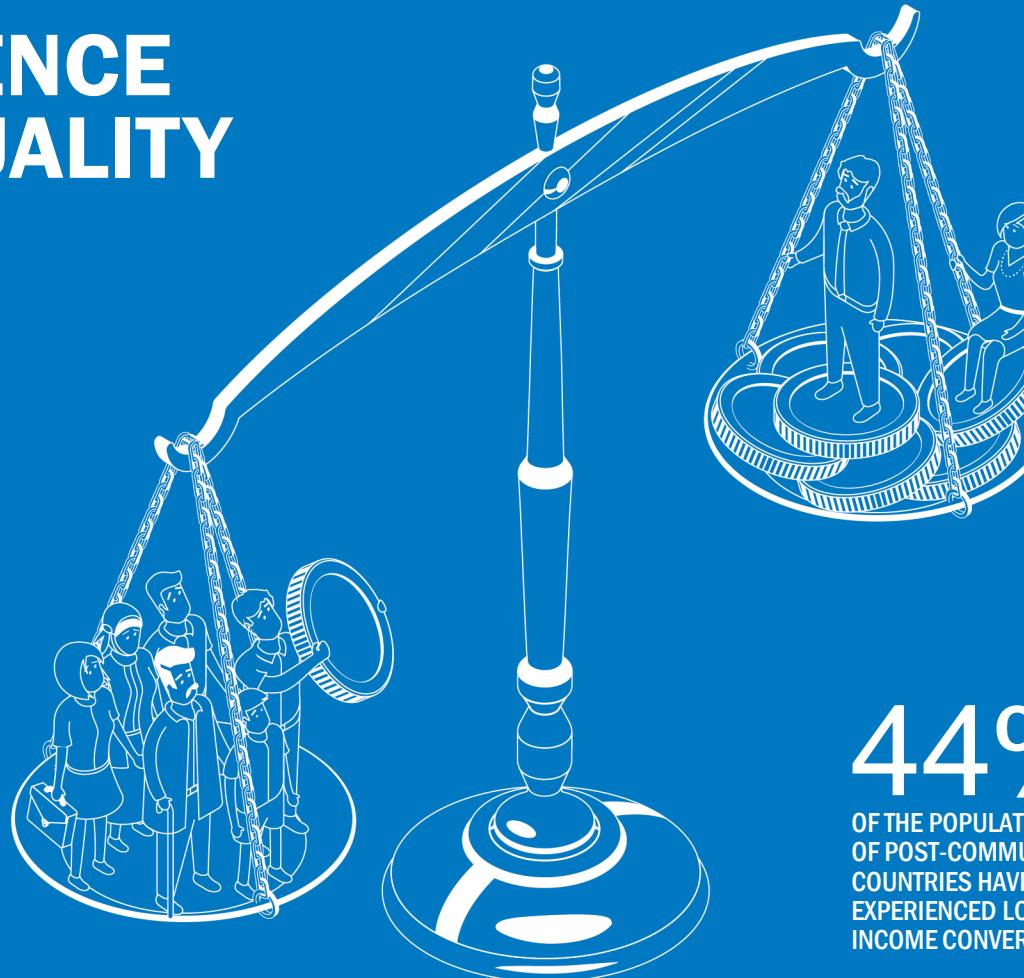
- III. Inequality of opportunity



- IV. Financial inclusion

# CONVERGENCE AND INEQUALITY

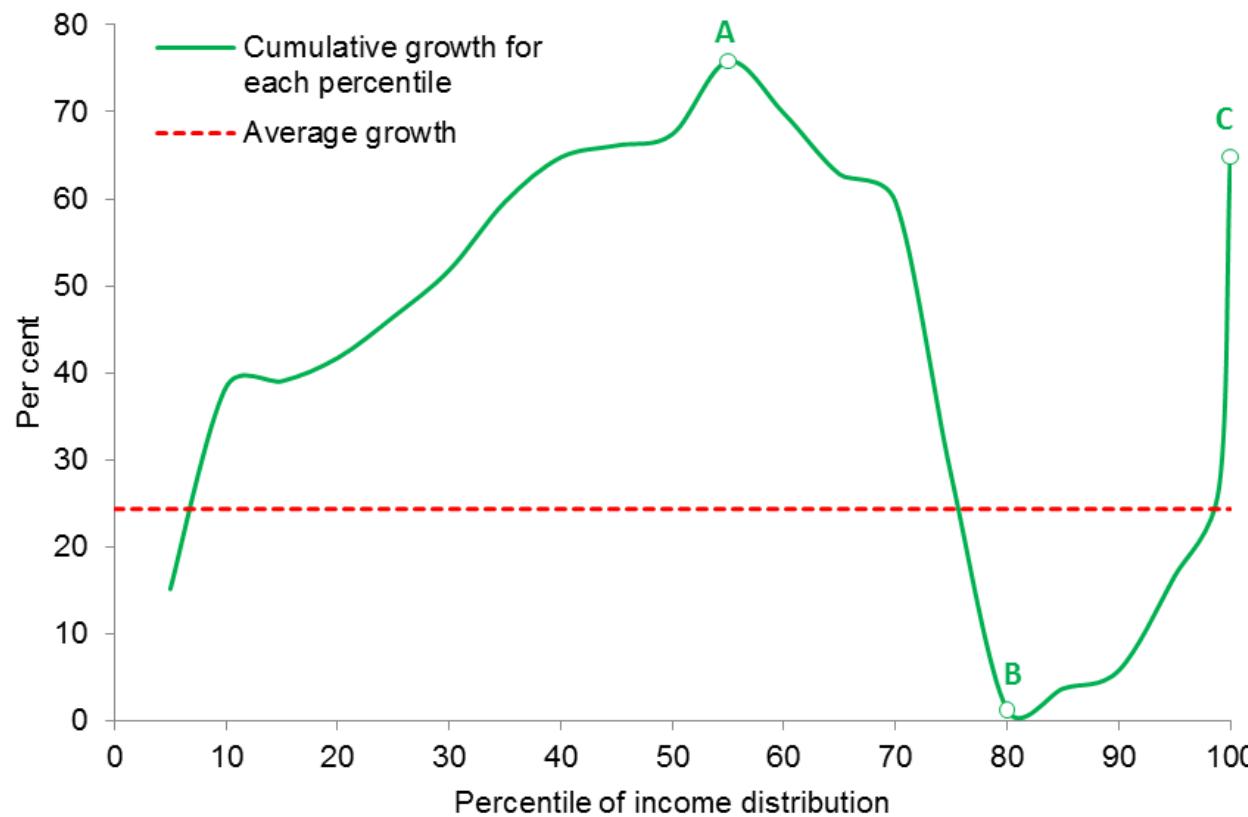
AROUND  
**60%**  
OF THE WEALTH OF THE REGION'S BILLIONAIRES IS DERIVED FROM COMMODITIES, UTILITIES AND REGULATED SECTORS, COMPARED WITH AROUND 13% IN ADVANCED ECONOMIES



**44%**  
OF THE POPULATION OF POST-COMMUNIST COUNTRIES HAVE PERSONALLY EXPERIENCED LONG-TERM INCOME CONVERGENCE

# Global experience – the “elephant curve”– middle class in advanced economies losing out

Relative gain in real per capita income by global income level, 1988-2008



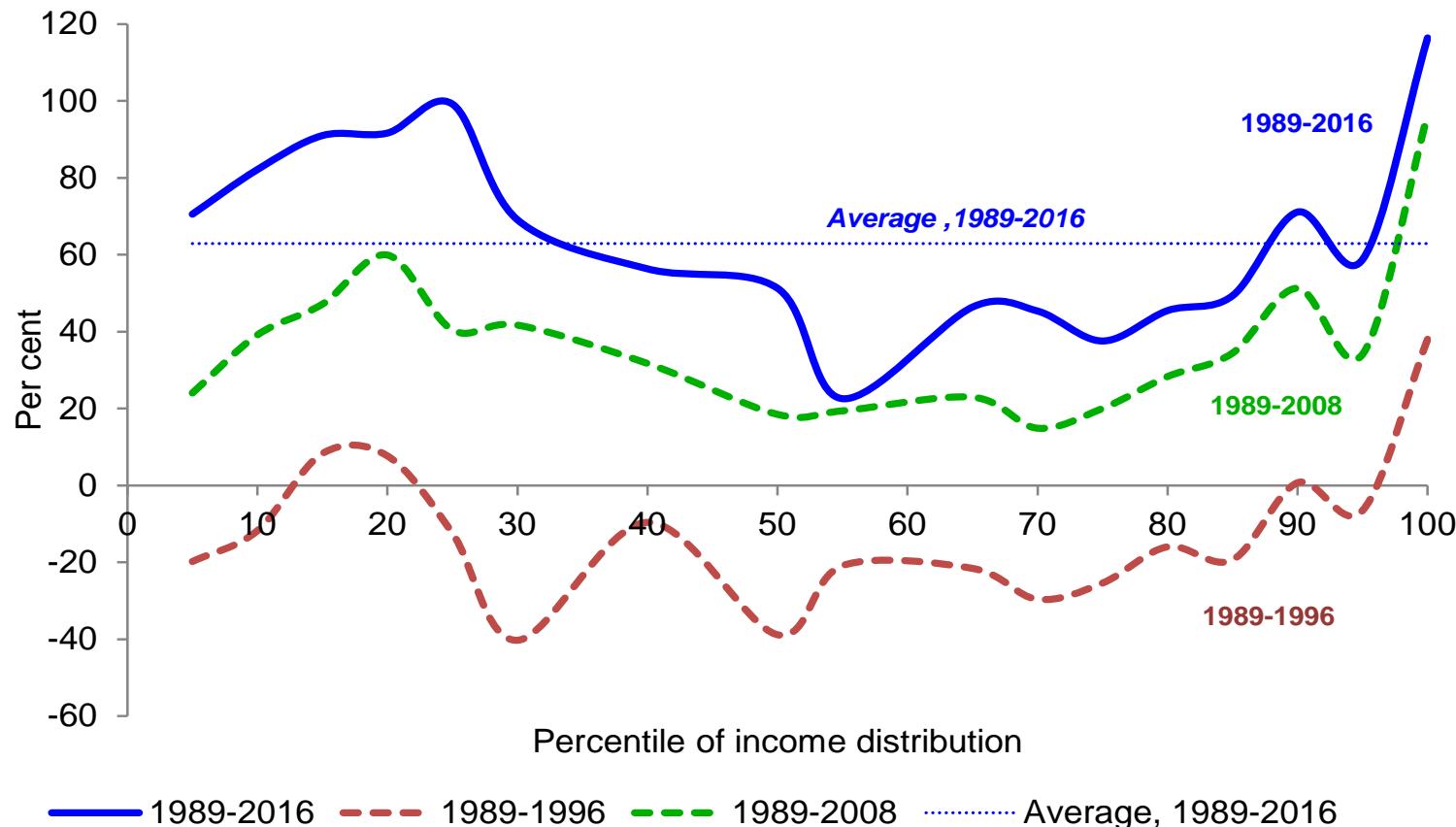
Sources: Lakner and Milanovic (2016)

Note: Analysis based on income shares of each decile and income growth.

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# In EBRD region: winners are the well-off in higher-income countries and upper-middle in lower-income countries

EBRD region: Cumulative growth in income since 1989 depending on initial income

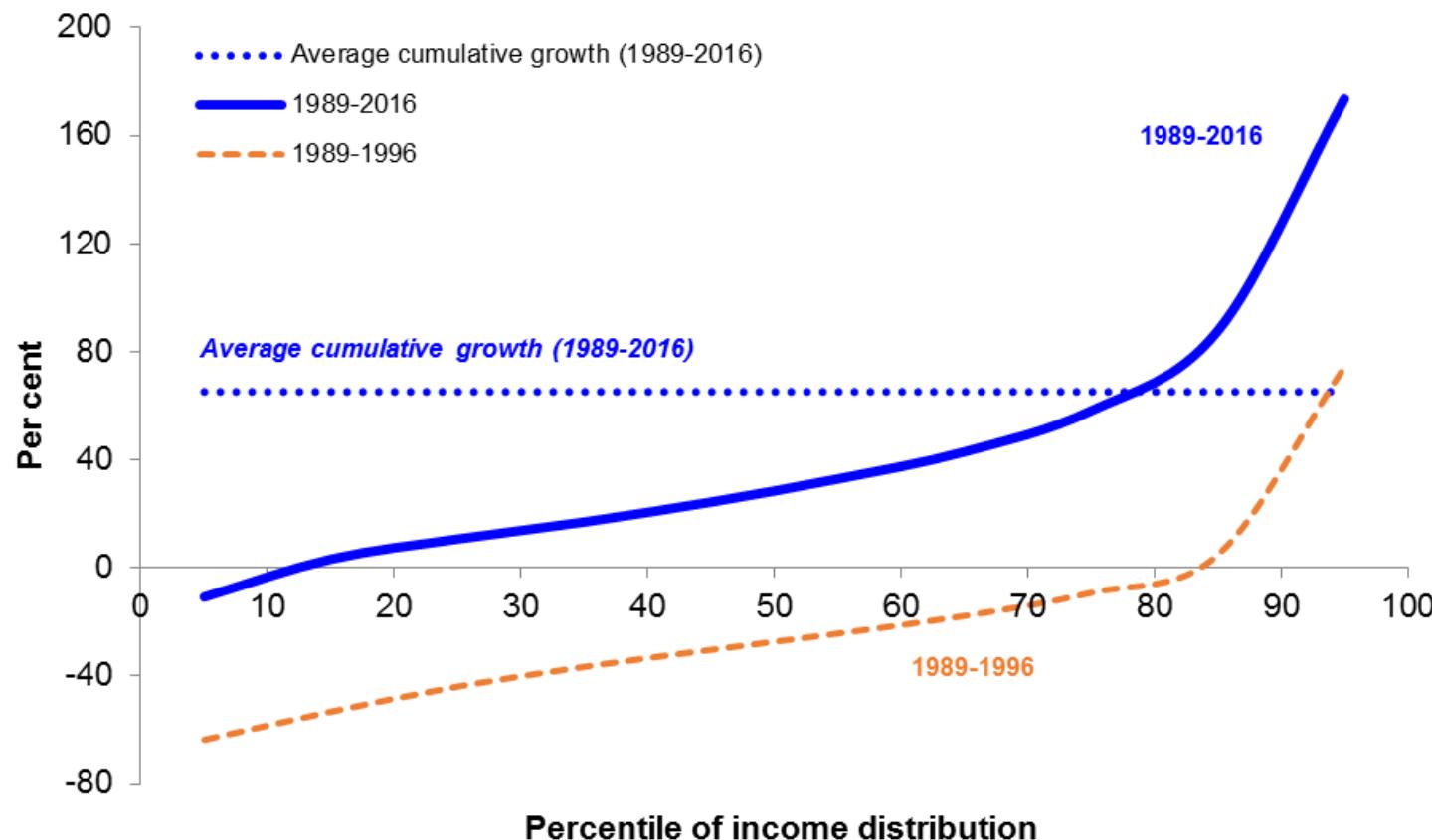


Sources: Povcalnet, IMF, World Bank, UN, and authors' calculations based on the methodology in Milanovic (2016).

Note: Calculations trace income growth of a specific decile in specific country in 1989 but not specific individuals.

# Within countries: Impressive convergence on average – but gains depend on one's place on the income ladder

Russia: Cumulative income growth since 1989 by income decile



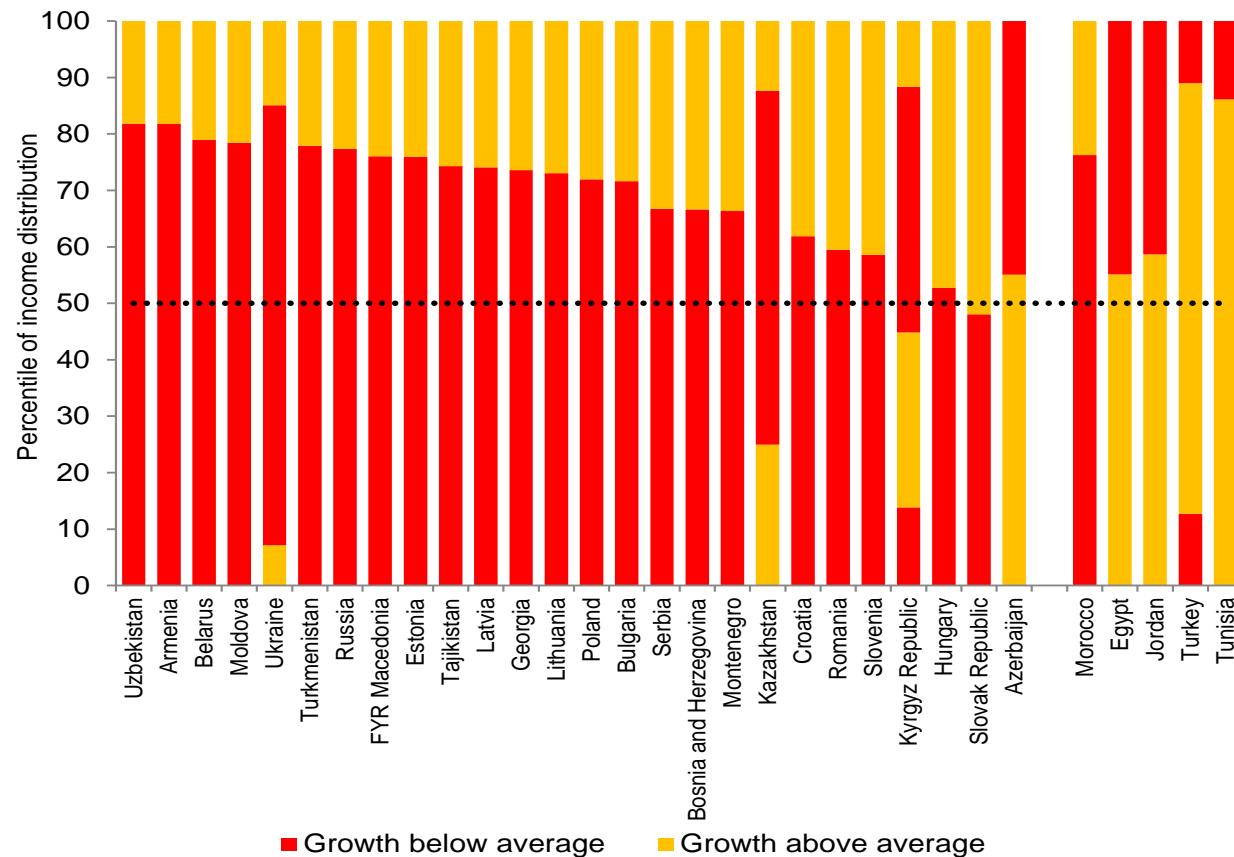
Sources: National authorities, World Bank Povcal database, IMF, UN and authors' calculations.

Note: Analysis based on income shares of each decile, income growth and various assumptions to fill in the gaps.

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# The income of only 27% of all people grew at a rate at par or above their countries' average

Percentiles of population with below-average income growth (1989-2016)

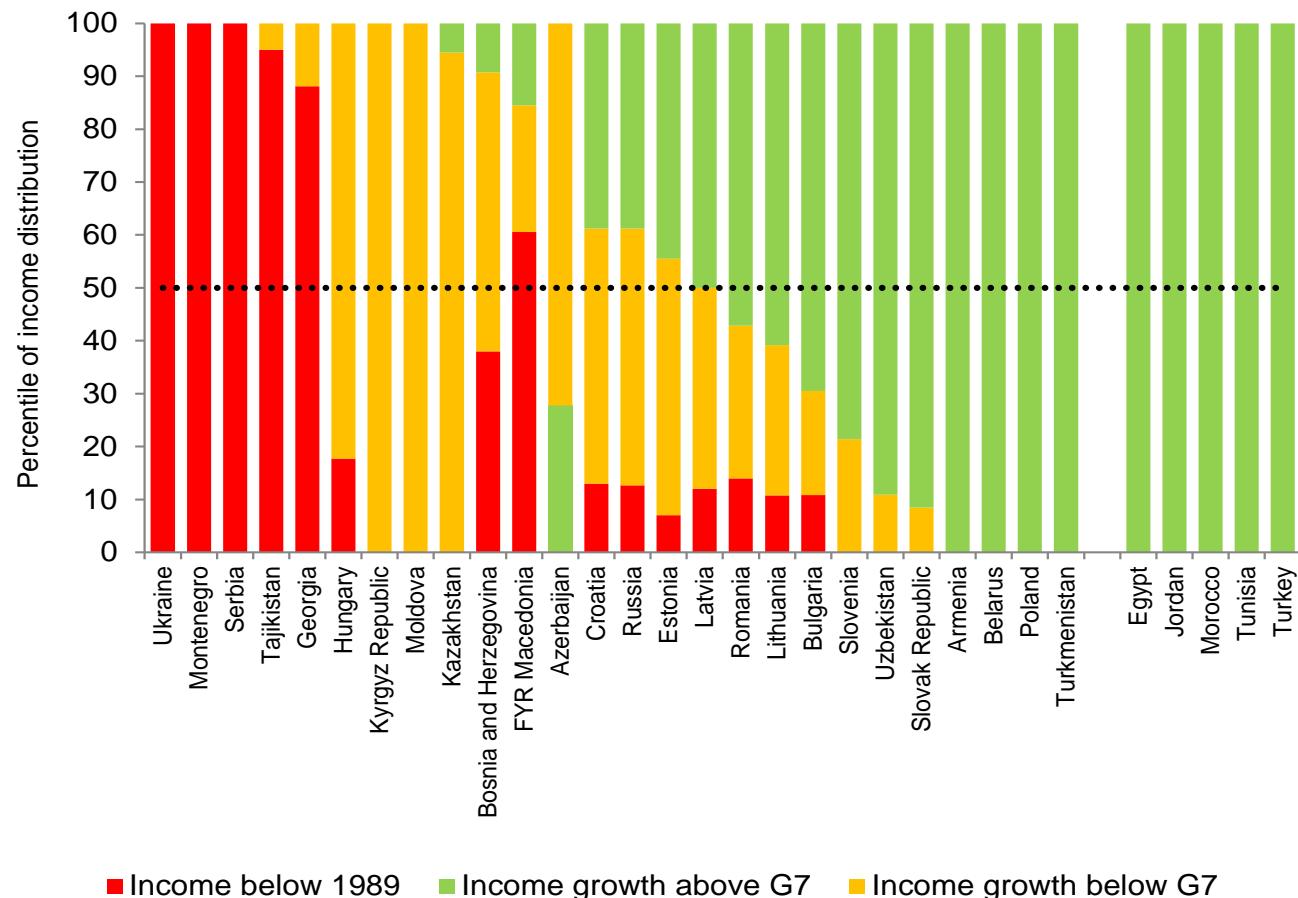


Sources: World Bank Povcalnet, IMF, World Bank, UN, authors' calculations .

Note: Bars ranked by income decile (bottom to top).

# Only 44% of all people have experienced long-term income convergence with G7

Percentiles of population with income growth below the G7 country average (1989-2016)



■ Income below 1989 ■ Income growth above G7 ■ Income growth below G7

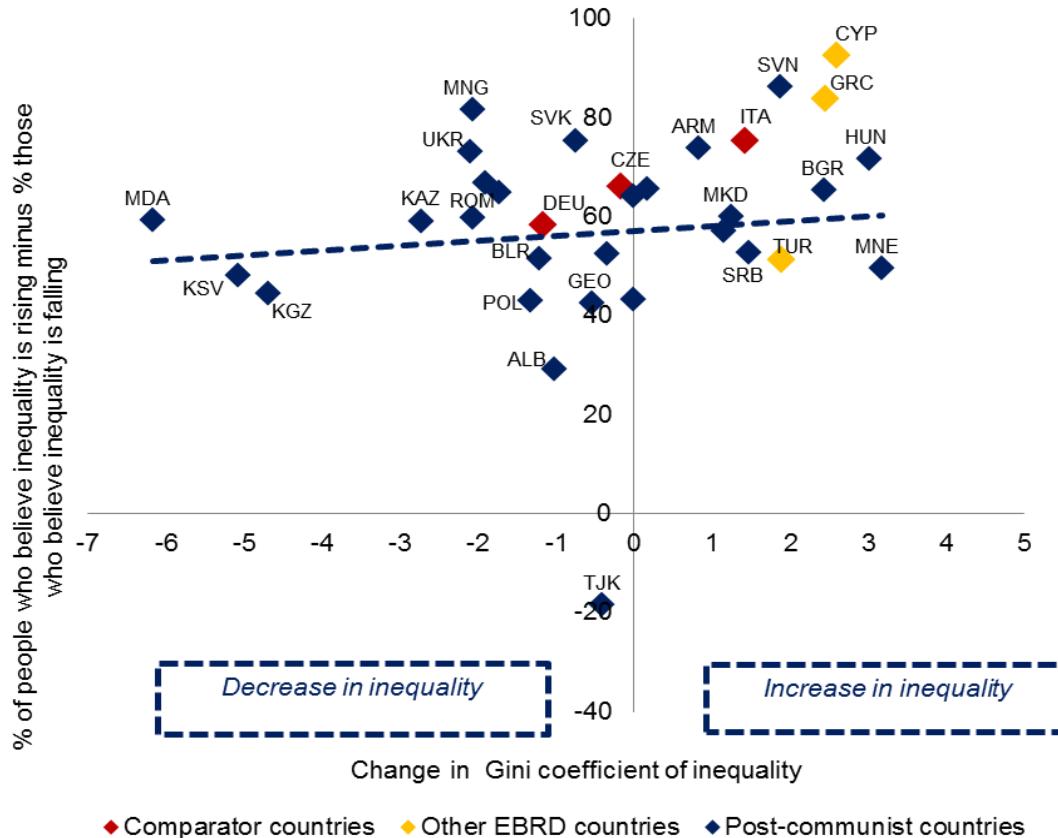
Sources: Povcal, IMF, World Bank Povcalnet, UN, authors' calculations.

Note: Bars ranked by income decile (bottom to top).

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# Income inequality remains modest but is perceived as high and rising – and perceptions matter

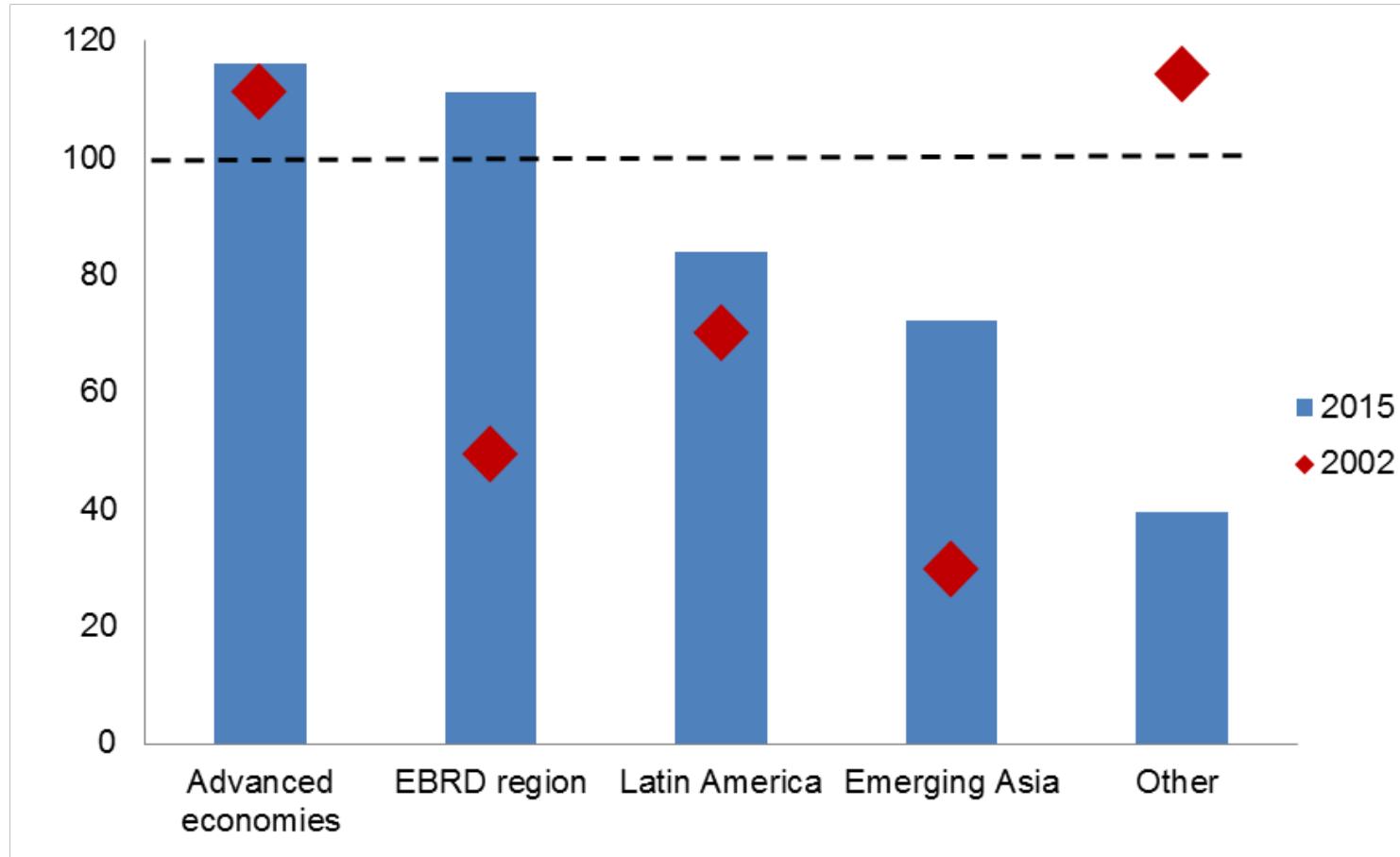
## Changes in inequality: measured and perceived



Sources: World Bank Povcalnet, Solt (2014), LiTS III and authors' calculations.

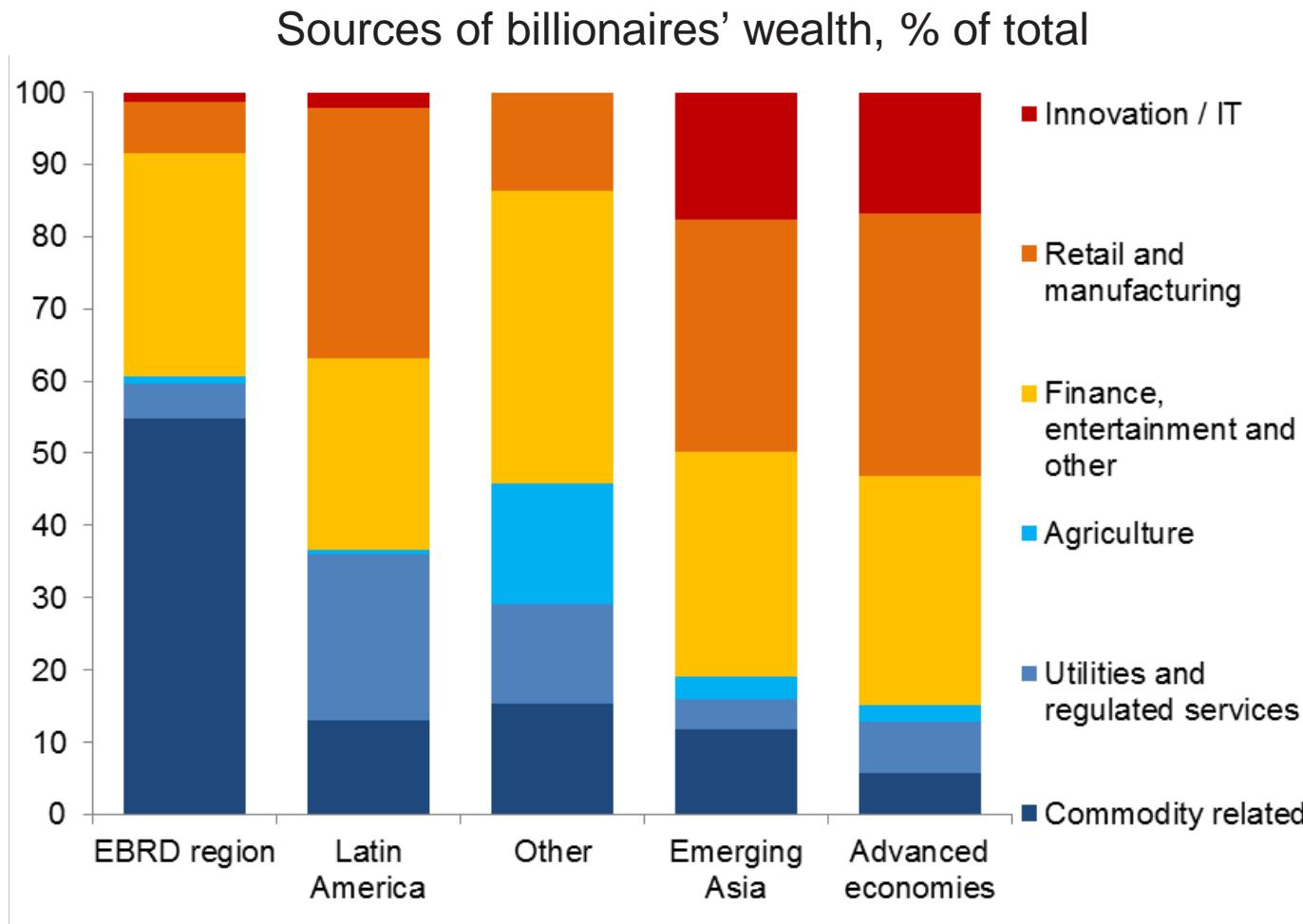
# Concentration of wealth at the top is high by international standards

Regional share of global billionaire wealth in % of regional share of global GDP



Sources: *Forbes*, IMF WEO and authors' calculations.

# And driven mostly by commodity rents, rather than innovation or competitive manufacturing



Sources: *Forbes* and authors' calculations.

# Wealth concentration, inequality, poverty: Different phenomena, different responses

## Wealth concentration

- Taxing wealth
  - 0.8% of GDP in EBRD region vs. 2% in OECD
- Taxing inheritance and rents
- Better institutions, governance and transparency
- Diversifying economies
- Stronger competition

## Inequality

- Redistribution:
  - Progressive income taxes and cash transfers; other fiscal measures
- PREdistribution
  - Reducing inequality of opportunity: education, health; access to finance

## Poverty

- Subsidies and cash transfers
- Targeted / means-testing with strong administrative capacity and monitoring
- Conditional transfer programmes (for example, school attendance; job search)

# THE IMPACT OF TRANSITION ON WELL-BEING

ON AVERAGE, PEOPLE BORN AROUND THE TIME OF TRANSITION ARE AROUND

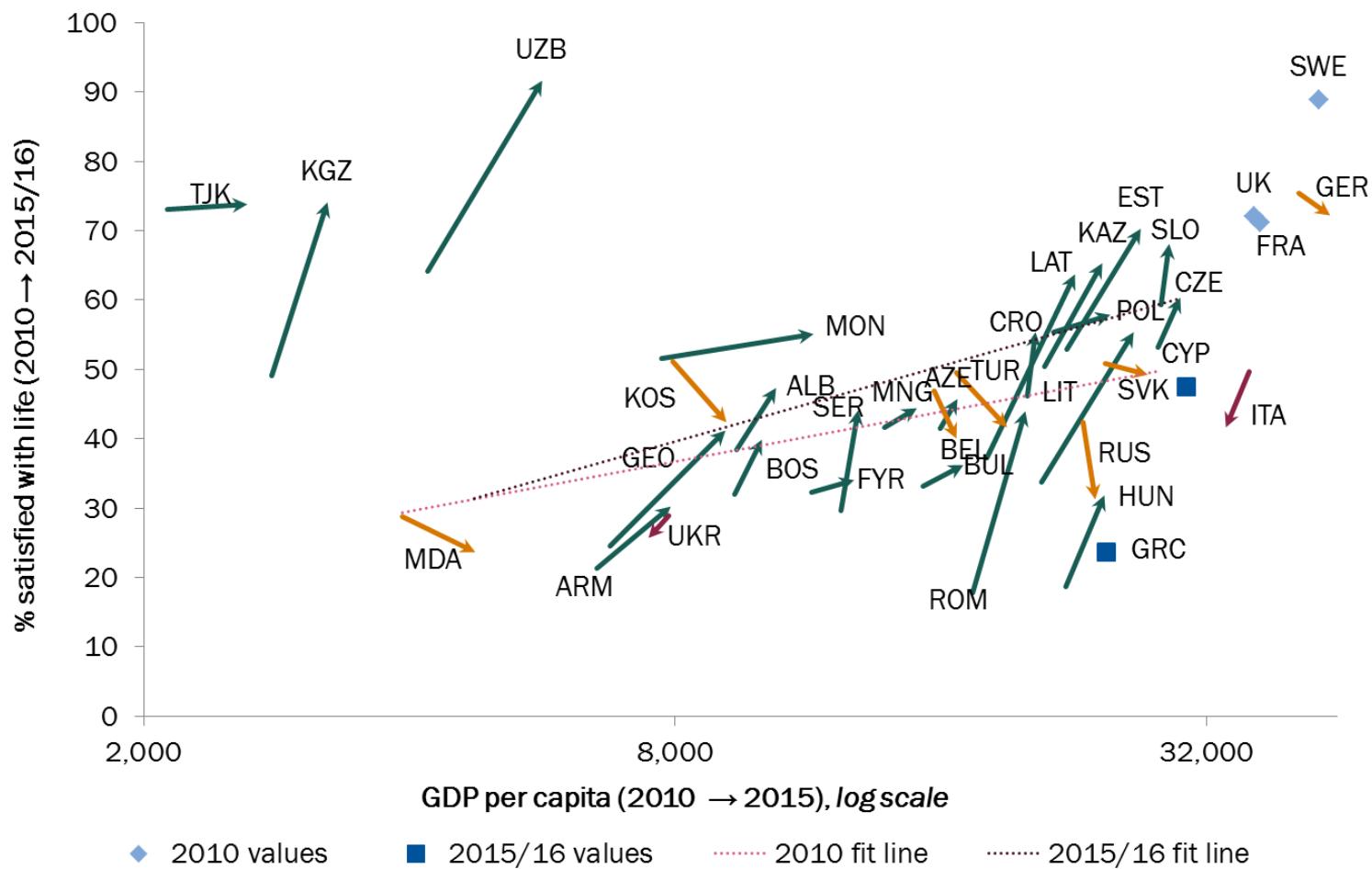
**1cm**

SHORTER THAN PEOPLE BORN BEFORE OR AFTER THAT PERIOD



**50%**  
OF RESPONDENTS LIVING IN POST-COMMUNIST COUNTRIES REPORTED BEING SATISFIED WITH THEIR LIVES, SIMILAR TO COMPARATOR COUNTRIES

# Satisfaction with life has been increasing in post-communist countries



Sources: IMF, World Bank, LiTS II, LiTS III and authors' calculations.

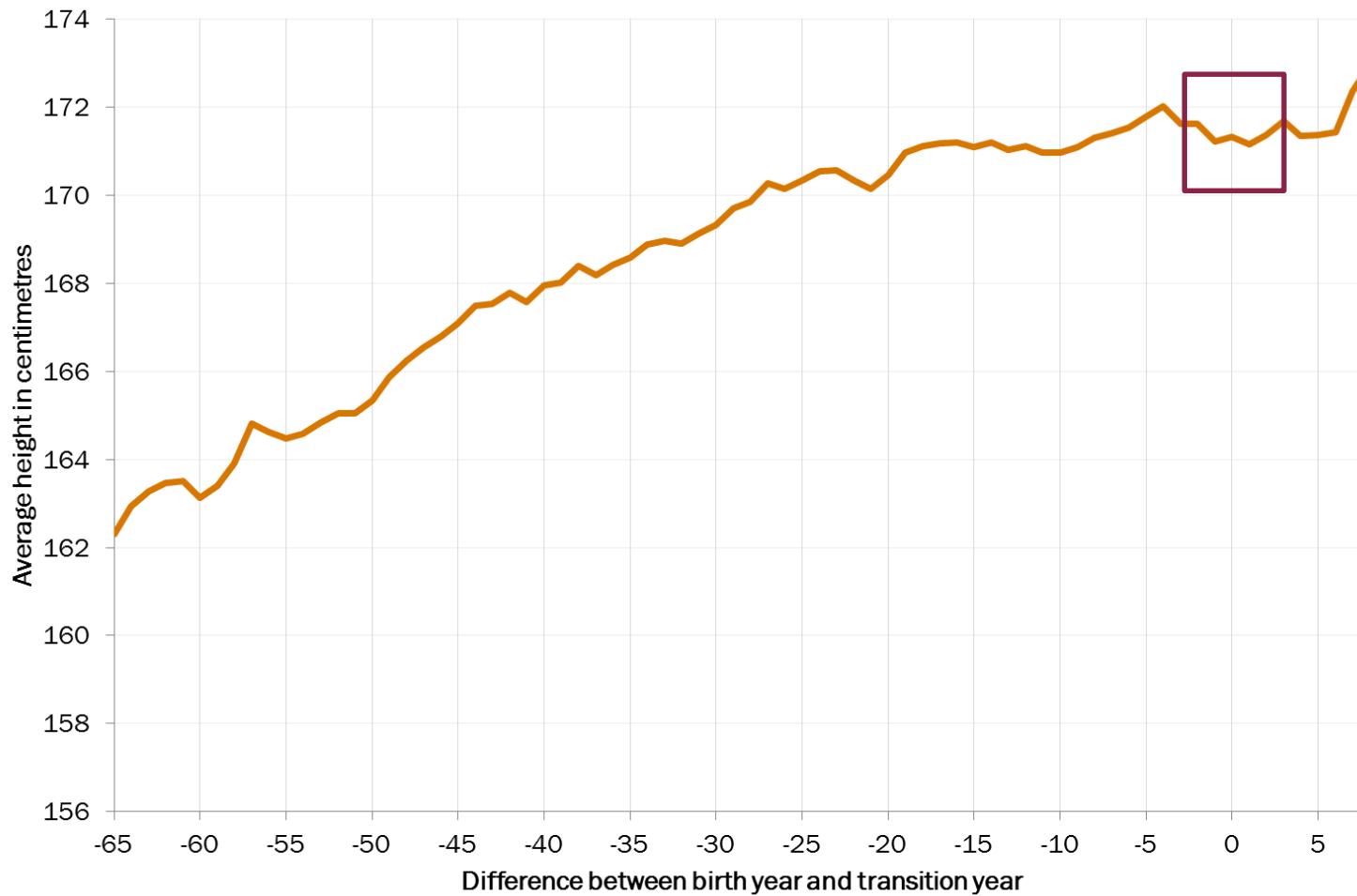
# So much that the happiness gap seems to have closed

	Satisfied with life (0/1)						
	(1)	(2)	(3)	(4)	(5)	(6)	(7)
Post-communist country	-0.038 (0.108)	0.012 (0.108)	-0.004 (0.093)	0.008 (0.105)	-0.009 (0.093)	0.065 (0.057)	0.039 (0.057)
Income		0.041 *** (0.007)		0.040 *** (0.007)		0.041 *** (0.007)	
Can afford holidays and meat			0.198 *** (0.016)		0.188 *** (0.016)		0.190 *** (0.014)
Can afford unexpected expenses			0.128 *** (0.013)		0.121 *** (0.013)		0.117 *** (0.011)
Education	Yes	No	No	Yes	Yes	Yes	Yes
Other controls	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Comparator countries	Ger / Ita	Ger / Ita	Ger / Ita	Ger / Ita	Ger / Ita	All	All
No. of observations	44,551	14,715	44,551	14,715	44,551	15,956	48,963

Sources: LiTS III and authors' calculations.

Note: Comparator countries comprise Cyprus, Germany, Greece, Italy and Turkey.

# Height has been increasing in post-communist countries, except around transition



Sources: LiTS III and authors' calculations.

# Hardship was so severe that individuals born around the start of transition are 1 cm shorter

	Born in transition year	Born or one in transition year	Born in transition year	Born or one in transition year
Born in transition	-1.057*** (0.398)	-0.768*** (0.282)	-0.777* (0.409)	-0.544* (0.292)
Average of log GDP per capita			1.129*** (0.215)	1.190*** (0.221)
No. of observations	42,853	42,853	40,854	40,887
R <sup>2</sup>	0.382	0.382	0.384	0.384

The fall in GDP alone does not explain the decrease in height.

Sources: LiTS III, Correlates of War Data, EBRD, Gapminder, UCDP/PRI Armed Conflict Dataset, and authors' calculations

Note: Taking into account for gender, urban/rural, parental education, religion, incidence of war when born, country-specific linear time trends and country fixed effects; also GDP and parental education (in columns 3 & 4).

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# Results confirmed when using measures of speed of market reforms

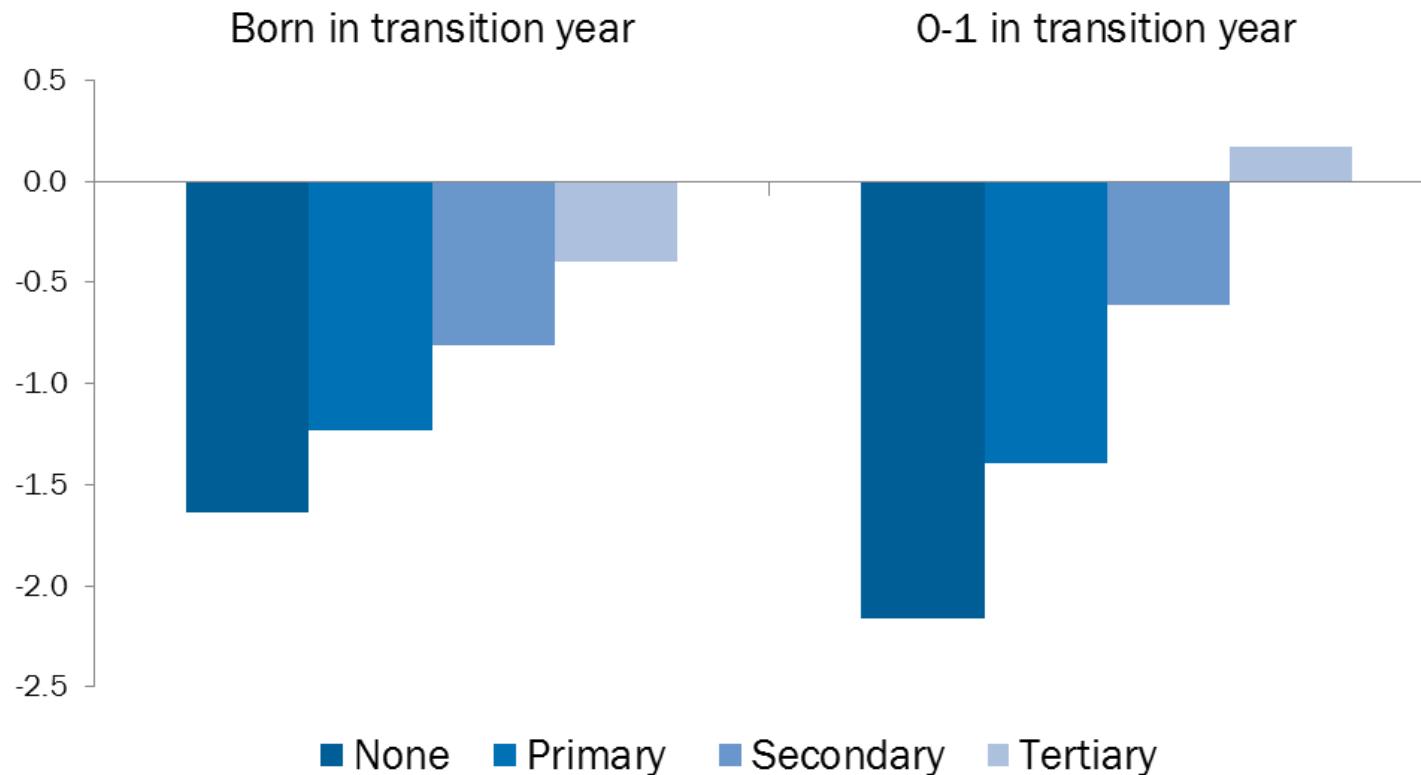
	Born in transition year	Born or one in transition year	Born in transition year	Born or one in transition year
Change in price liberalisation	-0.565 *** (0.194)	-0.343 *** (0.114)	-0.466 ** (0.204)	-0.274 ** (0.119)
Average of log GDP per capita			1.267 *** (0.229)	1.323 *** (0.233)
No. of observations	36,507	36,507	34,660	34,693
R <sup>2</sup>	0.373	0.373	0.375	0.375

Sources: LiTS III, Correlates of War Data, EBRD transition indicators, Gapminder, UCDP/PRI0 Armed Conflict Dataset, and authors' calculations

Note: Looking at changes in transition indicator of price liberalization.

# People from less-educated households affected most severely

Effect of transition on height, cm, by mother's level of education



Sources: LiTS III, Correlates of War Data, EBRD transition indicators, Gapminder, UCDP/PRIOR Armed Conflict Dataset, and authors' calculations

# The effect can also be seen using Russian Longitudinal Monitoring Survey

	Adults (cm)		Children (age z-scores)		Children, within-family (age z-scores)	
	(1)	(2)	(3)	(4)	(5)	(6)
	Born in transition year	Born or one in transition year	Born in transition year	Born or one in transition year	Born in transition year	Born or one in transition year
Born in transition	-1.392 *** (0.382)	-1.514 *** (0.286)	-0.216 ** (0.100)	-0.221 *** (0.080)	-0.545 ** (0.257)	-0.449 ** (0.191)
Implied change in adult height - girls (cm)			-1.47	-1.50	-3.71	-3.05
Implied change in adult height - boys (cm)			-1.56	-1.59	-3.92	-3.23
No. of observations	39,736	39,736	10,552	10,552	3,106	3,106
R <sup>2</sup>	0.514	0.514	0.154	0.155	0.571	0.571

Sources: : RLMS, EBRD transition indicators and authors' calculations.

Note: Z-scores represent the deviation from the mean as a multiple of standard deviation within each age cohort. Taking into account respondent's characteristics, linear trends and region fixed effects; mother's education and height (3 & 4), family fixed effects (5 & 6).

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# **Yet cohorts born at the start of transition are more satisfied with life than their peers**

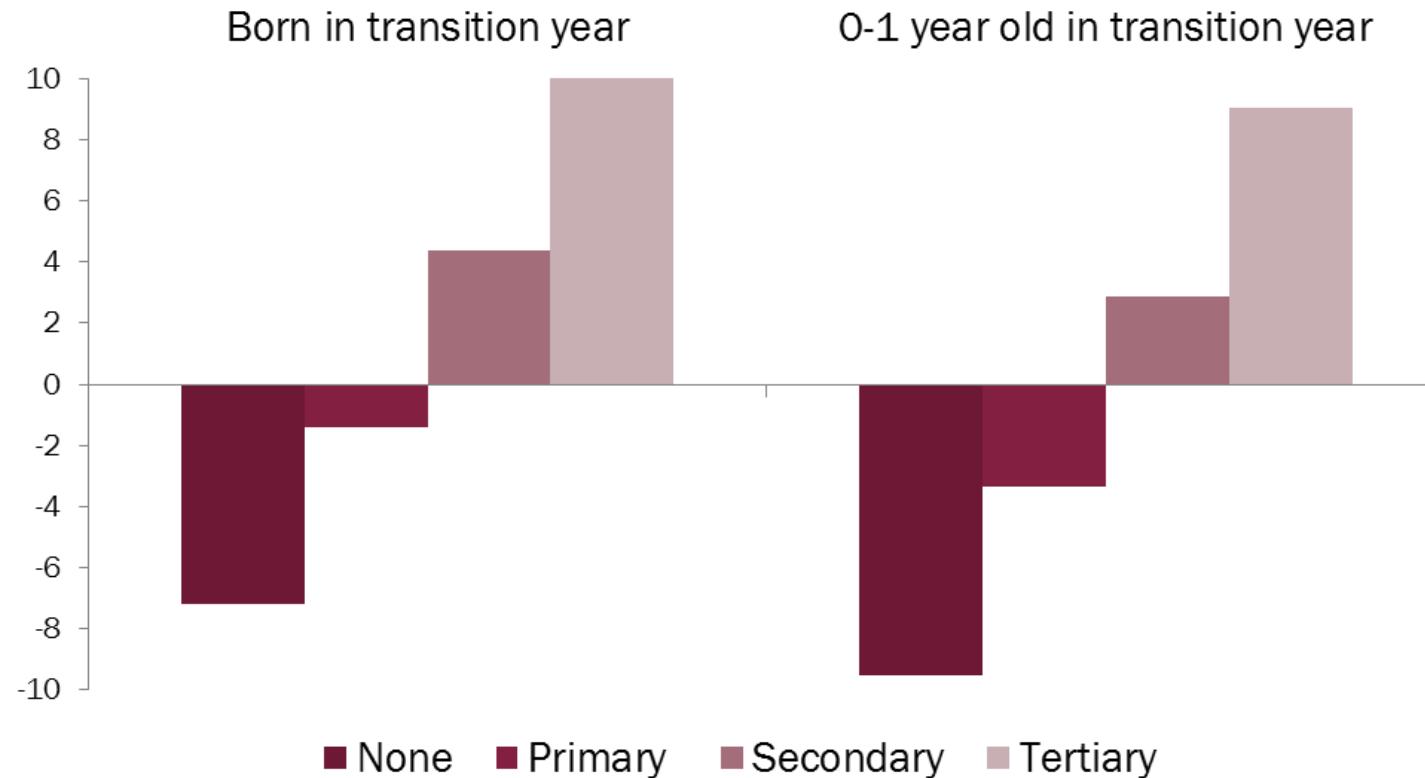
	Satisfied with life (0/1)	Satisfaction with life (1/5)	
	Born in transition year	Born or one in transition year	Born in transition year
Born in transition	0.141* (0.079)	0.104* (0.056)	0.148*** (0.057)
No. of observations	47,059	47,059	47,059

Sources: LiTS III, Correlates of War Data, EBRD transition indicators, UCDP/PRIOR Armed Conflict Dataset, and authors' calculations.

Note: Specifications control for country fixed effects and birth year effects. Additional controls include: gender, born in urban or rural location, respondent's religion, parents' level of education and incidence of war.

# Except for those from less-educated households

Effect of transition on life satisfaction, percentage points, by mother's level of education



Sources: LiTS III, Correlates of War Data, EBRD transition indicators, Gapminder, UCDP/PRIO Armed Conflict Dataset, and authors' calculations.

# Those who saw transition during their formative years are more likely to support democracy/markets

	Satisfied with life (0/1)	Preference for a market economy	Preference for democracy	Preference for redistribution	Trust
Experience of transition in formative years	-0.019 (0.014)	0.026* (0.014)	0.026* (0.014)	0.04 (0.084)	0.039 (0.029)
No. of observations	42,489	37,927	39,280	41,676	41,599

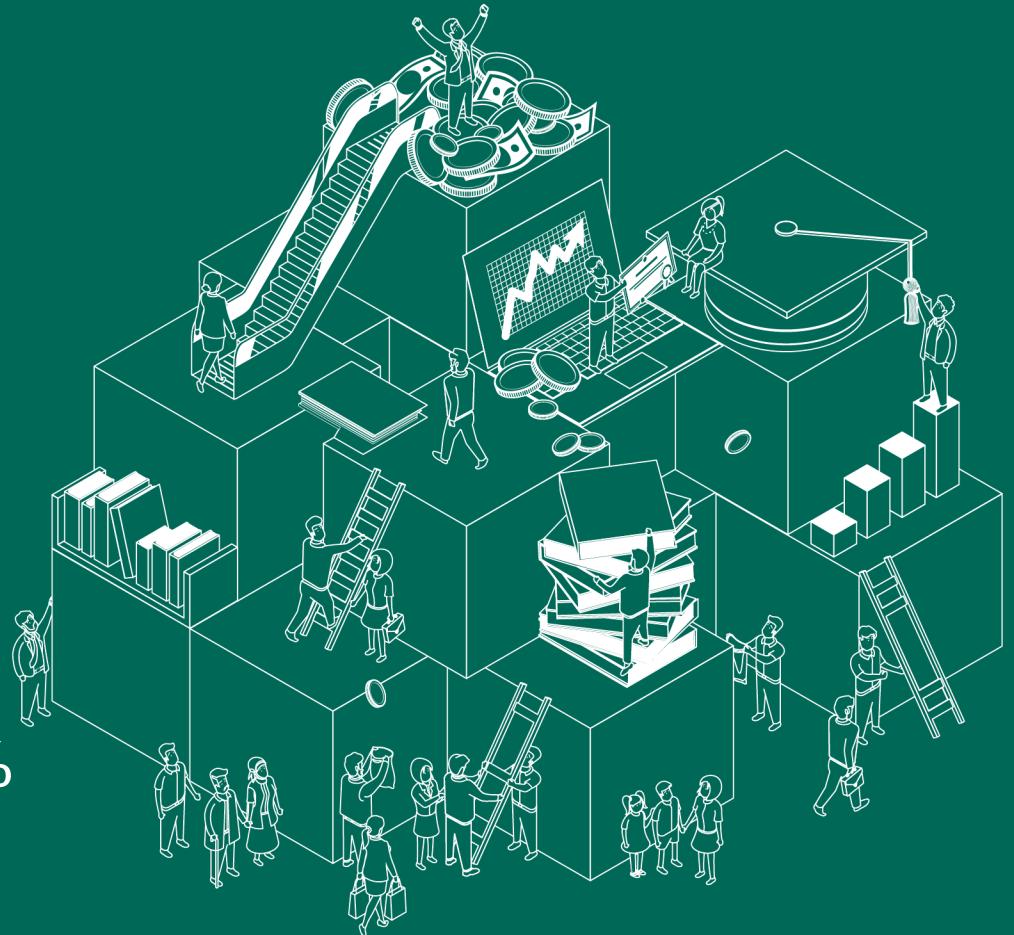
Sources: LiTS III, Correlates of War Data, EBRD transition indicators, UCDP/PRI Armed Conflict Dataset, and authors' calculations.

Note: Specifications control for country fixed effects and birth year effects. Additional controls include: gender, born in urban or rural location, respondent's religion, parents' level of education and incidence of war.

# INEQUALITY OF OPPORTUNITY

**31%**  
AVERAGE EARNINGS  
PREMIUM FOR PEOPLE IN  
THE REGION WITH  
UNIVERSITY DEGREES

AROUND  
**20-50%**  
OF INCOME INEQUALITY IS DUE TO  
CIRCUMSTANCES AT BIRTH IN  
MANY EBRD COUNTRIES



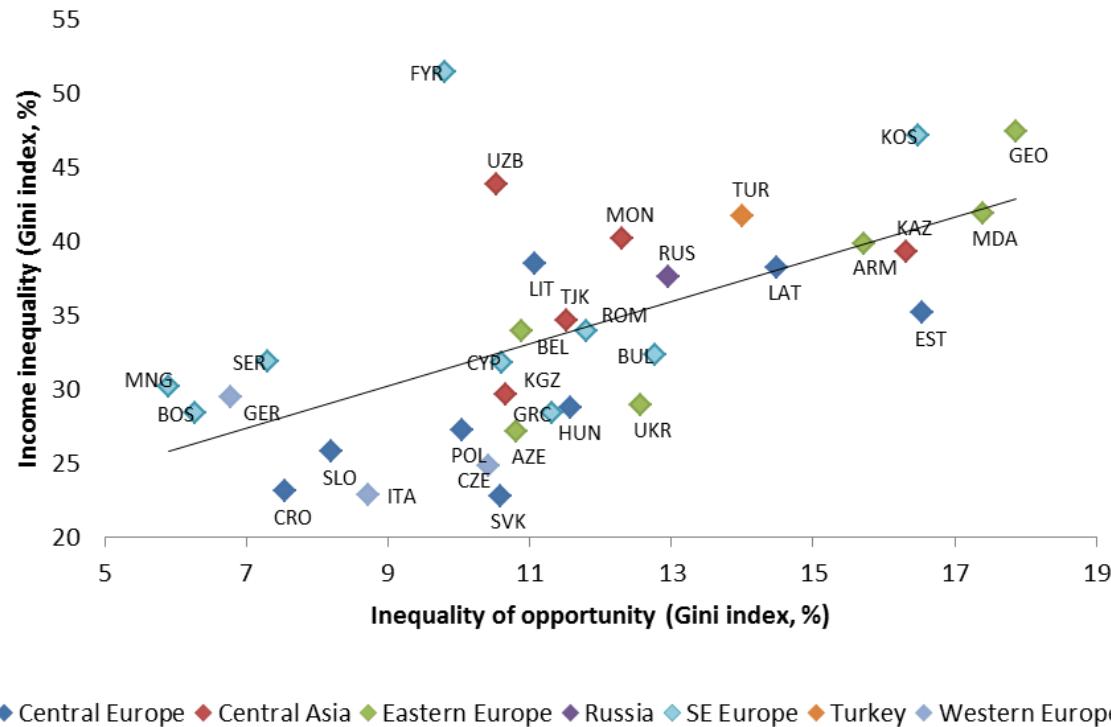
## Opportunity to have education, good job, income should not be limited by circumstances

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- In practice, gender, race, place of birth, and / or parental background have an impact
- Inefficient: prevents people from making the best use of their skills or from realising their entrepreneurial ideas
- Unfair: may lead to the loss of confidence in the key economic and political institutions that underpin societies and a market-based economic system

# 20% to 50% of income inequality in the EBRD region is due to circumstances at birth

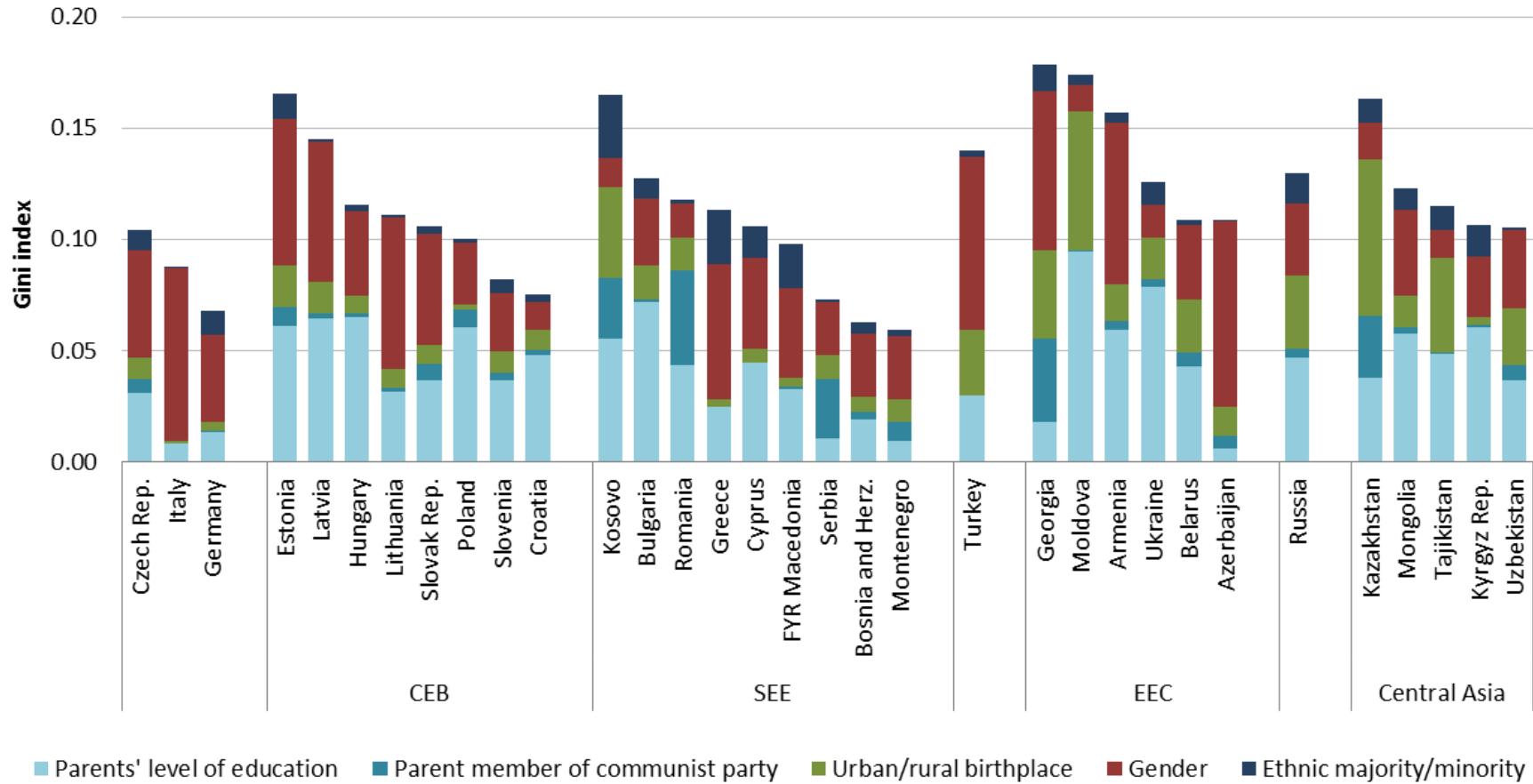
- Higher than in western Europe but modest compared with other emerging markets and the US



◆ Central Europe ◆ Central Asia ◆ Eastern Europe ◆ Russia ◆ SE Europe ◆ Turkey ◆ Western Europe

Sources: LiTS III and authors' calculations.

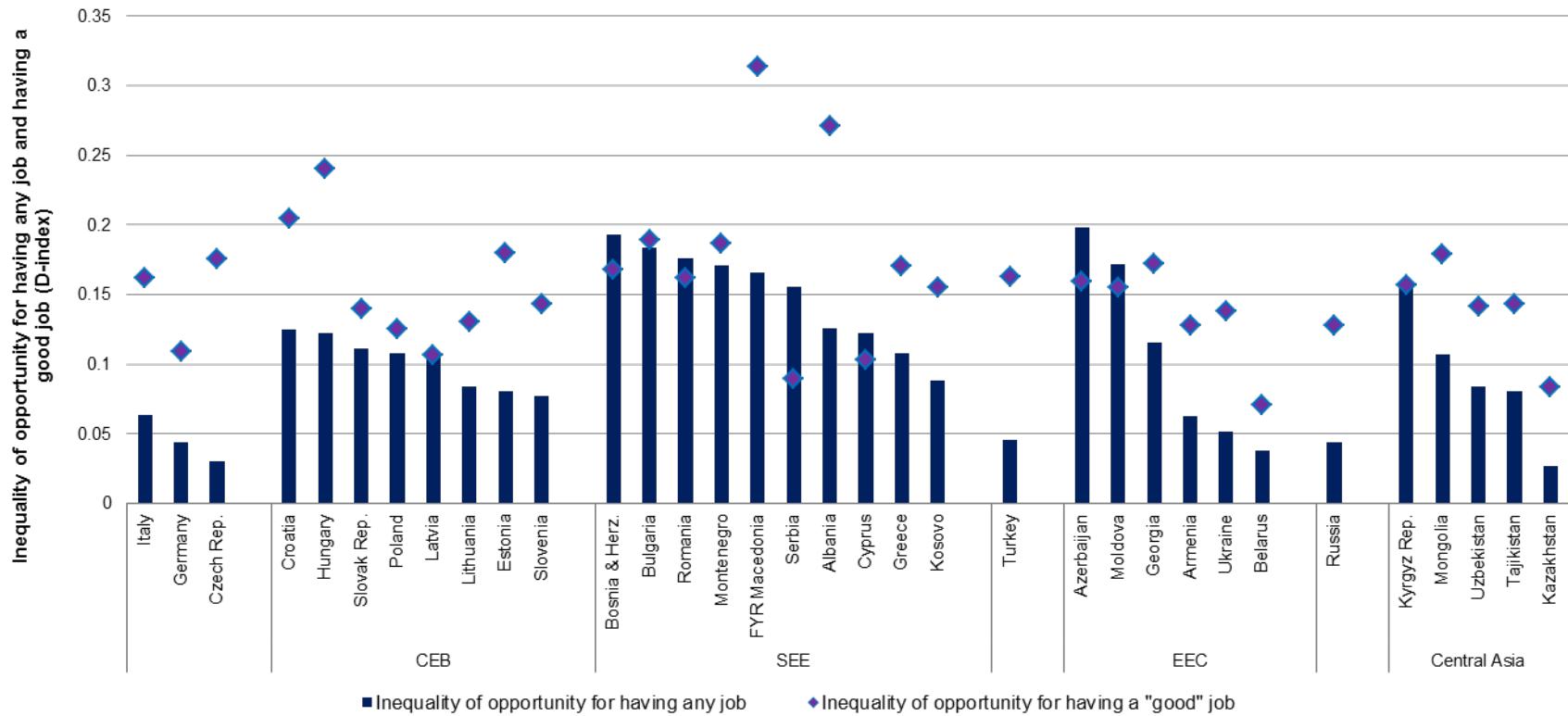
# Parental background is key factor behind inequality of opportunity, followed by gender



Sources: LiTS III and authors' calculations.

# Inequality of opportunity for having a good job is 50% higher than for any job

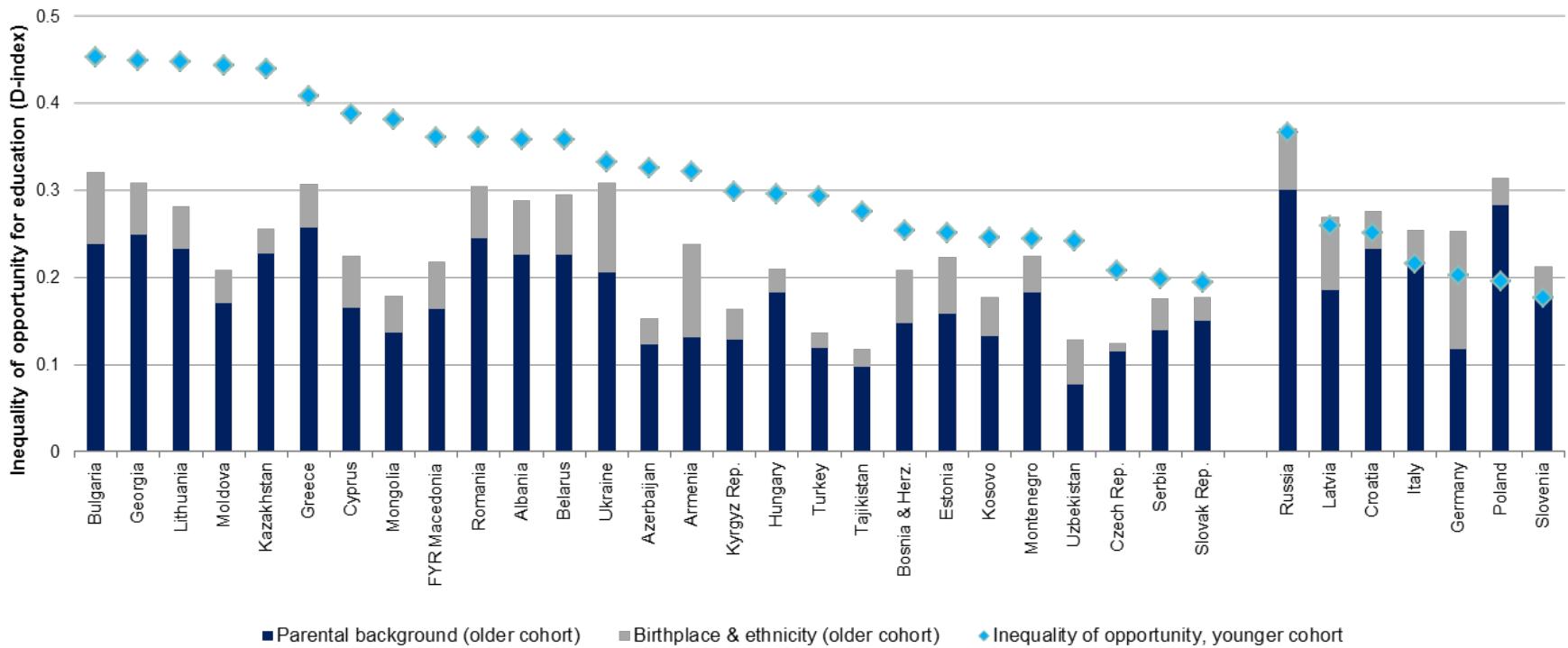
- Good job is one with financial security (contract + ability to cover unexpected expenses)
- Parental background is still the main determinant of job success



Sources: *Forbes*, authors' calculations

# Inequality of opportunity for tertiary education is higher for younger cohort

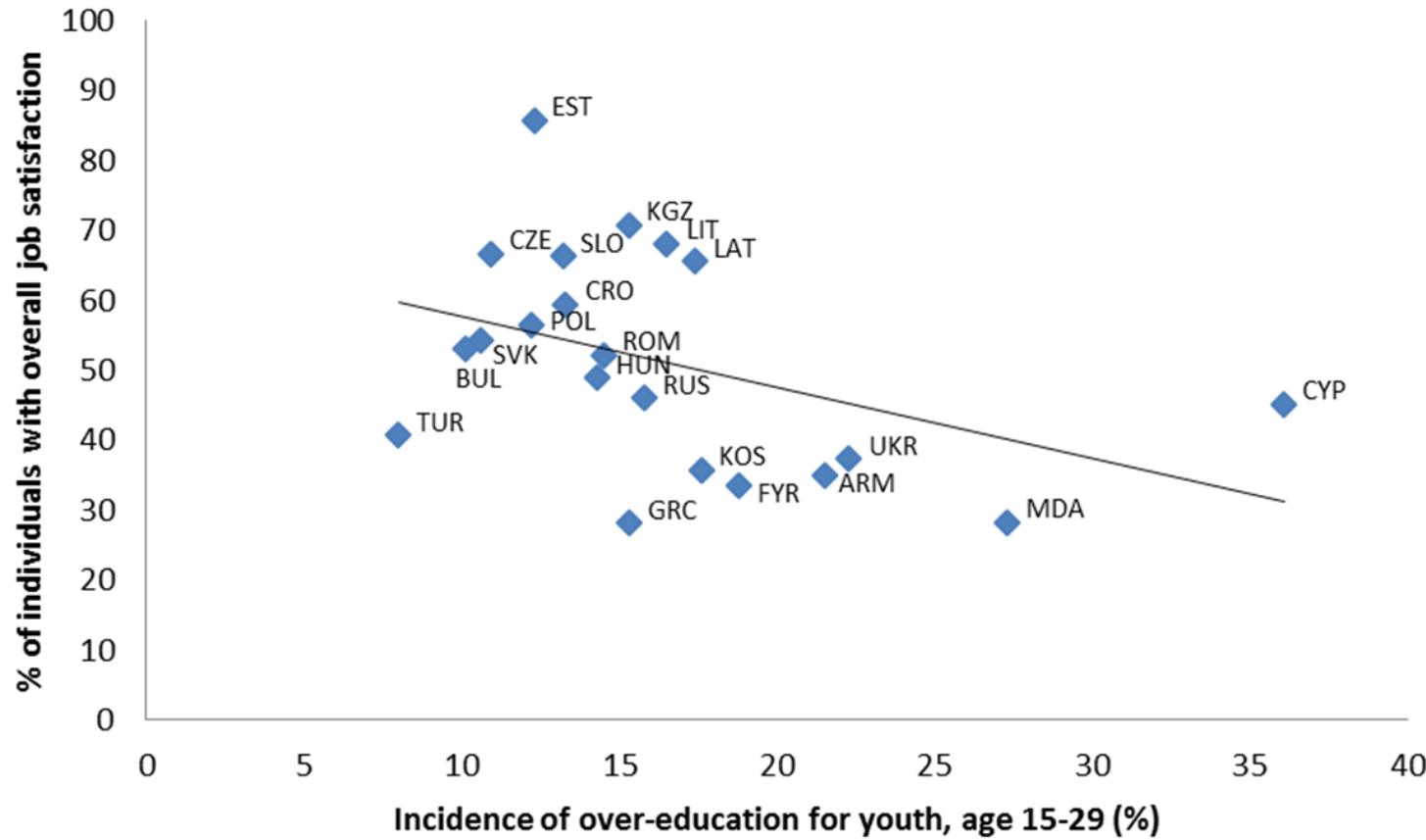
- People with a tertiary degree earn an extra 31% on average
- Parental background matters – more so for those who started school after 1989



Sources: *Forbes*, authors' calculations

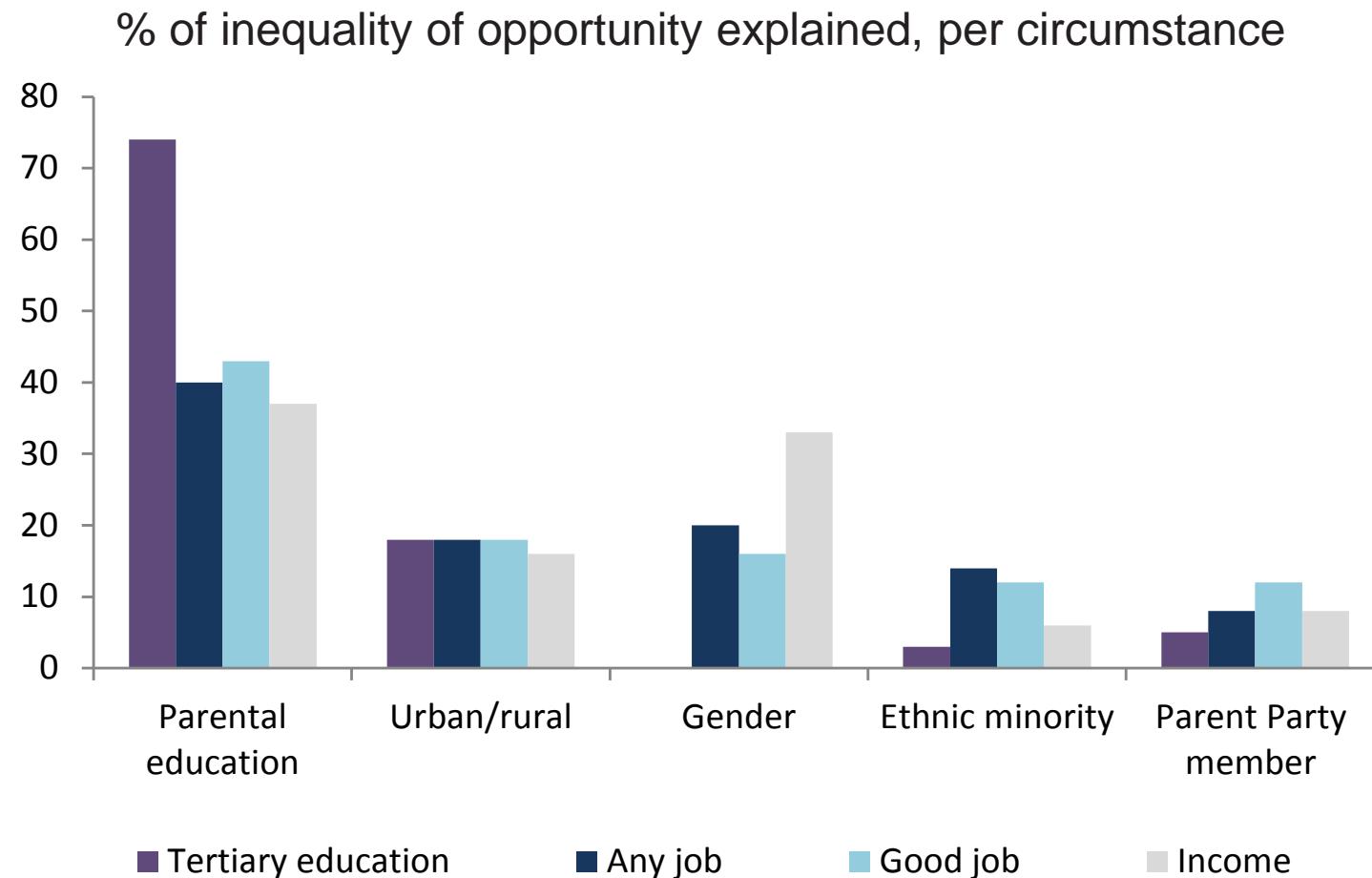
# Important to match education to market demand and address skills mismatch

- Over-education relative to available jobs negatively affects job satisfaction



Sources: *Forbes*, authors' calculations

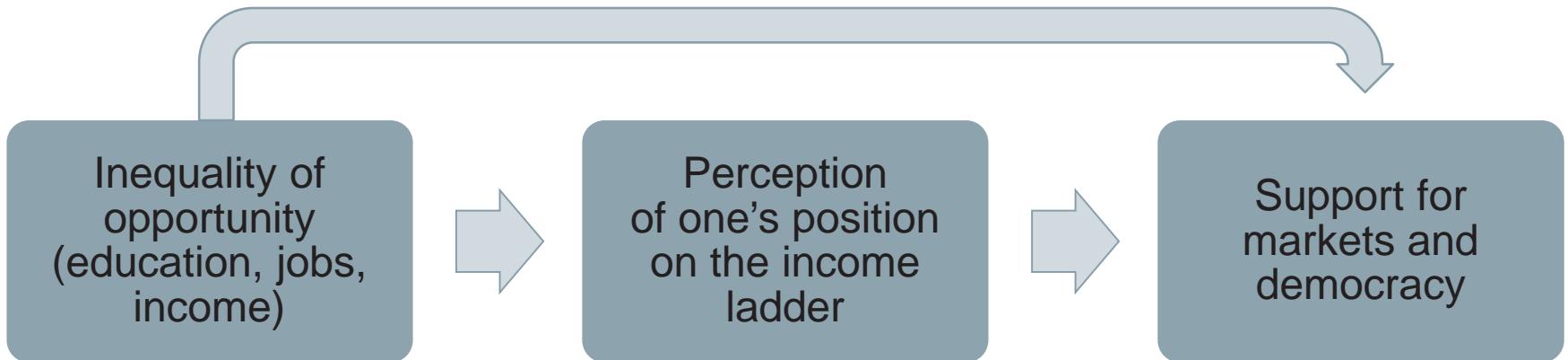
# Place of birth and ethnicity also play a role, albeit a smaller one



Sources: *Forbes*, authors' calculations

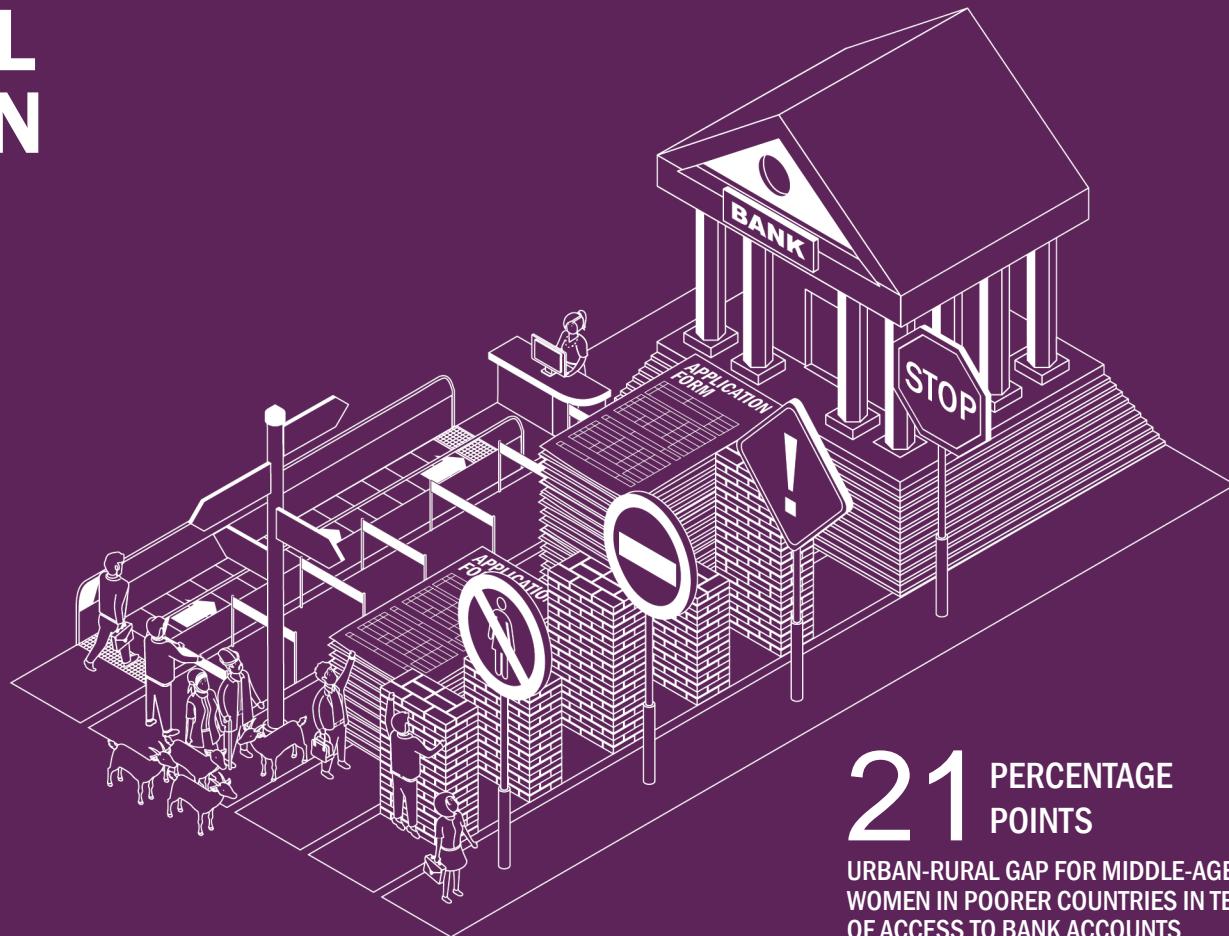
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# Inequality of opportunity has direct and indirect impact on support for markets and democracy



- Strong evidence that inequality of opportunity rather than income inequality matters

# FINANCIAL INCLUSION



ONLY

**18%**

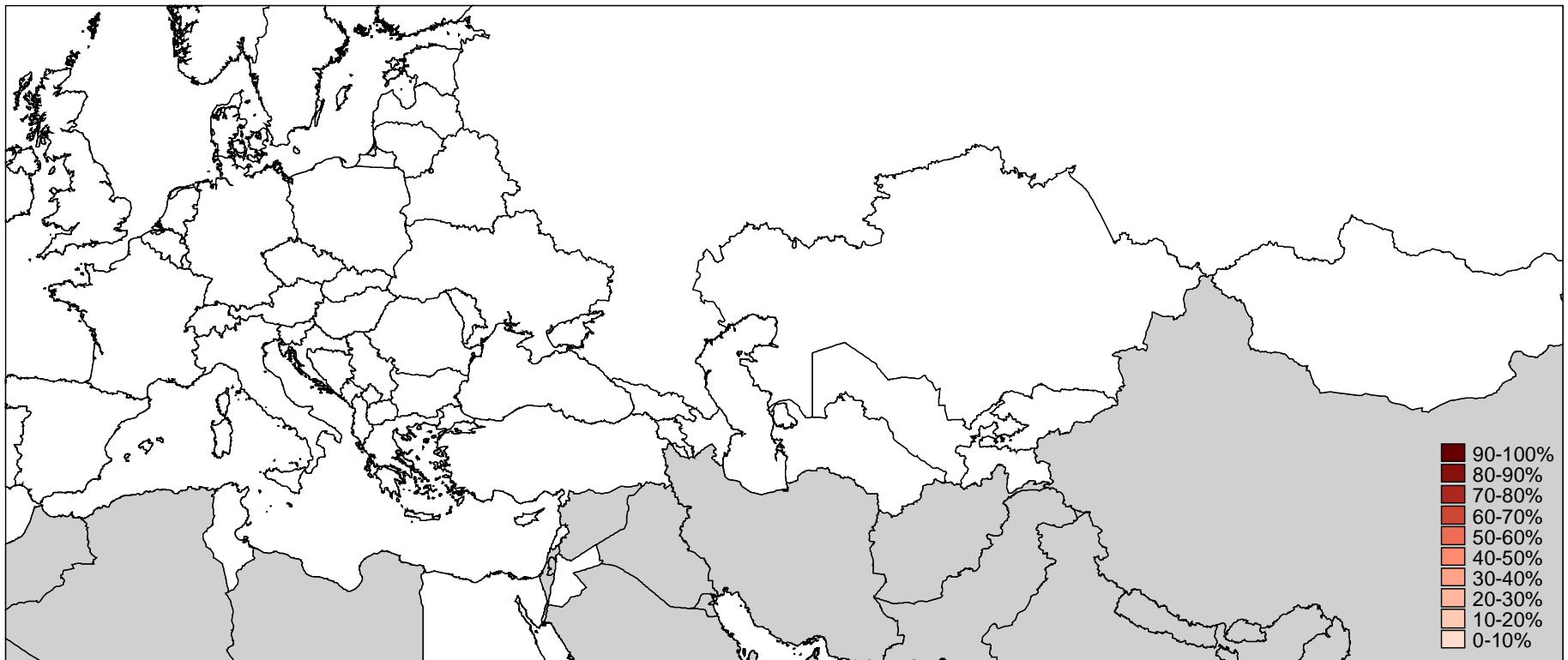
OF YOUNG PEOPLE IN THE SEMED REGION OWN AN ACCOUNT, WHICH IS LESS THAN HALF OF THE EQUIVALENT FIGURES FOR MIDDLE-AGED AND ELDERLY PEOPLE

**21** PERCENTAGE POINTS

URBAN-RURAL GAP FOR MIDDLE-AGED WOMEN IN POORER COUNTRIES IN TERMS OF ACCESS TO BANK ACCOUNTS

# Significant differences in terms of access to bank accounts

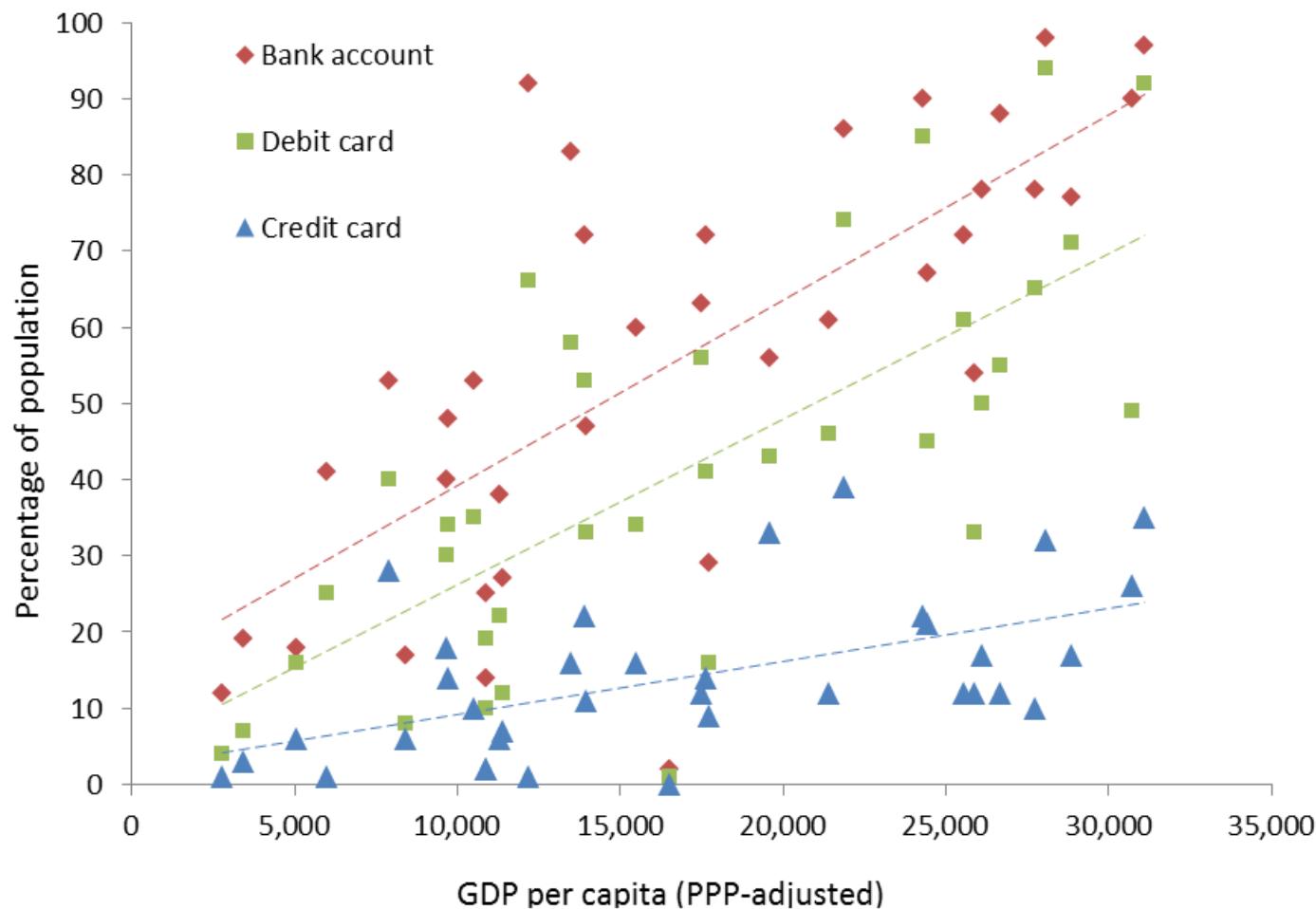
Bank account ownership



Sources: Findex database (2014).

Note: Percentage of respondents who own a bank account. Darker colours indicate higher bank-account ownership.

# Access to financial products improves as income grows

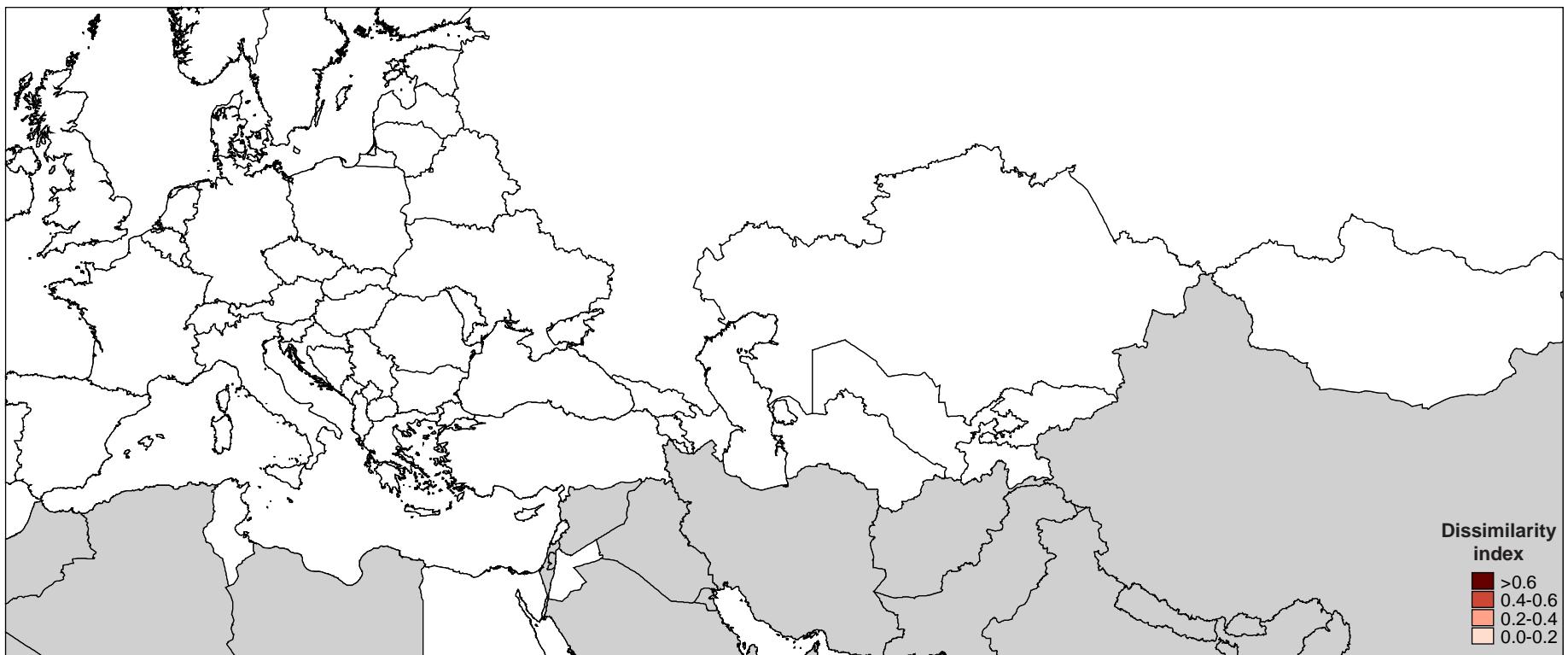


Sources: Findex database (2014), World Bank WDI (2015), and authors' calculations.

Note: Individual dots correspond to EBRD countries of operations.

# Inequality in terms of access to bank accounts is higher in SEMED, EEC, CA

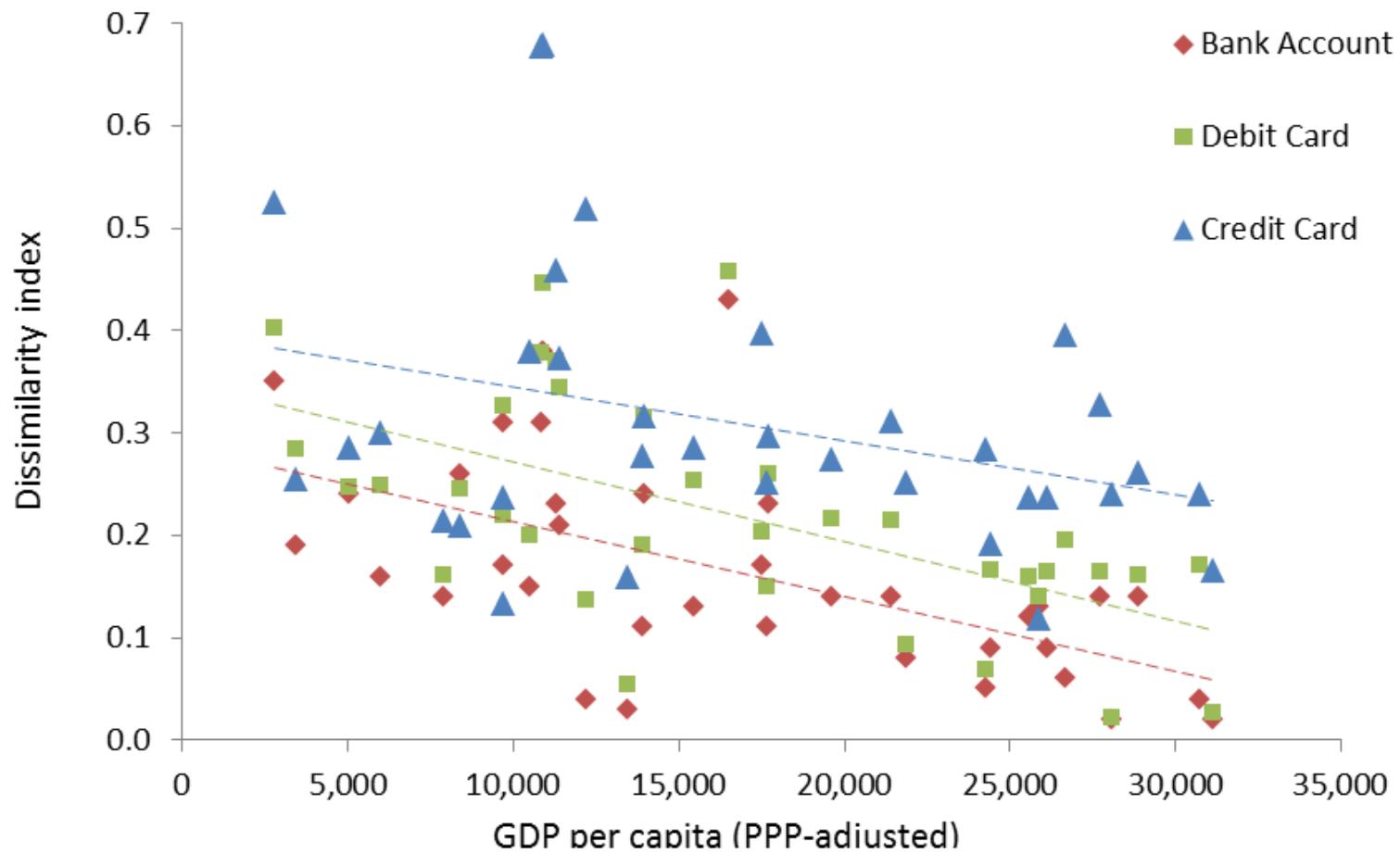
- Depending on income, education, gender and age



Sources: Findex database (2014) and authors' calculations.

Note: Dissimilarity index (on the 0-1 scale) measures the difference between the predicted probability of access based on individuals' characteristics and the average for the country. Darker colours = more unequal.

# Access to finance tends to be less unequal in more developed countries

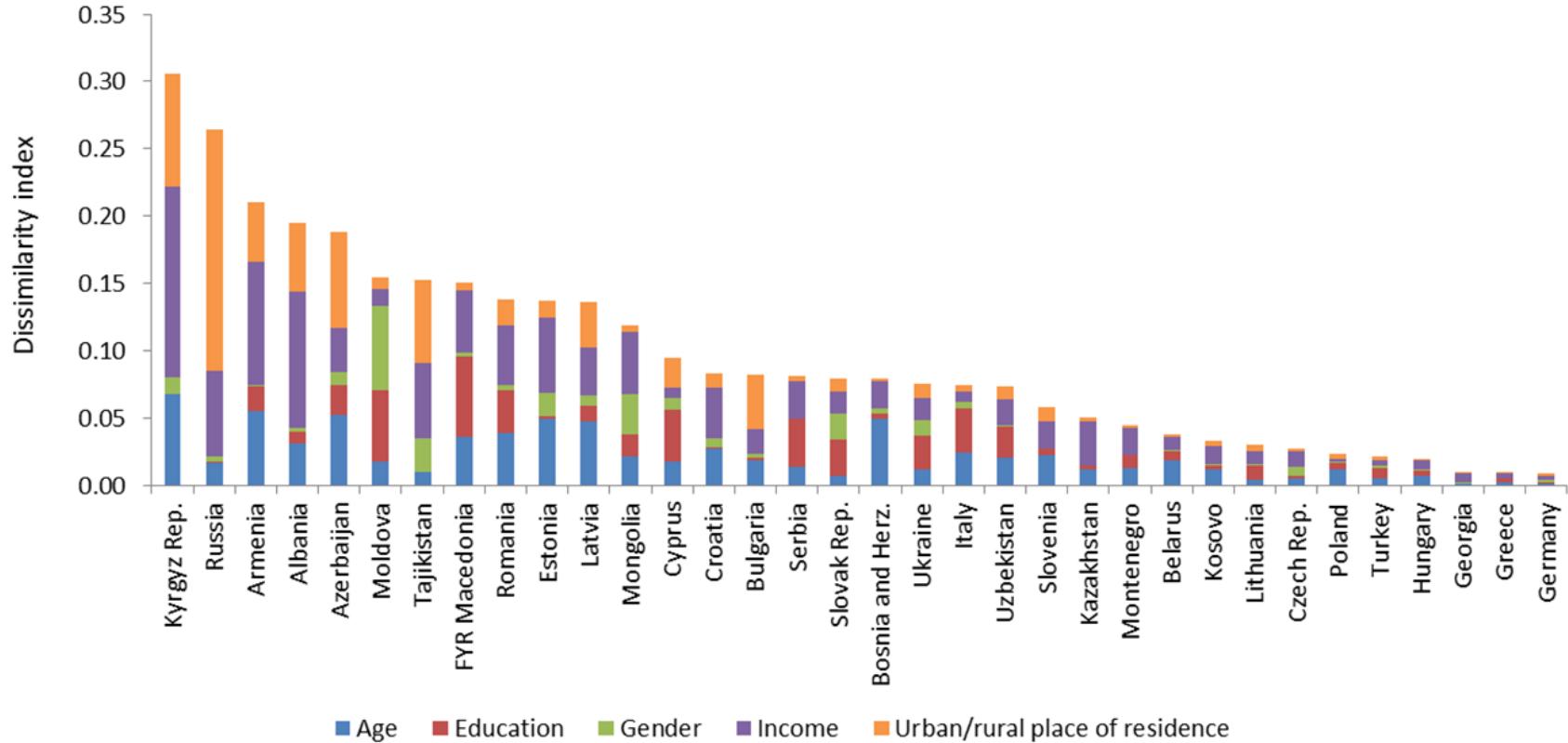


Sources: Findex database (2014), World Bank WDI (2015), and authors' calculations.

Note: Based on dissimilarity index (on the 0-1 scale) measuring the difference between the predicted probability of access based on individuals' characteristics and the average for the country. Individual dots correspond to EBRD countries of operation.

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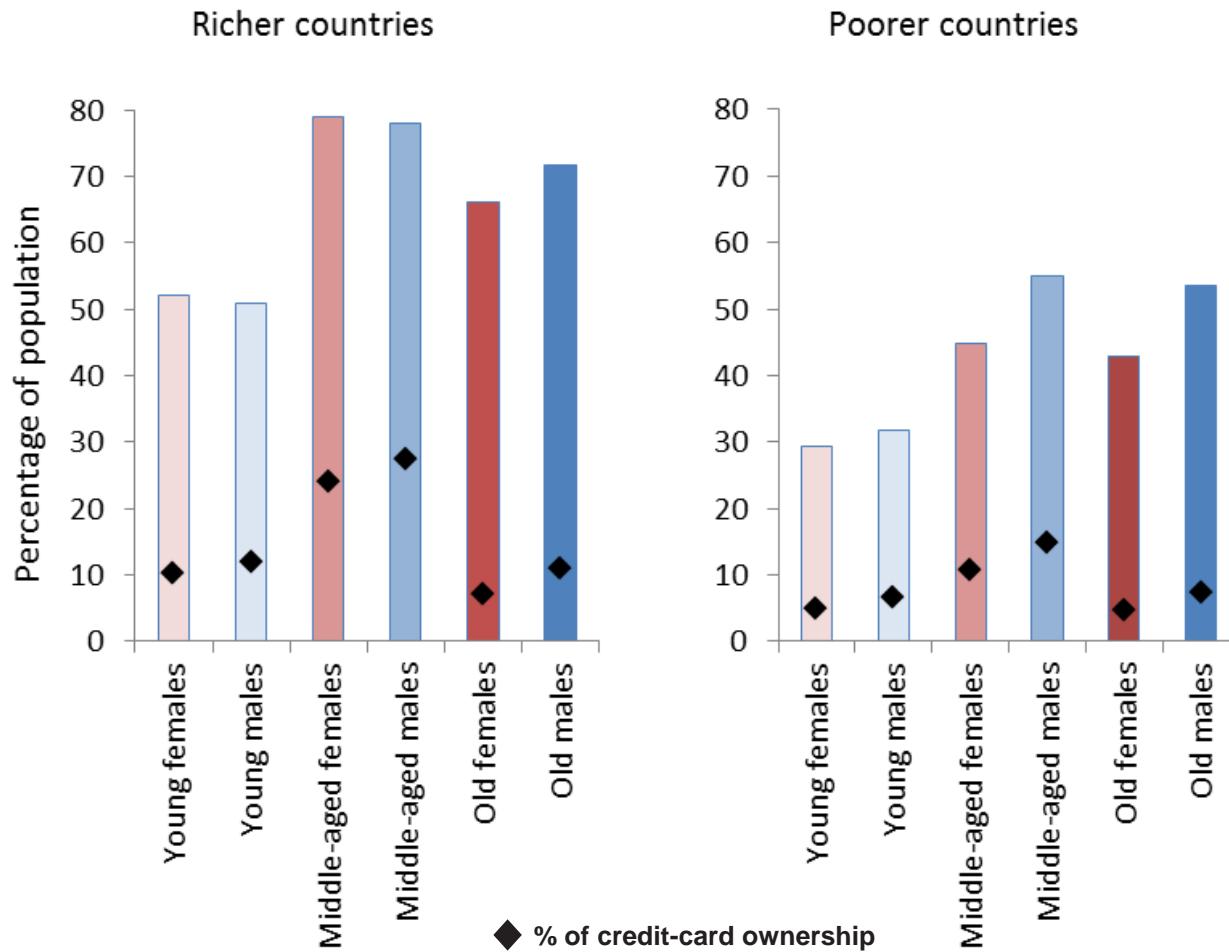
# Urban-rural divide, gender differences in terms of access to bank accounts



Sources: LiTS III and authors' calculations.

Note: Shapley decomposition based on dissimilarity index [0; 1].

# Larger age and gender differentials in access to accounts in poorer countries



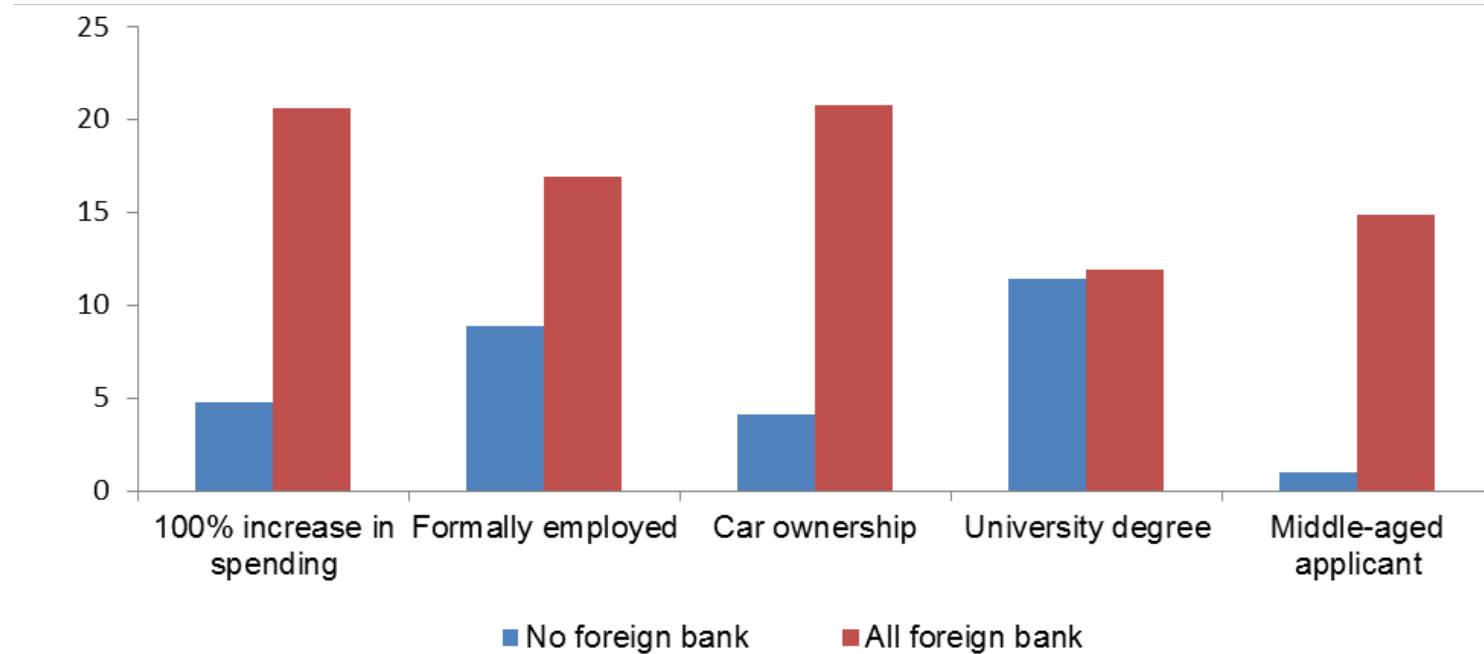
Sources: Findex database (2014) and authors' calculations.

Note: Young: <25 years; middle-aged: 25-64 years; old 65+ years.

# Foreign banks improve access to finance, but gains are uneven, accrue to less economically vulnerable

Those with higher spending are significantly more likely to have a bank account if they live in a location with all foreign banks – compared with an all-domestic-bank location

Impact of household characteristics on probability of owning a bank account, % points



Sources: LiTS III and authors' calculations.

Note: Impact for hypothetical localities, based on instrumental variable regressions. Spending comprises outlays on consumption goods, utilities and transportation services (proxy for wealth).

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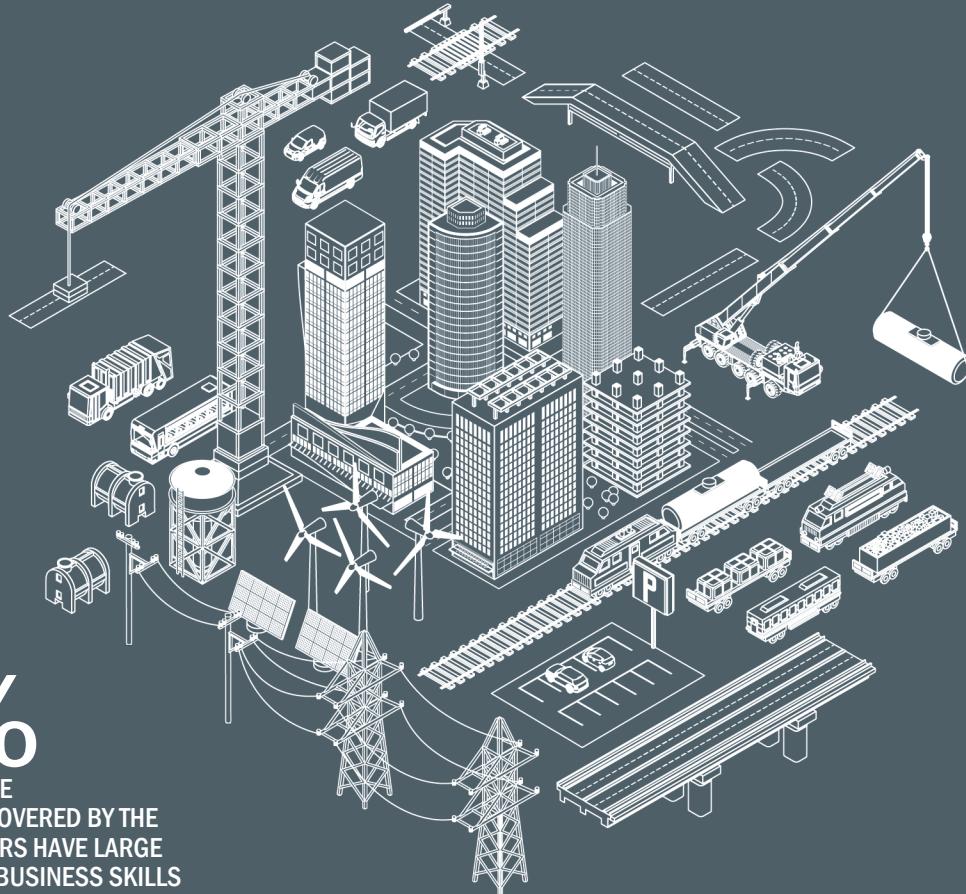
# STRUCTURAL REFORM

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COUNTRIES IN THE EBRD REGION ARE MEMBERS OF THE WTO, WITH KAZAKHSTAN THE LATEST TO JOIN IN NOVEMBER 2015

42%

OF COUNTRIES IN THE REGION THAT ARE COVERED BY THE NEW SME INDICATORS HAVE LARGE GAPS IN TERMS OF BUSINESS SKILLS AND STANDARDS



# Reform reversals are increasingly common – although the balance of reforms remains positive



Sources: EBRD transition indicators.

Note: Normalised by the number of countries.

## Transition for all?

- Transition was a traumatic experience – so much so that people born during price liberalisation years are on average 1 cm shorter
- It took a long time – but the happiness gap has now closed
- And income convergence has been impressive – but not everyone benefited
- In fact, rise in inequality from (notionally) low levels meant that only 44% personally experienced income convergence
- Redistribution may help but a greater emphasis on improving equality of opportunity – through education, financial inclusion and better connectivity – is even more imperative

# TRANSITION REPORT 2016-17



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**Video TR 2016-17**



**EASILY  
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