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Fiscal Redistribution in Belarus: What Works and What Doesn't?

Belarus proudly calls itself a social state. Indeed, Belarus boasts one of the lowest poverty and inequality levels in the region. Fiscal policy in Belarus is equalizing and pro-poor, effectively redistributing income from rich to poor. As in Russia and many other Post-Soviet states, the equalizing effect of the fiscal policy in Belarus is mostly attributable to the pension system. Some of the other social policies are highly inefficient, failing to redistribute income. The prominent examples are utility subsidies and student stipends, which mainly benefit the upper part of the income distribution. The lack of adequate unemployment benefits is an opportunity to improve the efficiency of the social support system in Belarus.

The Constitution of Belarus characterizes Belarus as a social state, and Belarus takes its social state status seriously. The economic growth in the beginning of the 2000's was strongly pro-poor (Chubrik, 2007). Poverty according to the national definition (calorie-based poverty line, which in 2015 corresponded to $10.67 PPP per day) declined from 42% in 2000 to 5.7% in 2016, while the poverty according to the international threshold of $3.1 per day in PPP terms is fully eradicated. Belarus also has one of the lowest levels of income inequality in the region with a Gini coefficient of only 0.27 (UNDP, 2016).

How much of the pro-poor and equalizing effects could be attributed to the government policy? Probably it is impossible to give a complete answer to the question. Many non-formalized and not easily quantifiable government policies lead to the decrease in poverty and inequality. For example, the policy of support to state-owned enterprises might have redistributive effects through job creation. However, the absence of access to relevant data makes it impossible to estimate the effects of the policy.

Some of the government policies, on the other hand, are easily quantifiable with available data. Bornukova, Chubrik and Shymanovich (2017) analyze the redistributive effects of fiscal policies in Belarus using the Commitment to Equity methodology (Lustig, 2016). The authors find that the direct taxes and transfers in Belarus (taxes, transfers, and subsidies) are equalizing and pro-poor, lowering the national poverty headcount by 17 percentage points and the income Gini coefficient from 0.41 to 0.27. The high equalizing effect of the fiscal policies in Belarus surpasses those in other developing countries, including Russia where the direct taxes and subsidies reduced the income Gini coefficient by 0.13 (Lopez-Calva et al., 2017). The remaining discussion in this brief is based on the results from Bornukova, Chubrik and Shymanovich (2017), if not otherwise stated.

Fiscal policies and their redistributive effects

Taxation

The two types of direct personal taxes – the personal income tax and the social contributions tax – are both almost flat in Belarus. To fight tax evasion, the Belarusian authorities introduced flat tax rates in 2009, following a successful experiment in Russia. The personal income tax has some small exemptions for families with children, while the social contributions tax has a lower rate for agriculture employees. However, the effect of these deductions is relatively small: the direct taxes decrease the Gini coefficient by only 0.015.

The indirect taxes – the value-added tax, the import duties, and the excises – are weakly regressive, putting the burden of taxation on the poor. This is particularly true for the alcohol and tobacco excises. Again, the main purpose of these taxes is to penalize unwelcome behavior, and not to redistribute income, hence the result is not unexpected, and common for many countries. Overall the indirect taxes in Belarus increase the Gini coefficient by 0.05.

Direct transfers

Direct transfers are responsible for most of the equalizing effects of the fiscal policies. This is not surprising, given that the main purpose of the direct transfers is to fight poverty and provide support for those in need. However, most of the transfers are not need-based or targeted to the poor. Instead they are assigned to households based on their socio-economic characteristics aside income, such as age and maternity status.

Pensions are the main factor of reducing poverty and inequality. They reduced the Gini coefficient by 0.11 and decreased poverty (according to national definition) by 19 percentage points. The incredible effectiveness of the pensions is largely explained by the absence of other sources of income of the retirees. The majority of them does
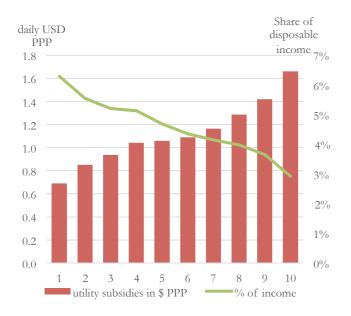
not work, and have no other pension savings or passive income. Pensions in Belarus are also redistributive in nature since they only weakly depend on one's income during the working life.

Different benefits and privileges also decrease poverty and inequality, but at a much smaller scale. The childcare benefits (for families with children aged 0-3 years) contribute most to the effects, decreasing the Gini coefficient by 0.013 and poverty by 3 percentage points. The variety of privileges does not contribute much due to their relatively small size.

Subsidies

Utilities and transport subsidies are also important elements of the social support system, and their existence is usually justified by the necessity to support those in need. Since the utilities subsidies are incorporated into tariffs and available for everyone independent of need, they are in fact benefitting the rich (i.e. people with big apartments and houses).

Figure 1. Incidence of utilities subsidies by income deciles

Source: Bornukova, Chubrik and Shymanovich, 2017

As seen on Figure 1, upper deciles receive more support through utilities subsidies, and this support is quite substantial, often surpassing $1 per day in PPP. However, as a share of income the

utilities subsidies are still progressive, and they in fact decrease the Gini coefficient by the tiny amount of 0.006, and decrease poverty (as any handout). The same is true for transport subsidies.

What could be improved?

Due to the flat nature of direct taxation and an absence of well-targeted needs-based transfers, some of the people in need still fall through the cracks. 1.9% of the population actually becomes poor after we account for the direct taxes and transfers. This headcount increases to 3.3% if we account for indirect taxes.

Another important issue is the efficiency of government transfers and subsidies in fighting poverty and inequality. It is not surprising that pensions have the largest equalizing contribution, as the government spends almost 11% of GDP on pensions. If we account for this fact and look at the efficiency (effect on poverty and inequality per dollar spent), pensions are not the leading program. It is in fact surpassed by different kinds of child support. Given that mothers in Belarus are allowed to take 3 years of unpaid maternity leave, which decreases household income, childcare benefits are relatively efficient.

The unexpected leader in efficiency is unemployment benefits, despite (or maybe due to) their negligible size. Shymanovich (2017) shows that unemployed face high risks of poverty, suggesting that an increase in the size of unemployment benefits and an easier access may bring huge benefits. The current minuscule size of the benefits (around $10-15 per month) is still enough to lift some people out of poverty, and has important equalizing effects, generating the biggest "bang for the buck" out of all benefits.

The student grants (stipends), the utilities subsidy and the transport subsidy have very low efficiency. These programs relocate a lot of funds to the upper deciles of the income distribution. Our calculations show that if all benefits, privileges and subsidies were not available to

those in the top two income deciles, the Belarusian budget could save 1.4% of GDP.

Conclusion

Fiscal policies in Belarus are quite effective in redistributing income. Bornukova, Chubrik and Shymanovich (2017) show that the direct taxes and transfers in Belarus result in a decrease of poverty by 17 percentage points, and decrease the Gini coefficient of inequality from 0.41 to 0.27. The pension system has the most important contribution, decreasing poverty by 19 percentage points, and the Gini coefficient by 0.11.

However, the absence of a needs-based, well-targeted social support system leads to many inefficiencies. Direct and indirect taxes lead to impoverishment of 3.3% of population, which is not compensated by direct transfers.

The absence of targeting also leads to 1.4% of GDP redistributed towards the two upper income deciles through benefits, privileges and subsidies. This is, of course, highly inefficient. Better targeting could allow saving these funds or redirecting them to unemployment benefits – the most efficient but a very small benefits program so far.

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