

Real and Perceived Inequality, Poverty and Well-Being in South East Europe: Challenges of the Welfare State and Democracy

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1. Introduction: Inequality and Poverty vs. Legitimacy¹

The post-socialist economic transformation has resulted in rising inequality and poverty levels. Inequality, particularly in some countries/regions, is not only high if compared with the socialist era of relatively high levels of egalitarianism, but also if compared with many countries of West Europe. Poverty has become in many countries a major social and political issue (Górniak, 2000), and a major reason for personal concern, as attested in numerous public opinion surveys. While this is true for the whole of post-socialist Europe, there are some typical patterns: inequality tends to be higher and poverty more widespread in the countries of South East Europe (the ‘south tier’ of transition), than in those of Central and Eastern Europe (or ‘north tier’ of transition); both tend to be highest in CIS countries. (For illustration, see Tables 1 and 2; for more detail see UNICEF, 2001; World Bank, 2000; Fox, 2003). In addition, in both respects fast reformers seem to be doing better than slow (or stalled) reformers (World Bank, 2000 and 2002).

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In this paper, thematically, the focus will be on the issues of legitimacy of post-socialist reforms vis à vis increased inequality and poverty levels. The importance of subjective perceptions for democratic consolidation will be stressed. Some implications, particularly concerning the welfare state will be discussed as well.

Territorially/regionally, the paper's focus, though not exclusively, will be on the countries of South East Europe, which share a number of characteristics. They are typically lagging behind the so-called 'northern tier' countries in all relevant aspects of transformation: economic, political and institutional; they are falling behind in the process of economic development and exhibit basic disequilibria – fiscal, external and labour markets (as clearly shown in Gligorov et al., 2003; see also EBRD Transition reports, various years, for example EBRD, 2002, Table 2.1. Very indicative also are Freedom House transition scores where SEE countries are clearly converging: see Table 1, Tsukimura, this volume). They experienced a serious fall in output, major unemployment coupled with an 'abysmal employment record' (Gligorov et al., 2003), high instability, and they failed to establish foundations for sustainable and modern economic growth (Bičanić, 2003). In addition, they typically suffer from numerous institutional and democratic deficits; they are large but weak states (Gligorov, 2003); and they are 'slow reformers'. Typically, the 'second phase' transition indicators are much more behind than the 'first phase' ones (see EBRD Transition Reports). Most of them, in addition to standard transition challenges, have faced the challenge of building independent nation states under quite dramatic conditions of ethnic conflicts and war (Kasapović, 1996) which heavily influenced priorities, sequencing and choices in reforms, as well as the economic and political context of actors' behaviour in the societies concerned. A combination of weak states, high capture/corruption and serious fiscal deficits contributed to higher growth of both inequality and poverty than in the 'northern tier', in some countries quite dramatically – particularly those countries of the former Yugoslavia which suffered war, destruction and major ethnic migrations (Table 2). That poverty particularly affected war affected areas, displaced

persons and other war victims is clearly shown in World Bank, 2001; Bogićević et al., 2003; UNDP BiH, 2002).

It may be argued that rising inequality has been a necessary consequence of the post-socialist transformation (cf. World Bank, 2001: x; Fox, 2003), and is implicit to reform consensus on market and democracy in Eastern Europe, which necessarily involved dismantling of socialist egalitarianism and giving priority to material/monetary incentives through overall marketization of societies. This is seen as a consequence of dramatic distributional changes induced by the privatization of state/social ownership (Birdsall and Nellis, 2002); by private sector growth in general (Corricelli, 1997); by deep economic disorganization and reallocations (stressed by Blanchard, 1997) offering numerous entrepreneurial opportunities; by the liberalization of output and input markets, particularly labour markets leading towards increased wage differentials (Corricelli, 1997; Commander, 1997; Milanovic, 1999); and by changes in the size and composition of government spending (Commander, 1997).

All of the above-mentioned points could have been expected as inherent to economic transition formula of liberalization and privatization. However, 'increases in inequality were not correlated with the intensity of market reforms' (Fox, 2003: 7). What was not expected (particularly not in the Washington consensus inspired literature with its strong reliance on market-optimism) has been such a strong impact on that increase of widespread capture and corruption, of the explosive growth of the informal economy, of the failure of states to provide transfers to those in greatest need, and of the impact of monopoly on earnings differentials (UNICEF, 2001). Also, the dramatic collapse of some governments' capacity to govern and control the processes and to commit credibly to welfare policies was not expected.

Moreover, the increase in poverty, as well as its specific phenomenology (e.g. the 'new poor') has been clearly linked to the increase in inequality (World Bank, 2000). This coupling of inequality and poverty has become a major reason for concern, a major source of pressure on post-socialist states, and a source of profound uncertainty concerning the future of economic and po-

litical reforms and their sustained legitimacy in societies with new (even if imperfect) democratic constitutions. And this may particularly be problematic when:

- There is a conflict between actors' perceptions and expectations based on accepted rules of the inequality game. This may be particularly serious when: (i) economic growth is failing, and (ii) 'more' inequality is simply becoming 'too much'. Both seem to be true for the SEE countries. None of them has reached the 1990 GDP level (see, WIIW, 2003) but most have experienced a high increase in inequality (World Bank, 2000).
- Pathological inequalities and poverty (not a part of the early reform consensus) combine when the rise in inequality and poverty is largely perceived as unjust, due to corruption, war profiteering, organized crime, and absence of the rule of law, and when predatory behaviour and rent-seeking prevail as the dominant mode of behaviour, as, for example, in Bulgaria (Ganev, 2003). The whole region is seen as an area of high corruption (Jovic 2003), with weak states but high capture (Hellman et al., 2000).
- A 'stalled reform' syndrome develops, with early winners and powerful vested interests blocking socially beneficial reforms (Hellman, 1998; Havrylyshyn and Odling-Smee, 2000). The World Bank report strongly underlines the tendency of less inequality and poverty being present in advanced reformers and it being more present in 'stalled' or 'partial' reformers (World Bank, 2002; UNICEF, 2001: 28; Fox, 2003: 7). Gedeon also argues that due to democratic deficiencies and specific histories, 'Central European countries were more successful than East European and Balkan countries in constraining the winners in their activities to hinder economic reforms' (Gedeon, 2004: 90).

In all these cases, or a combination of them (which are arguably typical of the countries of South East Europe), we may expect that the political economy of the emerging wealth and income distribution structure could be contested, and legitimately so,

using democratic constitutions and rules. Does this mean that democratic transformation and economic transformation may come into conflict? In discussions on democratic transformation and consolidation in Eastern Europe, the paradoxes and inherent conflicts between the two have been widely discussed. The literature on tenuous or even conflicting relations between democratisation and marketisation in post-socialism abounds (for reviews see Gedeon, 2004; Orenstein, 2001; Rizman, 2003; Pridham, 2003; also Franičević, 2001). However, instead of taking a very general course, in this paper I shall be concerned with the possible impact of rising inequality and poverty on legitimacy and sustainability of reforms. It is important to note that the legitimacy of rising inequality very much depends on the actors' perceptions and interpretations of the processes involved. This interpretation involves norms, it is embedded in popular notions of fairness and equity, and it is filtered through the actors' 'moral economy' interfaces.

My usage of the term 'moral economy' clearly goes back to Adam Smith and his too often forgotten *The Theory of Moral Sentiments* (Smith, 1759). Smith was well aware that 'commercial society' could not survive if egoistic passions were not controlled by actors themselves.² If political economy is about accumulation and distribution, conflicts and power, states and markets, control and governance, moral economy is about social norms and perceptions, the values and judgments actors have about their individual participation and roles in economic processes, as well as about the nature of the economic system and its general outcomes. It is particularly about equity and justice, fairness and rewards, acceptable and unacceptable. Its central role is in providing the

2 However, according to Granovetter (1994) the first to explicitly use the idea of 'moral economy' was British historian E. P. Thompson in his 1971 paper 'The Moral Economy of the English Crowd in the Eighteenth Century'. In that paper, Thompson describes the violent collective actions of peasants in the 18th century in order to affect the price of grain 'which was grounded upon a consistent traditional view of social norms and obligations, of the proper economic functions of several parties within the community, which, taken together, can be said to constitute the moral economy of the poor' (1971: 78-79, quoted in Granovetter, 1994).

economic system, processes and outcomes with legitimation (Franičević, 2002).

This is why I find particularly important subjective perceptions and the notion of subjective poverty in particular, to which I turn in the next section. After that section's more general considerations, in the third section I shall discuss South East Europe; in particular subjective poverty and pessimism will be discussed in their relation to social restructuring and democratic consolidation. The fourth section deals with the challenges of the welfare state in post-socialist settings, particularly those facing high fiscal deficits. The paper ends with short concluding deliberations.

2. Real and Perceived: Subjective Perceptions Do Matter

Standard (objective) measures of inequality and poverty (see World Bank, 2000), based on absolute (adjusted poverty line) and relative poverty line measures (relative to the median or average), certainly indicate trends in distribution and welfare: they point to an increase in inequality and they certainly point to the – however uneven – increase in poverty across the region (Table 2).³ While such trends raise important policy issues concerning income policies and pro-poor policies (discussed, for example, in World Bank, 2000; UNICEF, 2001; UNDP Croatia, 2003; UNDP HDR reports on countries of the region and UNDP, 2003; Bogičević et. al, 2003), this paper primarily focuses on the issue of actors' perceptions concerning their well-being in the process of transformation. Namely, there is a phenomenon that absolute measures of poverty – showing in some cases comparatively low levels as we find, for example, in the Croatian case – are correlated with typically much higher subjective perceptions of being 'impoverished' and generally being pessimistic about the future. This discrepancy of absolute and relative measures of poverty, on the one side, and subjective perceptions on the other, was registered in other countries of

3 Górnjak provides a very good discussion on the relative merits of different approaches to measuring poverty lines and related dilemmas in different transition countries (Górnjak, 2000: 149-156).

the region (Krastev in UNDP, 2002; IDEA, 2002) as well as in countries elsewhere. Fox (2003: 9) warns, ‘Even in countries where income levels had recovered and most of the population was better off in expenditure terms than they had been in 1990, many reported being worse-off since the transition began’.

How much importance should we attribute to subjective perceptions? When analysing people’s welfare, mainstream economists mostly tend to shy away from subjective interpersonal comparisons based on individuals’ views on their welfare, well-being or happiness.⁴ In the mainstream paradigm ‘it is assumed instead that the economist knows the answer on the basis of objective data on incomes and prices’ (Ravallion and Loshkin, 1999: 2). However, it has been argued from Scitovsky onwards that subjective perceptions do matter, and that they typically run counter to some standard theoretical expectations concerning the relation between economic growth/income and well-being: ‘economic growth – rapid or otherwise – does not raise subjective well-being, even though the cross-sectional relation between well-being and income is positive’ (Easterlin, 2002: x).

It has been recognized that subjective welfare implies relative comparison with other people and with one’s own (and other people’s) pasts: i.e. it is under the impact of a person’s environment and his/her past experience (Easterlin, 1974 and Frank, 1985 explicitly introduced a ‘relative income explanation’), while Scitovsky (1976) ‘stressed comparison with past experience’ (see Easterlin, 2002: xi). Namazie and Sanfey (1999), in their paper on happiness in transition, firstly, review ‘the relative versus absolute debate’ and point to the arguments against overstressing the relativeness of happiness. They quote Veenhoven, who argues that ‘happiness in the sense of life-satisfaction depends only partly on comparison’ (Veenhoven, 1991) and finds (in Veenhoven, 1996) that ‘the correlation between happiness and income is much stronger in poorer countries’ (Namazie and Sanfey, 1999: 7).⁵

4 Ferrer-i-Carbonell et al. (2001) provide a useful discussion on measuring subjective welfare (economic concept) and subjective well-being (broader life satisfaction).

5 Unfortunately, Veenhoven’s papers were not available to me. The papers

Secondly, in their research on Kyrgyzstan they find widespread dissatisfaction with life ‘whether measured by income or expenditure’, that is in absolute terms. Yet, they also found ‘some support for the increasingly common view that the level of relative income helps make people happy or unhappy’ (Namazie and Sanfey, 1999: 20).

Ravallion and Lokshin examine subjective economic welfare in Russia and show that ‘there are clearly many other factors influencing subjective perceptions of economic welfare besides income’ (1999: 16): for example, relative incomes, incomes at different dates, expenditures, educational attainments, health status, employment and average income in the area of residence (1999: 24-25). Finally, they conclude: ‘The ways in which poverty is conventionally measured – the equivalence scales, regional cost-of-living deflators and so on – do not accord well with subjective perceptions of who is “poor” ... the systematic inconsistencies between a conventional objective measure and self-rated assessments suggest that greater caution is needed in interpretations that economists and others routinely give to conventional metrics of welfare’ (Ravallion and Lokshin, 1999: 25).

Even if there are many controversial issues, theoretical and methodological, related to subjective poverty and well-being (also see Ferrer-i-Carbonell and van Praag, 2001), subjective perceptions and assessments are certainly important: ‘people most often compare their present situation with that of others, with their own situation in the past or with their expectations for the future’ (Górniak, 2000: 152; also May, 2000: 27). In that respect, it seems plausible to claim that in post-socialist countries both factors – first, a dramatic break with past income and consumption habits, rights and guarantees, and, second, a significant/dramatic rise in inequality and uncertainty, accompanied with the emergence of narrow groups of nouveaux riche on the top, and broad groups of very poor on the bottom – could have played an important role in sub-

quoted by Namazie and Sanfey are: Veenhoven, R. (1991), ‘Is Happiness Relative?’, *Social Indicators Research*, 24: 1-34; and Veenhoven, R. (1996), ‘Developments in Satisfaction Research’, *Social Indicators Research*, 37: 1-46.

jective assessments of personal welfare and/or well-being, and provide an explanation of the cases of relatively lower proportion of the poor (by objective standards) in comparison to higher proportions of those ‘feeling poor(er)’.

Subjective poverty analysis may also provide an important link between economic and social reforms and their political legitimacy. In every society an increase in absolute and relative poverty is certainly a major reason for concern, which necessitates policy intervention per se – and this is certainly so in SEE (as shown by all recent issues of country Human Development Reports from the region). However, in SEE there are also high subjective poverty levels and a widespread perception of being on the losing side of post-socialist transformation. This prevalence of pessimistic expectations is the subject matter of the following section.

3. Poverty, Polarization and Legitimacy in South East Europe

What are the relevant trends in South East Europe? Even if available data on subjective poverty, as well as complementary data (those provided by IDEA, 2002), are far from complete and allow for nothing more than tentative conclusions, they are certainly indicative. While by the late 1990s, in most countries of the region, both the economic and political situation had improved (as pointed out in recent EBRD Transition Reports), public surveys regularly show that very large sections of the population feel poor(er) and do not expect significant improvements in their welfare (e.g. IDEA, 2002; see Table 3).

Take Croatia, a clear South East European leader in many respects. While Croatia’s poverty rate was found to be among the lowest in the region – about four per cent when using an internationally comparable standard of US\$4.30 a day per person at PPP and about ten per cent at maximum when using a nation-specific poverty line (World Bank, 2001: vi-vii; UNDP Croatia, 2003: 77) – ‘the gap between the rich and the poor in Croatia is wider than in middle or low-inequality countries’ (World Bank, 2001: x, also p.

15). However, individuals' subjective evaluations of how they fared during the 1990s offer a much bleaker picture. Despite the fact that during the 1994-98 period considerable economic growth, together with real wage growth, was recorded (when compared to other transition countries in the region), it did not change subjective evaluations very much: 'the number of people in Croatia who consider themselves poor relative to others is high (80 per cent, p. 22) and had fallen only marginally in 1999 compared to 1994 (by six per cent – V.F.), indicating deep discontent among the population about growing inequality' (ibid., x; similarly in UNDP Croatia, 2003 and Malenica, 2003). Of course, this perception of inequality is not only about income, but also about wealth distribution – privatization in Croatia particularly failed in terms of equity, and not only in terms of efficiency, producing deep social discontent (Franičević and Sisek, 2002). In spite of the fact that in the 2000-2003 period, after a deep recession, considerable economic growth was achieved, the level of dissatisfaction and pessimism remained high according to a recent survey of Croatian households. As reported in the press, 42 per cent households can hardly cope, 15 per cent is dependent on borrowing; one third does not believe that they will ever reach a satisfactory living standard; and about two thirds believe that next year the economy will be the same or worse. However there is more cautious optimism concerning five-year expectations: 42 per cent believe that the economic situation will improve (modestly, most of them) (Slobodna Dalmacija, August 17, 2003).

Pessimism, according to Krastev, seems to be widespread in the region: 'The results of the Balkan Survey conducted by International IDEA in the beginning of 2002 confirm a trend of collapsing expectations and growing disappointment with transition. Albanians are the only optimists for the future' (UNDP, 2002: 6). Even if we take into account that the survey actually shows a somewhat more differentiated situation across the region than that implied in the above statement, particularly concerning forward-looking expectations (one year vs. five year expectations – the latter tending to be more optimistic), it is still true that pessimism is widespread (Table 3; on Serbia also see UNDP Serbia, 2000).

Framing the issue of poverty in the context of actors' perceptions and normative judgements indicates that much more may be at stake. Firstly, there is a connection between poverty and inequality, on the one hand, and social restructuring on the other. Secondly, there is a connection between the poverty/inequality nexus and legitimacy.

Concerning social restructuring, there is little doubt that the increase in poverty and inequality in the region is underlined with deep social dislocations and changes which actors are well aware of, both in terms of personal welfare/well-being and in terms of their children's opportunities and prospects. Some groups tend to be poorer than others, and some (previously well-off and secure) have newly discovered poverty (the 'new poor', UNDP, 1998). In the context of increasing inequality, 'stresses between the socially excluded and the socially included which may, as in Russia, increase difficulties in governance' are growing (Mosley and Kalyuzhnova, 2000: 118). The proportion of those who consider themselves as 'losers' is greater than one could possibly expect from real data (on growth, real wages, etc.) (UNDP, 2002). Milanović, on a number of occasions, stresses as one of the most important sources of increase in Gini to be the 'hollowing out of the middle' (e.g. Milanovic, 1999: 321), and argues that emphasis should be placed on the issues of polarization rather than inequality per se (Milanovic, 1999: 321). If true, then a question emerges: Is it possible that the perception of being worse-off is more a subjective reflection of increased polarization (even dualization) of post-socialist societies, rather than just growing inequality and poverty? Malenica points in that direction as well: in his view high levels of subjective poverty in Croatia reflect not only downwards (on the social ladder) movement of individuals or families, but on larger social groups and/or professions as well (Malenica, 2003: 18). While it has been quite popular around the region to lament the disappearance of the middle classes during the transition, and of the formation of 'hourglass societies' (Bluebird, 2002), there has not been enough research on these fundamental processes of social restructuring to fully substantiate such claims.

In terms of social policies, if poverty is not only about material deprivation but also about inequality and social exclusion, if 'the

factors which drive poverty are also those which drive inequality and social exclusion' (as clearly recognized by the World Bank, Mosley and Kalyuzhnova, 2000: 119; see, for example, World Bank, 2000), and also drive loss of social position and status, then policies should be very much concerned with influencing social dynamics and inequality. They should be concerned with opportunities and capabilities, and not simply by offering a 'safety-net': they should deal with issues of winners compensating losers as well as issues of intergenerational compensation. This is especially important in SEE. Namely, besides those who are facing social exclusion for reasons we can find in all post-socialist societies, in this region there are great numbers of those who are not only socially but also physically excluded/displaced. A major, but not exclusive, part of these are war victims (Blue Bird, 2002; UNDP, 2002: 15-16), which only increases the pressure on already over-strained public and social policies and funds (as shown in Bogićević et al., 2003 for Serbia).

The second issue concerns the legitimacy of reforms in the region and, in connection with this, democratic consolidation. A low level of trust in political and public institutions prevails (Table 5), there is erosion of social capital, and corruption and state capture are high. In almost all countries of the region, a major public survey shows that the three most important public issues (although in differing order) are: unemployment, poverty, and corruption (crime ranks among the top three in Bulgaria and Republika Srpska) (IDEA, 2002). Moreover, there is a major coincidence between public perceptions on most important policy issues in SEE countries and personal fears (Table 4; IDEA, 2002).

The World Bank experts/reports are increasingly stressing the positive effects of good governance, not only for long-term growth but also for more egalitarian outcomes (through higher social spending and more effective targeting). They claim that both corruption and state capture adversely affect the poor and equality, but also the continuation of reforms – leading to 'stalled reforms', (see World Bank, 2000, pp. 163-170) or, as we may rather call it, the 'winners' curse'. Does this combination endanger democracy? Can it lead towards a legitimacy crisis (Choe, 2001: 16)?

Krastev is probably overstating his case in arguing that ‘in democratic politics perceptions are the only reality that matters’, which leads him to diagnose a ‘crisis of democracy’ in the region rather than a state of ‘unfinished democratization’ (UNDP, 2002: 6). Perceptions, however, do matter a great deal: ‘they are political reality’ (Gligorov, 2002). Moreover, they are a window for actors’ interpretation of the environment. They are framed with ideologies, mental models, and social norms (to paraphrase North, 1990) and they are embedded in actors’ moral economies. And actors do act upon them. One consequence is that pressures on the state to revert to a radically changed path may become too strong, and the legitimacy of the whole reform-package may become questionable if too many feel themselves to be on the losing side, or simply fear ending there. That such concern exists is shown by Delhey and Tobsch (2000) who demonstrate in their research on the consolidation of democracy in post-socialist countries that, generally, ‘support for political regime is more strongly related to social and economic indicators than it is to political indicators’. This is why ‘the improvement of individual welfare is a decisive but yet unfinished task for politicians in order to achieve a consolidated democracy’ (Delhey and Tobsch, 2000: 27). The fact that there does not seem to exist – presently – any viable and/or potentially preferable alternative to parliamentary democracy may be comforting, but should not elude us.

While in Romania and Bulgaria, and in Croatia too, the democratization process seems to have reached an advanced and/or sustainable level, some countries/territories are quite far behind: being in the process or at the start of the process (Albania, Serbia and Montenegro), being in political crisis (Macedonia), or being quasi or de facto international protectorates (BiH and Kosovo) (Gligorov, 2002: 3). In spite of the fact that surveys show a high general level of support for democracy in the region, there is also significantly low trust in democratic institutions and the rule of law (Table 5; IDEA, 2002).

Democratic consolidation and legitimacy of democratic regimes and ongoing reforms relies not only on the economic and social output, but also on people’s perceptions and (moral) inter-

pretations of it. And in all these respects, reasons for major concerns remain, as well as major challenges: serious institutional and democratic deficits, uncompensated losers and undeserving winners, inequalities and uncertainties concerning personal and intergenerational and interregional developments. The bases of fundamentalist nationalism are strong: still prevailing organic/traditional ethnic identification is heavily exploited by illiberal nationalist parties (particularly in countries of the former Yugoslavia, see Sekulić, 2003). There are too many people with pessimistic expectations. Perpetuation of such a situation may easily lead to questioning the post-socialist reform agenda, particularly if economic growth is not sustained, which, again, is not assured in SEE (Bićanić, 2003). Gligorov is right in concluding that 'it is not the case that the future of democracy is in any way assured in South-east Europe' (Gligorov, 2002: 9).

For SEE post-socialist states all of this is a source of major challenges and pressures. If the high share of subjective poverty and pessimistic expectations are indicative of the dramatically increased insecurity and uncertainty citizens are experiencing when faced with radical marketization and related distributional changes, if they are indicative of the doubtful legitimacy of increased polarization in post-socialist societies, then, clearly, the major challenge for the post-socialist state is to reduce this insecurity and uncertainty, to provide policies which will not deal with accumulation and growth only, but with equity and fairness, opportunities and well-being.

4. Challenges of the Post-Socialist Welfare State

The generalized marketization of post-socialist societies has radically increased the uncertainty and risks under which actors perform, and therefore the risks of defaults – both business and personal. Subjective poverty trends strongly suggest that individuals and families are well aware of the fact that not only their material welfare has changed, but the underlying rules of the game have changed as well, decisively influencing their social status and future, and thus their overall well-being.

However, inherent risks and insecurities of the market ‘have to be managed in order for the social legitimacy of the market to be maintained’ (Rodrik, 1997: 435). In societies with a great deal of social anomie, institutional gaps and democratic deficits, with announced rules of the game being quite different from the real ones, the risks of (non)adaptation are certainly increasing. Yet, there are too many who cannot privately insure against these risks, and for many risks markets for insurance are missing. And this is precisely the area where market failures are inherent. However, for the post-socialist state this is one of the most difficult issues. It is, namely, necessary but very hard to break with the legacies of bureaucratic paternalism, clientelism and lack of personal or business responsibility nurtured over decades, and at the same time to provide a socially reasonable amount of insurance against the unbearable risks of market society.

No doubt, the issue of compensation is central for the political economy of reforms (Roland, 2002). Namely, are the winners in the transition game (most likely a minority for the foreseeable future in SEE) going to be able to compensate the losers (most likely a majority for the foreseeable future)? This is particularly important in intergenerational terms. Will children have prospects to live better than their parents? The credibility of an affirmative answer rests both on economic growth and distribution of opportunities. Economic growth is necessary if commitment to compensation (redistribution) will be the credible one. Yet, it is not sufficient. For the emerging post-socialist welfare states not only affordability is problematic, so are the politics of welfare reform.

Concerning affordability, if economic growth is weak; if bottom-up development of new firms is heavily constrained (by market and regulatory failures/barriers) (Bartlett, 2001) and is unable to make up for the loss of jobs in privatized and public sectors; if unemployment is high, persisting and has major structural characteristics; if poverty and inequality are high (see Bićanić, 2001; EBRD, 2002: 10), then we may only witness a growing number of potential ‘clients’ looking to the state to provide relief, security, opportunity and fairness. This is putting a lot of pressure on the fiscally weak states of SEE, most of which, let us not forget,

have high fiscal deficits (see Gligorov et al., 2003; WIIW, 2003). Whatever choices of welfare system are made, they most likely mean: (a) reduction of rights and entitlements; (b) greater reliance on the market and individual participation in risk insurance; (c) greater expectations of alternative modes of provision based on civil society initiatives, public and private partnerships, local initiatives and collective organization.

Concerning politics, 'the welfare sector is the subject on which electioneering speakers are most prone to promise the impossible' (Kornai, 1997: 1186). In countries with major illiberal actors and constituencies, populist challenges to the state, accompanied by demands for reversals and full socialization of risks, are more likely to emerge. For would-be liberal-democratic states, the supply of paternalistic alternatives and the demand for them do not need to mean a full collapse in universal paternalism and a full reversal to socialization of market risks and failures. Yet, it may force them to accommodation, with uncertain influence on both the private sector of the economy, and fiscal sustainability. An accommodation towards corporatist solutions is particularly likely in those countries where the design and execution of social policies is strongly influenced by all-encompassing ethnic and/or religion based ideologies and institutions, for example the Catholic church.

On the other hand, due to heavy fiscal constraints, experimentations with the 'new paternalism' (MacGregor, 1999) may also ensue that this 'third way' includes 'decentralisation, local variation, more discretion to bend rules on the local level ... demonstration projects, and better informed governance'. It is particularly targeted at the 'socially excluded' – therefore different principles and rewards are operating at different social strata: for 'the poor and the deviant, those who cannot or will not assume responsibility for their own well-being, there is the new paternalism' (MacGregor, 1999: 109).

However, whatever choices on the welfare systems and policies are made, their failure may have important implications for the legitimacy of further reforms, thus risking 'undermining the market-oriented system that is the ultimate objective of the reform' (Rodrik, 1997: 440). For SEE countries, resolving the nexus of

accumulation and legitimation is certainly a major challenge for years to come.

5. Instead of Conclusions

The main argument of this essay was that subjective perceptions of one's welfare and/or well-being do matter, that subjective poverty is an important variable that should be taken seriously into consideration when approaching both sustainability of reforms and consolidation of democracies in post-socialist societies, in this case particularly those of South East Europe.

Why might the widespread feeling of impoverishment, of reduced well-being and pessimism be important for the future of reforms in South East Europe? No doubt, the dynamics of poverty and inequality are deeply influenced by the dynamics and nature of reforms. However, it is no less important to realize that, conversely, reforms may be deeply under the impact of real social trends and actors' perceptions, interpretations and judgements of these trends, that is under the impact of their 'moral economies'. The moral economy of the citizen plays a central role in providing the economic system, processes and outcomes with legitimacy (Franičević, 2002). And this may be even more so in the context of post-socialist democratizations, which, even if imperfectly, provide actors with constitutional rights and widened terrain to legitimately act upon their perceptions, interpretations and moral judgements.

Standard measures of poverty cannot fully grasp the above connections. Subjectively, impoverishment is viewed not only in terms of material welfare but also in terms of social well-being, in terms of being included/includable or excluded/excludable from the social games and opportunities offered by the great post-socialist change. It also seems that post-socialist actors perceive distributional changes not just in the simple framework of redistribution and the short term, but rather as something more substantial, the long term reaching across generations. The underlying process, taking place in the context of radically increased uncertainty, is a deep social restructuring, where individuals and

families are defining not only their position on the emerging new social ladder, but also their chances of climbing up in the future, or the risks of falling down.

All this is putting a lot of pressure on the fiscally weak post-socialist states of South East Europe. If post-socialist transformation means transforming socialist welfare states (and there is still a lot of nostalgia around and about them) into different states – states respecting both markets and human rights and if a welfare state is a constituent of the modern understanding of both democracy and good society, then the major challenge is to achieve the credibility of such a transformation. Yet, this is precisely where major uncertainties persist. Formal democratic arrangements and stability proven through multiple elections do not suffice. Will a ‘virtuous circle’ form and consolidate in the countries of the region, or a ‘vicious’ one that seems very much connected to further trends in inequality. It seems plausible to argue that ‘economic equality is a strong determinant of trust’ in a society, while ‘trust leads to policies that create wealth and reduce inequalities’. However, ‘there is also a vicious circle: misanthropy and inequality feed on themselves’ (Uslaner, 2003: 15-16). If Uslaner is right then we can hardly overstress the importance of ‘government policies that foster a more equal distribution of resources’ (Uslaner, 2003: 1), but of opportunities too, and economic growth which can only make such policies sustainable. In both respects, SEE countries are still falling behind, thus making a full consolidation of working democracy, with governments enjoying trust and legitimacy to act, with trusting citizens ready to engage for the collective/public good, still uncertain. Whether in this difficult process some new visions of a better society, and not just a more efficient economy, will (re)emerge to which practical proposals for social reforms will be linked, whether the ‘language of social’ will be (re)invented (as MacGregor, 1999, hopes), whether trust, interpersonal and relevant institutions of democracy, will increase in societies with particular political and cultural legacies, is yet to be seen. Clearly, the post-socialist transformation is not only about economic growth and efficiency; it is also about transforming society and the state.

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Table 1. Inequality and Poverty in CEE, SEE and CIS Regions (averages SEE, CEE, CIS) 1999-2000

	CEE and Baltics*	SEE**	CIS
Distribution of income (Gini)	0.30	0.34	0.70
Poverty rates	13.8	41.3	56.8

Notes: * Includes Croatia; **Albania, BiH, SiM, FYRM, Bulgaria and Romania

Source: EBRD, 2002, table 1.1, p. 10

Table 2: Absolute Poverty Rates and Income Inequality in Transition Economies

COUNTRY	Absolute Poverty Headcount*		Gini Coefficient for Income Per Capita		
	\$ 2.15 / day	\$ 4.30 / day	1987-90	1993-94	1996-99
<i>CENTRAL EUROPE</i>					
Czech Republic	0.0	0.8	0.19	0.23	0.25
Hungary	1.3	15.4	0.21	0.23	0.25
Slovak Republic	2.6	8.6	n.a.	n.a.	n.a.
Slovenia	0.0	0.7	0.22	0.29	0.25
Poland	1.2	18.4	0.28	0.28	0.33
<i>SOUTH EAST EUROPE</i>					
Albania	11.5	58.6	n.a.	n.a.	0.27
Bulgaria	3.1	18.2	0.23	0.38	0.41
Croatia	0.2	4.0	0.36	n.a.	0.35
Macedonia, FYR	6.7	43.9	n.a.	n.a.	0.37
Romania	6.8	44.5	0.23	0.29	0.30
Serbia**					0.33
Bosnia and Herzegovina***					0.26
<i>BALTICS</i>					
Lithuania	3.1	22.5	0.23	0.33	0.34
Latvia	6.6	34.8	0.24	0.31	0.32
Estonia	2.1	19.3	0.24	0.35	0.37
<i>CIS</i>					
Russian Federation	18.8	50.3	0.26	0.48	0.47
Ukraine	3.0	29.4	0.24	0.47	0.33
Moldova	55.4	84.6	0.27	n.a.	0.42
Belarus	1.0	10.4	0.23	0.28	0.28
Armenia	43.5	86.2	0.27	n.a.	0.59
Azerbaijan	23.5	64.2	n.a.	n.a.	n.a.
Georgia	18.9	54.2	0.29	n.a.	0.43
Kyrgyz Republic	49.1	84.1	0.31	0.55	0.47
Kazakhstan	5.7	30.9	0.30	0.33	0.35
Tajikistan	68.3	95.8	0.28	n.a.	0.47
Turkmenistan	7.0	34.4	0.28	0.36	0.45

Notes: *Mostly: 1998-99;

**Serbia: poverty 2000; Gini 2002

***Bosnia and Herzegovina: 2001

Sources: World Bank, 2000, p. 35, Table 1.1 and p. 140, Table 4.1; Gini -Bogićević et al., 2003; For BiH: UNDP BiH, 2002

Table 3: Satisfaction with the Economic Situation in South East Europe

3A: How are you satisfied with your present economic situation?

	Very satisfied	Somewhat satisfied	Neither satisfied nor dissatisfied	Somewhat dissatisfied	Very dissatisfied	Don't know / NA
Croatia	3,1	29,4	23,3	17,4	26,2	0,5
Macedonia	1,2	19,5	19,9	21,8	37,4	0,2
Montenegro	1,6	20	21,9	17,1	36,3	3,1
B&H	3,1	22	22,6	17,5	32,8	2
Bulgaria	0,2	6,8	10,1	17,7	63,6	1,6
Romania	1,1	16,7	18,1	36,9	26,9	0,4
Serbia	1,4	24,5	22,2	22,6	29,2	0,1
Republic of Srpska	2,5	21,5	24	19,1	32	0,8
Kosovo	4,7	42,6	23,4	12,7	13,6	2,9

3B: Compared to January 2001(one year ago), can you say that in the present your economic situation is...

	Much better	Somewhat better	The same	Somewhat worse	Much worse	Don't know / NA
Croatia	0,9	12,2	55	20,9	10,4	0,6
Macedonia	1,5	7,7	36,1	29	25,3	0,3
Montenegro	1,8	14,3	26,5	26,5	29,3	1,8
B&H	1,3	16,2	49	22,1	10	1,3
Bulgaria	0,1	4,1	36,8	34,9	23,1	1
Romania	1,5	15,9	34,8	31,6	15,4	0,8
Serbia	1,7	28,7	34,6	19,5	15,3	0,3
Republic of Srpska	2,2	17	36,9	24,3	18,7	0,8
Kosovo	5,3	39	36,3	14,1	3,3	1,9

3C: Over the next 12 months, do you expect the economic situation of your family to get better, to get worse or to stay about the same as now?

	Much better	Somewhat better	The same	Somewhat worse	Much worse	Don't know / NA
Croatia	2,6	30,1	50,3	11,4	2	3,6
Macedonia	2,2	26,3	43,2	20	7	1,3
Montenegro	6,3	29,4	27,7	8,9	11,9	15,8
B&H	2,3	28	46,1	8,5	3,6	11,5
Bulgaria	0,2	11,9	38,3	20,5	11	18,1
Romania	0,5	26,5	36,2	23,6	4,7	8,5
Serbia	4,9	45,4	31,5	8,6	6,7	2,8
Republic of Srpska	2,3	29,5	35	15,7	9,7	7,9
Kosovo	10,6	42,9	27,6	5,9	1	11,9

3D: During the next 5 years what do you think will happen to your economic situation?

	Much better	Somewhat better	The same	Somewhat worse	Much worse	Don't know / NA
Croatia	9,6	45,4	23	7,8	1,8	12,5
Macedonia	4,4	47,6	23,8	15	3,6	5,6
Montenegro	14,2	37,8	8,5	6,7	5,9	27
B&H	8,4	40,3	17	8,2	1,1	24,9
Bulgaria	2,8	23,4	17,8	7,9	5,8	42,3
Romania	1,3	36,1	26,3	19,7	3,1	13,5
Serbia	13,7	54	11,5	7,2	2,7	10,8
Republic of Srpska	4,7	35	14	11,3	8,7	26,4
Kosovo	23,2	46,6	4	2,8	0,1	23,3

Source: IDEA, 2002 (Survey, March, 2002)

Table 4: Most important policy issues vs. personal fears

4A: Three most important public issues

Three most important public issues are:

B&H R. Srpska	unemployment	corruption	crime
B&H Federation	unemployment	corruption	poverty
Kosovo	unemployment	poverty	corruption
Croatia	unemployment	poverty	corruption
Serbia	unemployment	corruption	poverty
Macedonia	unemployment	poverty	corruption
Bulgaria	unemployment	poverty	crime
Romania	corruption	poverty	unemployment
Montenegro	corruption	unemployment	poverty

4B: “What do you fear the most in the present?”

Bulgaria	unemployment	poverty	crime
Croatia	unemployment	poverty	poverty
Kosovo	unemployment	crime	poverty
B&H – R. Srpska	bad political situation	poverty	unemployment
Montenegro	bad political situation	poverty	unemployment
Macedonia	war, conflicts	poverty	unemployment
B&H - Federation	poverty	unemployment	crime
Romania	poverty	unemployment	bad political situation
Serbia	poverty	unemployment	bad political situation

Source: IDEA, 2002 (Survey: March, 2002)

Table 5: Public trust in institutions

Country/ Institution	<i>Presi- dency</i>	<i>Parlia- ment</i>	<i>Govern- ment</i>	<i>Local authori- ties</i>	<i>Courts</i>	<i>Police</i>	<i>Mass media</i>
Bulgaria	53.2	19.1	30.7	27.2	12.0	33.0	56.7
B&H – Federation	21.0	18.0	19.7	18.4	32.0	44.3	33.3
B&H – Republic Srpska	36.2	30.2	31.5	20.5	31.9	34.9	27.0
Croatia	42.1	24.4	25.9	21.9	17.2	30.8	25.1
Kosovo	55.0	66.0	57.5	57.5	68.8	75.6	35.0
Macedonia	23.5	12.5	11.7	16.9	19.6	38.9	26.2
Montenegro	40.7	31.4	33.4	30.8	35.4	27.2	21.5
Romania	52.6	31.9	44.3	49.5	37.8	46.4	68.7
Serbia	50.6	21.2	29.9	18.7	21.5	23.5	24.8

Note: Numbers in cells give summed percentages of those who ‘trust very much’ and those who ‘trust a fair amount’

Source: IDEA, 2002 (Survey: March, 2002)