



- *Aggregate economic indicators, such as GDP growth, do not reflect distributional inequalities.*
- *In Belarus, inequalities in distribution are mainly linked to intergenerational and spatial differences.*
- *Growing economic insecurity, affecting vulnerable households, calls for new approaches to the design and coverage of social assistance programs.*

Characteristics of Distributional Inequalities

Structural economic changes are generating four major distributional inequalities in Europe and Central Asia: (i) the intergenerational divide, or disparities between young and old; (ii) inequalities among workers engaged in different occupations, such as clerical workers and machine operators versus nurse's aides and private security guards; (iii) inequality in access to economic opportunities based on geographical location; and (iv) inequalities of opportunity based on gender, ethnicity, background or other characteristics rather than individual ability and effort. According to the World Bank report *'Towards a New Social Contract'*, published in September 2018, focusing on Europe and Central Asia (ECA), these inequalities can generate tensions that undermine social cohesion. They have implications for the stability of the 'social contract', or the shared principles used to regulate markets, define responsibilities and benefits, and redistribute outcome, based on equity and fairness preferences.

Of four tensions, lower intergenerational mobility and spatial divides have been observed in Belarus. According to the World Bank report *'Fair Progress? Economic Mobility across Generations Around the World'*, released in May 2018, relative mobility, the extent to which the education (or incomes) of children is independent of the education (or incomes) of their parents, while high in Belarus compared to the ECA average – has been declining over time. It is lower for the cohort of individuals born in the 1980s vis-à-vis those born in the 1940s. Meanwhile, absolute mobility, or the share of children with better educational outcomes than their parents' generation, has been lower for the 1970s and 1980s birth cohorts compared to earlier birth cohorts, and remains lower than absolute mobility in upper middle-income and high-income countries. While overall inequality in Belarus is low compared to other countries in the region, both World Bank reports find that youth in the region is losing ground relative to older generations. Similarly, *'The Life in Transition Survey of 2016'*, conducted by the European Bank for Reconstruction and Development in collaboration with the World Bank, shows that young Belarusians are pessimistic about their living standards compared with their parents', and about the likelihood of the next generation faring better than the current one.

While Belarus is not experiencing rising overall inequality, the economy is characterized by spatial disparities in welfare. Among 35 countries of Western, Eastern, and Southern Europe, Belarus has the seventh-highest spatial inequality as measured by the coefficient of variation of disposable income or consumption. Moreover, the gaps in mean consumption between urban and rural areas as well as between regions (*oblasts*) have widened in Belarus between 2003 and 2013. The average gap in household per capita consumption between the richest and the poorest region in Belarus is now close to two-thirds of the country's mean consumption. However, overall inequality in Belarus is slightly lower (as measured by the Gini coefficient) than in the two countries with the lowest spatial inequality: Austria and Denmark.

Improving Mechanisms of Social Support

Distributional tensions combined with gaps in social protection hinder economic growth. Three policy principles could help build a sustainable and growth-enhancing social contract: (1) adequate support through flexible social policy instruments that address different family and economic situations; (2) fiscal sustainability of social support; and (3) policies to promote re-employment and minimize dependency on social assistance.

Strengthening the reach of targeted social assistance is an important policy instrument to reduce vulnerability and inequality. While the range of social assistance programs in Belarus is extensive, the income replacement rate from social assistance is low when compared to other countries in Europe. The World Bank's study *'Fiscal Incidence in Belarus'* conducted in 2017 shows that cash and in-kind benefits make up around 4 percent of disposable income for the bottom 10 percent of households by income, and only around 1 percent for the second income decile. These low rates suggest that the current social assistance system provides little direct poverty relief or protection from adverse economic shocks. Furthermore, one of the shortfalls of the targeted income support system (GASP) of Belarus is the high rate of exclusion of working poor households.

The current system of social support in Belarus can be strengthened while minimizing benefit dependency. The current social protection of vulnerable households with working members can be modified in two ways to reduce working poverty. First, by increasing the coverage and generosity of the basic income support, such as GASP. Second, by ensuring

that the incomes of beneficiaries on social assistance increase when they get jobs, through financial work incentives and employment support. This is not always the case if the benefit is withdrawn at the same rate as increased earnings. Estimates show that such measures would require additional resources but could still be affordable and cost-effective in terms of reduction in poverty rates and ensuring basic income.

Spatial Inequalities in Belarus

Spatial disparities in consumption are related to differences in income-generating abilities between the capital region and the other five oblasts. In 2017, Minsk City alone accounted for 27 percent of Belarus's GDP, while the gross regional product (GRP) per capita of Minsk exceeded the national average level by 1.6 times and by about two times the GRPs per capita of other *oblasts*, except Minsk. The capital city area is the major agglomeration node in the economy; other nodes around large cities lag behind. During 2015-2016 recession, the disparities between the central region and other *oblasts* have widened – the gap between the GRPs of Minsk and Mogilev *oblasts* increased by one-fourth between 2010 and 2016. Quantitative analysis confirms that location explains more than 80 percent of the variation in key regional indicators between 2006 and 2016, including industrial output, investment, employment, and household incomes. In addition, economic density is highly correlated with the distance from the capital city, with more distant areas having less dense economies.

The current economic landscape is in part inherited from the Soviet Union. In the 1960s-1970s, Soviet planners selected 19 geographical areas – each comprising several *rayons* (excluding the capital city) – to develop specific industries linked to endowments. Within *oblasts*, the economic activity tends to be concentrated in urban, densely populated *rayons*. In 2017, about 75 percent of Belarus's industrial output was produced in just 20 of 138 *rayons* (including large cities), and the population of these territories constituted 60 percent of Belarus's population. If selected economic indicators of *rayons* are distributed by quintiles, then per capita industrial output per hectare of the highest quintile is 3.6 times higher than the country average and almost 87 times higher than those of the lowest quintile. Moreover, more industrialized regions are characterized by better infrastructure: the share of land under roads, streets, and dwelling is 1.6 times higher than the country average and 2.4 times higher than in the lowest quintile, while population density is 3 and 13.1 times higher, respectively.

Private sector development is reinforcing patterns of economic density. Data record clustering – growth in the number of micro- and small-sized enterprises (MSEs) is positively correlated with growth in the number of large companies at the *rayon* level. Also, *rayons* with sizeable rural populations have seen less growth in MSEs than those with large towns. To address this unevenness, the authorities have used geographically concentrated tax preferences – including 'free economic zones', tax reductions for residents of small urban and rural areas – to attract business to regions other than Minsk. While these measures have helped to increase the number of small private companies across regions, spatially neutral policies – such as gradual, economy-wide liberalization of economic activities – have done more to encourage regional growth of MSEs. Panel data econometric analysis for 2006-13 shows that improvements in *Doing Business* ratings has had a significant and positive impact on the private sector development throughout all Belarus's *rayons* both in the short and the long run.

Going forward, Belarus's economic development will continue to be regionally uneven. The appropriate policy response will be to help people that experience job losses rather than try to counteract the forces of economic agglomeration. Instead, minimizing the economic distance among regions should be addressed mainly with spatially blind or universal policies, such as reducing the differences in quality of public goods, particularly education, provided in peripheral regions and improving connectivity. Instead of high-cost targeted interventions to save regional jobs by large-scale public investment projects, universal programs are needed to support a transition to more productive employment, preferably in the private sector. These universal programs can be supported by more robust social assistance programs, with improved targeting for vulnerable social groups.

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