TITLE: FAMILY SAFETY NETS AND ECONOMIC TRANSITION IN EASTERN EUROPE: Summary of Findings from a Study of Inter-Household Transfers in Russia

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FAMILY SAFETY NETS AND ECONOMIC TRANSITION IN EASTERN EUROPE:
Summary of Findings from a Study of Inter-household Transfers in Russia

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Executive Summary

The social safety net is a crucial component for successful economic transition in Russia, and most discussions of income redistribution and social insurance focus on the public sector. We call attention to another component of the safety net, private inter-household transfers, using the Russia Longitudinal Monitoring Survey. We find that private transfers of cash and goods in Russia are quite large and widespread, and that such transfers help equalize the distribution of income and prevent poverty. In addition to flowing from upper to lower income households, private transfers tend to flow from old to young. Private transfers are responsive to the socioeconomic characteristics of households such as employment status, education, age, female headship, marital status and number of children.

We used an econometric model to simulate the response of private transfers to economic fluctuations. Such transfers could mitigate substantially the shortfall in income from unemployment, though only one out of ten affected households would be expected to receive such aid. Private transfers also interact with policy. For example, we find that the effects of a reduction in public pension income would be cushioned somewhat by increases in private transfers.

The private safety net weakened with the onset of the economic hardships of 1993. Though participation in private networks attenuated only somewhat, private transfer amounts, as a fraction of total income, fell by over a third.
Consider the case of a Russian family whose primary earner has just been laid off from a discontinued state enterprise. Do families like these have more fortunate relatives or friends who can assist them with cash or in-kind gifts? And would an expansion of the public safety net tend to displace these private family safety nets?

Answering these questions is likely crucial for evaluating the potential for successful economic transition in the Eastern bloc. Economic dislocation from closing unprofitable firms threatens popular support for a quick transition. Rising unemployment and widening of the distribution of income are likely to increase the clamor for protectionist policies antithetical to economic reform. These dangers have prompted some to advocate publicly provided social insurance aimed at reducing both transitory and permanent poverty created by the transition to capitalism. But governments, despite being hard-pressed to increase social spending, are currently forced to re-direct some cash transfers and to reduce certain of the in-kind benefits.

However, public transfers are not the only means of shifting resources from one group to another. Family networks are an alternative to governments as a means of income redistribution. Knowing the size of the informal, private safety net is critical because these private transfers determine the necessary scope of public assistance to the poor once private mechanisms have been exhausted. A system of informal, inter-family networks is an important institution for poverty alleviation in many countries. The requisite scope for public transfers cannot be determined until we have information about the size of the informal private network.
Despite the potential importance of family networks during Russia's transition, we currently know little about how these networks might function. Economists have just started to analyze household survey micro-data containing information about private transfers for the former Soviet Union and Eastern European countries. The recent availability of new household survey microdata for Russia makes possible the exploration of the behavior of family networks there.

We find that private transfers in Russia are large, widespread and responsive to socio-economic characteristics of households. Patterns for private transfers tend to mimic what would be achieved with means-tested public income redistribution; they are targeted to vulnerable households such as female-headed households with many children, younger households and those affected by unemployment. Private transfers also help alleviate poverty. Poverty rates among households participating in private-transfer networks are over 10 percentage points lower than those of households not participating in private transfers.

**Private and Public Transfers**

Private and public transfers can interact. To see why, suppose that one household (a "donor") is giving money to another household (a "recipient"). If the government now taxes the donor and gives the proceeds to the recipient, it helps to achieve what the donor was intending to do privately. With his or her burden eased by government redistribution, the donor may decide to give less. This cutting back of private transfers in response to public redistribution is called "crowding out."

If crowding out does occur, it could pose especially difficult targeting problems for policy makers. To see why, think about what happens when poor households who are
already receiving private transfers are targeted for a public subsidy. The subsidy eases the burden of private donors who afterwards contribute less to their relatives and friends. In essence then, the government subsidy indirectly benefits donors. Since donors are often from upper income brackets, some of the government subsidy, intended only for the poor, is diverted to undeserving households.

What does "crowding out" imply in the Russian context? One possible implication is that Russian private safety nets might already be negligible, rendered obsolete by socialism's extensive web of public transfers. But the legacy of socialism could well have created countervailing forces enhancing the viability of private transfer networks. The former Soviet Union's controls on wages and prices, for example, created a shortage economy that could have easily encouraged private trading networks. A history of such trading could create the bonds of altruism and trust likely needed for a system of private safety nets. A recent survey indicated that Russians were more willing to share expenses with friends than New Yorkers were.¹

Data

Our study used the Russian Longitudinal Monitoring Survey (RLMS), a representative survey with information for about 6,500 households. We used data from two rounds of the survey, for the summers of 1992 and 1993. The RLMS contains information about money and goods transferred between households and the determinants of these transfers. Respondents were asked to report the value of money and in-kind gifts received, as well as money that they gave or lent to other households. In addition to questions about private

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transfers, the respondent is asked to report on income received by him/herself and other individuals in the household, as well as employment status. The survey also contains questions dealing with the demographic composition of the household: the ages and education levels of individuals, the number and ages of children and the location of the household.

Evidence

We find that private transfers in Russia are both widespread and significant. We characterize households as net donors, or net recipients, according to whether outflows of private transfers exceed or fall short of inflows. Twenty percent of the households were net recipients and the same percentage were net givers. The figures are given below:

<table>
<thead>
<tr>
<th>Number</th>
<th>Percentage of Sample</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net Transfer Donors 1,157</td>
<td>19.37</td>
</tr>
<tr>
<td>Net Transfer Recipients 1,197</td>
<td>20.04</td>
</tr>
<tr>
<td>Net Transfer Equals Zero ('Others') 3,599</td>
<td>60.59</td>
</tr>
</tbody>
</table>

Private transfers account for a significant fraction of total household income. For the sample overall, gross transfer receipts comprise 6.9 percent of total household income. Among net recipients the figure is 30.7 percent. Further, donors give away 12.9 percent of their income.

Another indicator of the importance of private transfers is the boost in the poverty rate implied by subtracting them from total income. The headcount poverty rate for the sample of net recipients was 28.1 percent. Subtracting private transfers implies a poverty rate that is much higher—44.9 percent. The pre-private-transfer income for net recipients is
less than half that of net givers. So private transfers tend to flow from the "haves" to the "have-nots," at least when economic resources are measured by current income. But in other ways recipients and donors are similar. They both have higher college graduation rates than those not involved with transfers. Further, they both have poverty rates under 30 percent, in contrast to other households, who have a poverty rate of over 40 percent. Being involved in a private transfer network clearly helps prevent poverty.

Still, in most ways recipients appear much more vulnerable than donors. They are on average headed by younger people, and are more frequently headed by women and unemployed persons. Recipient households are on average larger and relatively fewer of them have a plot of land upon which to grow food. Private transfers tend to flow from old to young. Nearly 40 percent of households aged 30 or younger received transfers, while less than 10 percent of those in their 60's received.

We estimated a multivariate model of private transfers, modeling them as a function of household resources, such as pre-transfer income, education and employment status, demographic characteristics, such as age, marital status and gender of the household head. We also entered health status and regional indicators of unemployment and income into the model. We used the model to estimate how much assistance from private sources would be forthcoming in the event that a typical household head were to become unemployed. We found that, if the household were lucky enough to receive private assistance as a result of a job loss, that such assistance would fill over half of the gap created by the job loss.

However, we estimated that the chances of such assistance occurring were only about 1 in 10. So while potentially important, the private safety net does not cover all households.

We also considered old-age pensions in our model. Recall from the discussion above that public transfers such as old-age pensions could crowd out private transfers. The flip side of this argument is that, if such pensions were to be cut back, private transfer networks could step in to fill the gap. Our estimations imply that, if pensions were cut back, private transfers to older households would increase. The increase would fill almost 20 percent of the gap created by the cutback in pensions.

*Changes between 1992 and 1993*

The months between the summer and early fall of 1992 to the summer of 1993 were marked by worsening inflation, declining real wages and rising poverty and inequality. Though participation in private-transfer networks declined only slightly, transfer amounts fell more precipitously. For example, gross receipts, as a fraction of total income, fell by over a third. The falloff in private transfers is similar to that which occurred during Poland’s economic transition. Aside from the falloff in transfer amounts though, basic transfer patterns remained the same as before: transfers flowed from high- to low-income households, for example, and from old to young. But like in the case of Poland, as conditions got worse, family networks appeared to weaken. One possible explanation is that worsening conditions, and perhaps increased uncertainty, heighten a household’s concern for its own well-being relative to that of others.