Social Protection and Social Inclusion in Ukraine

Executive summary

European Commission
Directorate-General for Employment, Social Affairs and Equal Opportunities
This report was financed by and prepared for the use of the European Commission, Directorate-General for Employment, Social Affairs and Equal Opportunities. It does not necessarily represent the Commission's official position.

http://ec.europa.eu/social/main.jsp?langId=en&catId=750

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Following the declaration of independence, Ukraine embarked on the course of socio-economical reforms and democratization that let out new opportunities to form social orientated market economy.

The transformation period of 1991–1999 in Ukraine was accompanied by deterioration in the socio-economic situation and living conditions, as well as by demographic crisis. Social policy was aimed at strengthening social protection; however the core of the social system remained unreformed.

Since 2000, efforts to improve the situation have been reflected in the GDP growth, development of a business environment, declining of unemployment, and increase income. However, some problems remained. These are: lack of structural reforms in the economic system, low innovative activity of national enterprises, and a large share of a grey economy. Orientation of economic policy on low wages and salaries is another obstacle for development. Inconsequent political actions, frequent elections, unwarranted increase of social expenditure created serious challenges for sustainability of social protection system in Ukraine.

1. General overview

1. The process of transition from a command to an open market economy in Ukraine slowed down, and became exhausting for both economy and population. In the context of transition, the first decade of Ukraine’s independence was marked by economic depression, hyperinflation, rising unemployment, decreasing of living standard. The GDP reduction during 1991-1999 was 59.2%. Since 2000 economic situation in Ukraine started to improve (average annual GDP growth in 2000-2008 was 8.5%). However, in 2008 the real GDP was only 74.1% of that achieved in 1990. GDP per capita in PPS in Ukraine still remains small in comparison with the EU-27 average (around 25%). The biggest challenges to Ukraine’s macroeconomic stability are: political instability, inflation, accumulation of foreign debt, a low level of domestic banks capitalization, and unsteadiness of national currency, a sharp decrease of production as a result of actual recession.

2. The share of GDP redistributed through the Consolidated Budget of Ukraine (Central plus local budgets) was 30% in 2007. In terms of the structure of the Consolidated Budget revenues, the main sources were value added tax (27.0% of total revenues in 2007), income tax (15.8%), profit tax (15.6%); the share of non-tax revenues was 22.1%. In terms of the structure of the Consolidated Budget expenditures, the social expenditures consisted 55.1%, in particular on social protection - 21.4%, on education - 19.5%, on health - 11.7% in 2007.

3. Employment trends in Ukraine reflect the absence of structural reforms in economy. Despite the growing number of jobs, their quality is worsening; the employment profile is characterized by large share of subsistence agriculture, and significant skills’ mismatch in the labour market. The economic growth during 2000-2008 did not catch up with a level of employment in Soviet period. In 2008 number of employed was 20.4 million persons (in 2000 — 20.2 mln, in 1990 — 25.4 mln). In 2008 employment rate (for age group 15-64 years) had increased up to 63.4% comparing to 58.6% in 1999. The economic activity rate in Ukraine in 2008 was 67.8%, which is lower in comparison with the EU average. Low economic activity rate in Ukraine can be attributed to a combination of factors, among which: a strong motivation of youth to obtain a higher education; low retirement age; pre-term preferential retirement (for men); and a lack of affordable quality child care facilities. Economic crisis leads to the growing underemployment (unpaid or partly paid administrative leaves or short daily (weekly) hours of work, and wage arrears delays) in order to retain staff employees and to avoid mass lay offs.

4. During the first decade of independence Ukraine experienced a growth of unemployment because of the reduction in the number of jobs in transition period. In 2000, when economy started to grow the rate of unemployment, according to the ILO-concept, was steadily decreasing and reached a level of 6.5% in 2008. However, relatively low level of unemployment is caused by labour migration, informal employment (in particular subsistence agriculture) and underemployment.

One of the major problems in Ukraine is the inequality in the development of urban and rural areas, therefore half of the rural employed is forced to work in the informal sector. Roma and Crimean Tatar communities are the most vulnerable groups among national and ethnic minorities in Ukraine that are characterized by extraordinarily high unemployment.

In spite of innovative technologies of job placement implemented by the Public Employment Service, the quality of jobs offered remains unsatisfactory. Despite decrease in a share of expenditures on the “passive” labour market policy (from 0.38% of GDP in 2002 to 0.25% in 2008), the share of expenditures on the “active” labour policy (0.1% of GDP) is significant less then in EU-27 (0.47% of GDP). The possibility to find a job with the assistance of the Public Employment Service is limited by the lack of vacancies offering decent wage (as a result of recession).

5. The problem of low wages is very urgent in Ukraine. Cheap labour does not motivate employers to introduce new technologies. Low wages lead to a poverty of employed population and to the decline in economic and labour activity, creating obstacles to the full-scale implementation of a social insurance system. About 85% of poor households have at least one employed member; moreover, employment has no impact on the poverty
risk. As a result of economic crisis, the practice of wage arrears accumulation went into force. On January 1, 2009 wages were delayed for 346.2 thousand regular staff in economically active enterprises (3.2% of total number).

6. Ukraine’s economy is characterized by large scale of informal (grey, shadow) economy that leads to a widespread practice of underreporting of wages, tax evasion and reflects all negative features of undeclared work. According to estimates of the Monitoring poll of Ukrainian population’s public opinion (April 2009), more than 19.0% of interviewed (polled) noted that a large part of their salaries was undeclared (“envelope payment”) even in case of formal job.

7. The development of educational system in Ukraine is characterized by the worsening of its quality, insufficient adaptation to the labour market demands, small-scaled and ineffective vocational training programs, low readiness to the innovative economy needs, the decrease of competitiveness, and by the weakness of institutional reforms in the educational sphere.

Network of pre-primary institutions was significantly reduced, due to fertility decline in 1990-2000. From 2001, fertility started to increase, and a need for pre-primary institutions increased as well. In 2008, only 57% of children of the preschool age attended pre-primary institutions.

In terms of enrolment in primary, secondary and higher education, Ukraine holds the 39th position among 172 countries. According to this rating, Ukraine is close to the EU countries and above the CIS countries (WEF, 2008).

However, there are problems of different educational standards for different groups. Namely, standards are varying according to inter-settlement and ethno-national features: quality and access to education are different in rural and urban areas; children from poor families have fewer opportunities to study in schools, which meet modern standards.

The budget expenditures on education have increased from 3.8% of GDP in 1990 to 6.4% in 2008. In terms of the structure, in 2008 budget expenditures on primary and secondary education that introduce a main part of expenditures was 41.7% of the total, while tertiary education absorbed 30.4%. A share of expenditure on pre-primary education was 12% of the total. Participation of private sector in provision of pre-school, secondary and tertiary education is not significant.

8. The demographic situation is characterized by ageing of population, low fertility and high mortality (especially among men of working age), and by the high prevalence of AIDS and tuberculosis. Ukrainian population is approximately 46.2 million and steadily declining. Percent of rural population has been unchanging and reached 32%. Demographic projections indicate that population will decrease by some 20% and will reach 36.3 million in 2050. Such large losses of demographic potential can be explained by widespread standards of small families, short life expectancy and negative migration balance.

9. During period of independence, regional disparities increased throughout all economic and social indicators. Industrial regions of eastern and southern parts of the country demonstrate better economic indicators, while Western part has better environmental and social indicators.

In terms of rural-urban disparities, the most unfavourable situation is observed in rural area because of the absence of jobs, degradation of social infrastructure, that cause insufficient living conditions (problems with sewage system, water-supply), and limited access to high-quality education and health care.

2. Social protection system

1. The Social Protection System in the former USSR provided benefits and services for old people, disabled individuals, and families with children. This System was built on the principle of “insurance without contributions”. Financial resources were accumulated on the base of payments from enterprises and transfers from the State Budget.

Since the independence of Ukraine, the insurance-based social protection system started to be implemented. Owing to this the role of employers and employees became stronger, and State Social Funds were separated from the State Budget.

2. The social insurance scheme is presented by four types of the Compulsory State Social Insurance: 1) against industrial accidents and occupational diseases; 2) against unemployment; 3) against temporal disability; 4) pension insurance.

The main sources of revenues Social Insurance Funds are contributions of insurers – employers and insured persons (except for the Fund of Social Insurance against Industrial Accidents and Occupational Diseases. Here contributions are paid only by employers); and transfers from the State Budget (for non-insurance payments and in case of the Funds’ deficit).
Total expenditure of the Social Insurance Funds was 15.7% of GDP in 2007, including 0.5% of GDP – against unemployment, 0.7% of GDP - against temporary disability, 0.4% of GDP - against industrial accidents and occupational diseases and 14.0% of GDP - Pension Fund.

3. Non-contributory social benefits and services schemes, that funded from the State Budget, include following items: social assistance (family allowance, assistance to low-income families, assistance to individuals handicapped from birth, disabled children’s allowance); privileges (war veterans, veterans of labour, victims of the Chernobyl disaster, certain type of professions); housing subsidies (in case if family’s income is not enough to pay for housing services and gas); and social services (usually for lonely persons with disability).

4. The largest share of Central Budgets’ expenditures on social protection is expenditure on pensioners (more than 50%). Reasons of high expenditures on social protection of pensioners are: a demographic ageing and low retirement age that cause large number of people of retirement age, and long list of privileges for pensioners (for example, all pensioners have a right on free urban and suburban public transport).

3. Poverty and social exclusion

1. During the period of former USSR a phenomenon of poverty was denied. There were no investigations or estimates of poverty. The research on population with low income was made at the country level, but not at republics or regions levels, and this data was closed. After statistical data became available, about 11% of the population in Soviet Ukraine were claimed to be poor.

   In Ukraine, monitoring the poverty is performed in accordance with two approaches: ‘relative’ (the national poverty line) and ‘absolute’ one (the subsistence minimum). The national poverty line is defined as 75% of the median total expenditures. It based on the equivalence scale that assigns a value of 1 to the household head, of 0.7 to each additional adult and of 0.7 to each child. The second national relative (‘extreme’) poverty line is defined as 60% of the median total expenditures, based on the same equivalence scale.

   The administrative subsistence minimum was established as a basic state social standard to calculate state social guarantees (minimum wage, minimum pension, state social assistance) in 2000. The size of the subsistence minimum is designed for different socio-demographic groups every year. It is calculated in accordance with a basket principle and is used as the absolute poverty line.

2. The dynamics of poverty cannot be investigated evenly for the every year of transition period of 1991-2008 owing to irregular and incomplete data up to 1999 when monitoring of poverty has been provided by the State Statistics Committee of Ukraine. According to the expert's estimation on the basis of the families' budget survey in 1996, 85-90% of Ukrainians were poor using poverty line of 1990. Since 1999 State Statistics Committee of Ukraine provided regular monitoring of poverty. Results of the 1995-1996 survey “Incomes and Expenditures of the Population of Ukraine”, supported by the World Bank, and proved that the poverty was 29.4% using the poverty line of USD PPS 4.3 per day, while using the poverty line of USD PPS 2.15 per day – 3.0%.

   Beginning from 2000, when macroeconomic situation in Ukraine began to recover from transformation recession, absolute poverty dropped from 70.6% to 12.6% in 2008. At the same time, relative poverty was stagnating at the level of 26-28% during the last nine years (HHS-data). It can be explained by the fact that economic growth did not decrease inequality, which was established during the transition period.

3. In terms of vulnerable groups, the report indicates such key factors of poverty: age (children and elderly), place of residence, size of household, number of children in a household, and unemployment. High education (at least of one household member) is the only factor that can reduce poverty in a household. Employment might cause a small decline in the poverty risk, however, it does not protect from it. There is a big gap between people living in urban and rural areas: a share of poor individuals among rural population reached 38% in 2006-2007, while the urban poverty rate for the same years was 22.1%.

4. In order to fulfill National Millennium Development Goals two strategies for poverty elimination were developed: "Strategy of Poverty Overcoming" from 2001 and “Complex Program of Nation-wide Realization of Decisions, Accepted at the Global Summit on the Sustainable Development, for 2003-2015” from 2003. However, the implementation of strategies and programs remains a main problem in Ukraine. Obstacle to this is their multivariate nature that makes a broad range of life spheres to be involved; underdevelopment of monitoring and evaluation tools; and absence of goal-oriented funding.

5. The current social assistance system can do little to affect the poverty level due to the improper distribution of social benefits. The most vulnerable families with children are insufficiently supported by the state. The problem of high poverty among families with children is often related to the low remuneration of labour.

6. The most urgent aspects of deprivation in Ukraine include: inappropriate housing conditions, limited access to services of social sphere, lack of property, and inability to have a full-scale leisure. If to compare with urban, rural population experience larger deprivation of social infrastructure, in particular, in terms of territorial
accessibility of medical and educational institutions. Comparing with households without children, households with children suffer from poor housing conditions (overcrowding) and greater need of money for family leisure.

7. The problem of long-term and inherited poverty and of so-called "new" groups of social exclusion (HIV/AIDS-infected people; drug consumers (in particular, injection users); homosexuals, homeless, etc.) is little-investigated in Ukraine due to acute shortage of statistical information and survey data.

4. Pensions

1. Existing pension system includes following components: contributory compulsory state pension insurance based on PAYG principle (about 3/4 of total public pension expenditure); different state pension schemes, which are financed from the State Budget by additional pension contributions (about 1/4 of total public pension expenditure); and private (non-governmental) pension schemes based on voluntary participation (regular benefits have not been paid out yet).

2. In Ukraine, expenditures on pensions as percentage of GDP are the largest in Europe. During 2004–2008 due to frequent elections, the value of pension benefits increased five times in nominal terms. In 2009 pension expenditure will reach its record – over 17% of GDP (in the 1991-2003 period – about 8-9% of the GDP).

3. At the same time, at-risk-of-poverty rate is much higher for retired people than for the working age population (especially for women and individuals of 75 years and older) and has a trend to increase. Gender gap in at-risk-of-poverty rate for retired people is substantial - the rate is 5-6 percent points higher for old women than for old men.

4. Employment rate of elderly is relatively high (40% of individuals aged 55 to 64 are employed), accounting for the extremely low retirement age in Ukraine. The largest proportion of old workers is observed in those spheres of economy, where employees have right for early retirement: mining, water and air transport, education and health, culture and sports.

5. In 2009, due to financial and economic crisis, cash gap between revenues and expenditures of the Pension Fund was more than 3% of GDP. This deficit was covered by loans provided by the State Budget.

6. The long-term challenges for sustainability and adequacy of the pension system are related to demographic trends, in particular to very low fertility and ageing. Old age dependency ratio (65+/15–64) is projected to increase up to 38% in 2050, and pension system dependency ratio (pensioners/contributors) – up to 132%. Unless there is a substantial increase in the effective retirement age, such demographic prospects will have negative impact on financial sustainability of the system, in which a generation of working individuals supports a generation of pensioners.

7. Difficult financial situation and demographic trends require fundamental reforms in the sphere of employment and pensions. In the long-term, the extension of working lives would have the highest efficiency (inter alia via increasing the retirement age for women and decreasing number of categories of workers entitled to early retirement). Introduction of certain degree of pre-funding of pension expenditure could be another solution.

5. Health and long-term care

1. Ukraine health care organization, management and financing principles were inherited from the Soviet Union. According to the Constitution of Ukraine each person has a right to free of charge health care. However, in practice accessibility is limited. In spite of the big number of health care institutions, the system does not work effectively. The poor quality of health care is stipulated by insufficient investments and low wages in the health care system. As a consequence, the health outcomes are worsening.

2. The economic crisis of the transition period led to the deepening demographic crisis. In the first half of 90s the morbidity and mortality rates significantly increased, subsequently the situation has been flattened out, but persistent trend of improvement is not observed. In Ukraine life expectancy is the lowest in Europe; in 2008 life expectancy of males was 62.3 year, of females – 74.5.

3. The health care system reform is being discussed by governmental officials, politics and health practitioners for more than a decade. In general opinion, public health reform have been aimed to provide better access and better quality of health services for people and merited remuneration for doctors and nurses. However, there is no consensus about the sector's future organization and financing.

4. The lack of consensus on reform orientation and the slow progress of reform are rooted in economic and social crisis, frequent rotation of Governments, corruption of health care system and underestimation of health value in society.
5. The immediate measures which might be undertaken are as follows: to eliminate the resources fragmentation and to improve funds consolidation in localities; to divide out the functions of provider and payer in the health care services; to divide out the primary, secondary and tertiary care, providing the preference for the primary care; to optimize the hospital network and to reorganize the hospitals into independent non-profit municipal establishments; to introduce fee-for-service method of funding; to provide the sector with the highly-skilled managers; to organize the wide-scaled explanatory action in media and to find the support for the reform through the people.

6. Key challenges

1. The social protection system of Ukraine has a lot of challenges, some of them were inherited from the Soviet period. The lack of public finances leads to choose between development and consumption. Political instability and permanent elections (since autumn of 2004) inclined decision-makers in favor of consumption. Pressing challenges for Ukraine’s macroeconomic steadiness are lack of structural reforms, raw-material orientation of industrial production, low innovation activity, high inflation, corruption, insecurity of property rights, and poor legislation. The significant fluctuation of exchange rate, accumulation of foreign debt, low level of domestic banks capitalization became serious macroeconomic shocks as well. The nowadays crisis causes the sharp reduction of GDP and expansion of unemployment.

2. In terms of social protection system, key challenges are:
   - to reform the current system of privileges, in particular, to minimize professional privileges and to transform social privileges into cash means-tested benefits;
   - to improve the quality and efficiency of social services and to introduce social passports for families and individuals who apply for social service. It is necessary to develop individual programs for such families and individuals;
   - to direct efforts on training of skilled specialists of social services;
   - to provide functionality of appropriate social services’ institutions. The key position among such institutions can belong to non-governmental institutions; to adjust mechanism of support of public initiatives on the local level.

3. During the period of economic growth, Ukraine has made considerable progress towards reducing the absolute poverty. However, because of the lack of effective steps in implementing the state policy, it could not reduce income inequality emerged in transition period. As a result, relative poverty rates have been stagnating for 9 years.

   The Ukrainian society does not address problems of some minorities, which face social exclusion. It concerns traditionally vulnerable population groups (disabled, ethnic minorities such as Roma, Crimean Tatar, etc.) as well as new groups that appeared rather recently – HIV/AIDS-infected, drug consumers (in particular injection users), and sex minorities. Generally, tolerant attitude to such people is combined with intolerance of staying in their neighbourhood, leading to social isolation of these groups in all spheres of life.

   Strategic documents need to be revised and updated with consideration of the recent changes in the poverty situation and results of the new studies of poverty and social inclusion. New strategy has to take into account possible consequences of financial crisis and identify new steps to overcoming monetary poverty. The main task of new strategy is determination of groups of social exclusion and development of measures on their integration in the society.

4. The main challenges for stability and adequacy of the pension system are related to demographic trends, especially to very low fertility and to the population ageing, as well as to a slow progress of reforms. The most urgent problems of the pension system in Ukraine include:
   - improvement of the mechanism of assignments and indexation of pension benefits;
   - legislative regulation of a guaranteed minimum pension;
   - involvement of broad population groups into the pension insurance, increase of the retirement age and / or the necessary length of service (especially for women),
   - implementation of the compulsory funded pension insurance;
   - development of private pension schemes, in particular, occupational pension schemes for financing early retirement of people working in harmful conditions.
   - ensuring transparency of the pension system and codification of the pension legislation.

5. The key faults of health and long-term care sector are:
financial insufficiency and, at the same time, ineffective use of available resources;
rigid, complicated and non-transparent system of funding;
limited access to quality services; large-scale under-the-table payments.

The key challenges of the health system reform are coordination of the state guarantees with financial resources, restructuring of health care system on the principles of primary health care and universal coverage, the transition from administrative to contractual model.

6. In terms of statistical problems, the study was complicated by availability of data. In the beginning of transition period Ukrainian statistics conformed to soviet standards, and it was not adapted to market conditions and international methodology. Practice of sampling surveys in compliance with international standards was absent. Hyperinflation in 1992-1995 (37,193.2 times), introduction of national currency in 1996, and instability of exchange rate made investigation of dynamics impossible.

During 90’s international standards had been generally implemented in official statistics system. The Household Living Condition Survey and Survey on Economic Activity of Population were introduced on the permanent basis. However, there is a need for improving poverty measures, in particular, closer alignment between national systems of poverty monitoring and European practice.

Concerning labour force survey, there is a necessity of monthly monitoring and seasonality adjusting for more clear and operative supervision of trends. There are also some gaps in the system of indicators; in particular, the average labour market exit age is not calculated.

The statistical data on health, education, social protection is provided by corresponding Ministries and authorities. However, there might be not always comprehensive, transparent and objective.