

SOCIAL PROTECTION AND SOCIAL INCLUSION IN ARMENIA, AZERBAIJAN AND GEORGIA

EXECUTIVE SUMMARY- SYNTHESIS REPORT

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Executive Summary

This study gives a comprehensive recent picture of social protection and social inclusion in Armenia, Azerbaijan and Georgia. Starting with an analysis of the background, in particular economic, demographic and labour market developments, it provides a comparative picture of poverty and social inclusion, pension and health care systems.

The synthesis report on social protection and social inclusion draws on country studies on social protection and social inclusion in Armenia, Azerbaijan and Georgia which were elaborated in 2010. These studies are to be seen in the context of the European Neighbourhood Policy and in particular the Eastern Partnership Programme, which aims at enhanced cooperation between the EU and its Eastern Neighbours by providing “*support to economic and social policies designed to reduce disparities within each partner country and across borders*” ([Communication 823 of 3/12/2008](#)). They link up with European policies to modernise social protection schemes and promote social inclusion, referring in particular to the overarching *Open Method of Coordination* (OMC) and the headline target of the EU 2020 strategy to combat poverty and social exclusion. The synthesis report and the country studies of the Southern Caucasus countries follow earlier similar initiatives of the EU, in particular the Study on the Social Protection Systems in the 13 candidate countries (2003), the Synthesis Report and the Country Studies on Social Protection and Social Inclusion in the Western Balkan countries (2008/2009), and the Synthesis Report and the Country Studies on Social Protection and Social Inclusion in Belarus, Moldova and Ukraine (2009/2010).

Main factors influencing social protection and welfare

The Southern Caucasus countries have experienced fast economic growth in the past decade, overcoming a sharp recession after the break-up of the Soviet Union, at a faster pace than many other CIS countries. Nevertheless, the basis for economic growth was and still is vulnerable. The main reason for high growth rates in Azerbaijan was its expanding oil industry, which represents the most important economic sector of the country, while economic growth in Armenia and Georgia has been narrowly based on the service and construction sector and is considerably driven by remittances. This one-sided and thus vulnerable basis of economic development has been reason for concern for a couple of years. The 2008 financial and economic crisis has affected all three countries, in particular Armenia and Georgia, and was reflected in a substantial contraction of output. Armenia's economic decline was one of the highest in the region; only in Ukraine was the recession even more severe. The decline of the economy has been largely attributed to dependence on the Russian economy, a drop in remittances and a considerable contraction of the construction sector. Georgia was additionally affected by the economic downturn caused by the military conflict with Russia in August 2008. In autumn 2010 recovery of the economies in all three countries translated into positive growth rates of around 4-5%. Nevertheless, per capita income in Armenia and Georgia has barely recovered to pre-crisis levels.

The three countries are characterised by a high proportion of agricultural employment, insecure and seasonal jobs and high informality of the labour market, threatening public revenues due to low collection rates of tax and contributions. Informal employment in the whole region is much higher than in the new EU Member States or the Western Balkan countries. It also appears that economic growth in recent years only partly translated into a more equal income distribution in the countries. Wages have increased, but there are substantial disparities between the private and the public sector, between different economic sectors and between rural and urban areas. A significant gender pay gap is also reported for all three countries. Remittances play a significant role for income generation in all three countries. It is important to mention that due to the fact that remittances mainly stem from Russia, the countries are vulnerable to risks in the Russian economy. There are indications that the financial crisis and subsequent rising unemployment in Russia has led to a considerable decrease in remittances.

Substantial territorial disparities exist in Armenia, Azerbaijan and Georgia and are considered a serious obstacle to economic and social development. Such disparities reflect a common challenge in the Eastern Partnership region and have also been observed for Belarus, Moldova and Ukraine. Economic development, growth and wages are significantly higher in urban areas, but there has been only limited political response to the challenges of territorial disparities.

With regard to their demographic developments, the population of the Southern Caucasus region enjoys a high life expectancy compared to other former countries of the Soviet Union. In particular life expectancy of men is considerably higher in Southern Caucasus as compared to Belarus, Moldova or Ukraine. At the same time, fertility has been going down clearly in Armenia and Georgia. Like many other post-Soviet countries after independence, Armenia and Georgia in particular were seriously affected by out-migration. The net migration rate has been negative since the 1990s in all countries, but emigration was much more substantial in Armenia and Georgia compared to Azerbaijan. While the peak of emigration in Armenia was observed in the early 90s, Georgia faced persisting high negative net migration up to 2010. The main destination country of migrants from Georgia and Armenia is the Russian Federation. High emigration rates and the resulting decrease of the population are considered a considerable threat for labour supply and economic developments. But this will also affect the future of social protection: Due to lower fertility, continuing emigration trends and increasing life expectancy, the age structure in Armenia and Georgia is estimated to change significantly. The share of persons above 65 will increase considerably and the old-age dependency ratio is expected to increase to a level similar to that of Belarus, Moldova, Ukraine and EU member states. Azerbaijan, due to significantly higher fertility rates and less emigration, will experience a rather favourable development as compared to Armenia and Georgia.

While the statistical account of ethnic minorities is limited, the general picture shows that the ethnic composition in all three countries is rather homogeneous and the share of ethnic minorities has decreased since independence. The country studies reveal that access to education for ethnic minorities, e.g. Georgians in Azerbaijan or Armenians in Georgia, becomes more difficult as the common language in the region, Russian, loses importance. The limited information available on the Roma population in the Southern Caucasus suggests that in particular Roma children are not socially included and there are no policy initiatives to address their situation.

Following the conflicts in Nagorno-Karabakh, Abkhazia and South Ossetia, internally displaced persons (IDPs) represent a considerable share of the population in Georgia and in Azerbaijan. IDPs are at risk of being socially excluded and are characterised by higher poverty rates. They are affected by higher unemployment, and in particular displaced women experience higher unemployment rates. Children of IDPs are considered to be disadvantaged in the education system. IDPs are obviously seen as a vulnerable group in these societies. There are visible policy efforts to improve their social situation. However, initiatives are often limited to cash and in-kind benefits such as social assistance, free usage of health care, or free provision of electricity, gas and water. One of the main reasons of social exclusion of IDPs, however, seems to be their limited access to the labour market and the fact that they live in collective settlements. An important step towards improved social inclusion of IDPs thus seems to be targeted labour market programmes for IDPs and replacement of densely populated collective settlements by smaller units which allow for a better active social inclusion into society, while taking into account that certain groups of IDPs such as the elderly and disabled might need specific support.

As already mentioned, all three countries experienced considerable economic growth during the past years. This growth, however, has not been translated into increasing activity and employment rates. In contrast, in Azerbaijan and Georgia, activity and employment rates are declining. The countries are further characterised by low wage employment and high self-employment rates. Employment in all three countries is highly vulnerable due to the high shares of agriculture and small-scale informal activities in total employment. Subsistence

agriculture in most cases can be considered as hidden unemployment and as a coping strategy against poverty. Unemployment and underemployment are common features, with particularly high youth unemployment rates indicating the difficulties young people experience when entering the labour market.

The creation of jobs outside the agricultural sector offering decent working conditions is therefore crucial in order to reduce poverty and enhance human capital. The improvement of business environments in particular for SMEs and re-training measures for the unemployed are important pre-conditions for successful job creation measures.

All three reports show that education and decent employment are key factors for preventing poverty and social exclusion. People with higher education are more likely to become employed and employed people are more likely to escape poverty. However, it is also obvious that education is no guarantee for labour market integration, since in all three countries the share of unemployed among those with specialised secondary and tertiary educational level remains high.

Extreme underfunding in education accompanied by extremely low teacher salaries led to further deterioration of the infrastructure, low quality in education and considerable inequalities in access to educational services. The same applies to employment policies where extremely low funding renders their impact on employment nearly insignificant. There are wide and growing regional and rural-urban disparities on the labour market, and rural areas are also at a disadvantage compared to urban areas in terms of educational institutions and quality of education; corruption is widespread and favours children from rich families. In order to promote human capital, it is therefore crucial to increase funding considerably and to give individuals the opportunity to upgrade and adapt their skills and knowledge to the changing economic needs.

In view of high youth unemployment rates in all three countries, the modernisation of VET (vocational education and training) systems in particular with regard to governance, institutions and curricula needs to be continued, in order to strengthen links between vocational education and labour market needs and thus to render VET schools more attractive as important players in the skill-formation process. In this context, the capacities for monitoring labour market developments and skill needs analysis should be developed.

All of the countries apart from Georgia have implemented some active labour market measures, but the number of beneficiaries is extremely low. In order to prevent long-term unemployment, maintain employability and foster reintegration of unemployed back into the labour market, a considerable increase of funds available for active employment measures combined with an improved design and targeting, and strengthening the capacities of employment services are crucial. This applies to job creation measures, particularly the promotion of a business-friendly environment for SMEs, but also to measures targeted at the supply side of the labour market, and here in particular to the most vulnerable groups such as women, elderly and youth. The strengthening of capacities for measuring the impact of active labour market measures is critical in view of better design and targeting.

Key challenges with regard to social protection are the rather fragile economic development and the considerable negative impact of the financial and economic crisis on economic growth. In addition, the countries are challenged by substantial territorial disparities. Life expectancy is rather high as compared to other countries in the region, but Armenia and Georgia will be faced with rapidly aging societies. A crucial challenge in the coming years for Azerbaijan and Georgia are further efforts to improve social inclusion of IDPs. With regard to labour market developments, the creation of jobs outside the agricultural sector encompassing decent working conditions remains an important challenge for all three countries. This has to go along with the improvement of quality and relevance of (vocational) education and training of both youth and adults, in order to adequately respond to the changing needs of the economy.

Social Protection Systems

Public spending on social protection programmes in the Southern Caucasus is exceptionally low. While the system inherited general features of the old socialist social protection system, the rather comprehensive level of social protection could not be maintained during transition. Nevertheless, the design of social protection systems in the Southern Caucasus is still strongly determined by its institutional legacies. While policies during the last 20 years mainly aimed to ensure basic protection against poverty, they did not succeed so far in enhancing inclusiveness – a large part of the population working in agriculture or the informal economy are not covered by social insurance programmes. Further, the transition period was accompanied by a considerable growth of the informal sector, which excluded the informally employed from access to contributory social protection benefits. A general trend in all three countries was to replace category-based social protection benefits by means-tested social protection benefits, and in-kind benefits by cash benefits. While many efforts were made to improve targeting mechanisms of social assistance, the modernisation of social protection for the most vulnerable groups of society progressed slowly. The last decade was also characterised by substantial changes with regard to the social protection administration.

Labour markets in all three countries are characterised by a high degree of informality and a large agricultural sector. Although those employed in the agricultural sector in Armenia and in Azerbaijan can contribute on a voluntary basis to the social insurance system, they are not able to do so due to the low level of income. Thus, access to contributory benefits is limited for a large part of the population. The problem is acknowledged in the countries and there are attempts to increase coverage via simplified registration procedures. Nevertheless, there is still a large gap in coverage of social protection systems.

In all three countries combating poverty is considered the main priority of social protection policies. As in many other countries in the region, a substantial re-orientation from universal to targeted non-contributory benefits has taken place. However, the large share of informal employment and new emerging patterns of poverty represent challenges for means-testing and targeting. High poverty rates and scarce public resources made it necessary to identify those among the poor who were particularly vulnerable. Benefits for families and children are a key issue in all three countries. Means-tested social assistance payments to families with children have been introduced in Armenia, Azerbaijan and Georgia. However, with regard to their financial dimension these benefits are far less important than contributory benefits. In all three countries targeting mechanisms are considered effective, meeting a large part of the poor population. In fact, an income-based targeting or proxy means testing represented a considerable shift in the previous policy, which linked benefits to certain categories without need assessment. Nevertheless, key disadvantages of targeting are addressed in the studies as well: reach-out of the benefits, and corruption. Given the limited public resources, there is a debate in the countries whether scarce means should even be more targeted to concentrate the support on those who live in extreme poverty. However, given the very low share of overall spending on social protection policies in the three countries the question should be raised of whether the right course is a more comprehensive and inclusive approach to support those in need and to approach measures which combat the underlying reasons for poverty.

Despite the overwhelming evidence of uncovered needs, funds allocated to this area are still rather low, and the largest share of social protection expenditures is dedicated to pension benefits, which, however, seem to constitute an important income source for poor households. All the countries apart from Georgia have implemented unemployment insurance systems, but the level of benefits is extremely low. Further contributory benefits are sickness cash benefits and maternity benefits. Eligibility to contributory benefits is linked to employment and social contribution payment. In contrast to Armenia and Azerbaijan, where contributory benefits still constitute an important part of the social protection system, in Georgia public social protection benefits have lost their importance and benefits are either universal and tax-financed or private.

Social services are underdeveloped in all three countries and mainly consist in boarding houses and homes for the elderly and disabled. In general, a weak tradition of social work and community-based services could be ascertained. The lack of minimum income provisions and access to quality social services results in insufficient social protection of the most vulnerable. There is a weak development of integrated social services. Social protection is mainly focused on cash benefits. A lack of social service provision is particularly visible in the field of disability policies, which concentrate mainly on cash benefits in the form of disability pensions, but do not provide adequate re-integration and rehabilitation services. A further area where a lack of social services and social work at community level seems to be the reason for a very slow progress is the deinstitutionalisation of children living in homes.

The overall design and supervision of implementing social protection policies in all three countries is the responsibility of the Ministry of Labour. Nevertheless, the three countries have undergone different developments with regard to the institutional set-up and administration of social protection benefits in the last decade. While the semi-autonomous institutions administering social insurance programmes in Armenia and in Georgia have lost financial autonomy and institutional power, the State Social Protection Fund in Azerbaijan has strengthened its position. These institutional changes might also bear some risks. If social protection is administered directly by the government, funding of benefits might be at risk in times of low state revenues. A more decentralised administration of social protection systems including the right to collect funds earmarked for social benefits might be better able to protect social spending in financially difficult times.

The decision to decentralise social protection administration also involves risks and opportunities. While a centralised structure might ensure uniform financing and administrative procedures as well as better statistical monitoring, a more decentralised institutional structure is better able to respond to clients' needs.

International donors have given particular emphasis to support for refugees and IDPs as a consequence of the regional conflicts and have also provided substantial budget support in the context of the post-conflict recovery programmes.

In summary, the former comprehensive social protection systems are fragmented and underfunded. They are characterised by a low coverage of contributory benefits, while social assistance and minimum income provisions do not ensure a decent living for a large part of the vulnerable groups. Key challenges are to make social protection systems more inclusive and to establish more universal minimum income provisions. A further challenge is to develop and upgrade social services.

Poverty and social inclusion

Until 1989, poverty officially did not exist in the Soviet Union as guaranteed employment, a universal system of entitlements as well as consumer subsidies from the state provided food and other basic necessities to almost all of the population. The cornerstone of the Soviet social welfare philosophy was a job guarantee combined with substantial non-cash benefits provided at enterprise level. Furthermore, a formal system of transfer payments provided for retirement or compensated individuals at a disadvantage such as disabled and orphans. Last but not least, due to free health care and education services the Soviet system was characterised by widespread access and high levels of service use.

In the years following the break-up of the Soviet Union, poverty rates and income inequality considerably increased. While definite data on poverty levels at the end of the last millennium are not available, the existing data based on national poverty lines suggests that half of the population in Armenia, Azerbaijan and Georgia lived below the national poverty line in 2001. The reasons for this development are manifold. As a consequence of the enormous decline in GDP, all three countries experienced labour adjustment processes including declining employment rates and a considerable reduction or non-payment of wages. The jobs once guaranteed by the state ceased to exist and private-sector activities could not absorb the losses. Moreover, wages and pensions in real terms eroded due to rapid inflation.

Although it proved possible to reduce absolute poverty considerably in the last decade, a large part of the population of the region is still at risk of poverty and social exclusion. Taking into consideration that comparisons have to be made with caution due to data limitations, it seems that poverty rates are lowest in Azerbaijan and highest in Georgia. Poverty rates are higher in rural than in urban areas, indicating that the dominant subsistence agriculture contributes to the persisting high number of working poor. Furthermore many people, in particular in rural areas, have limited access to basic utilities, social and health services. Inequalities in terms of employment opportunities and access to education are widespread, hindering people from escaping poverty. Last but not least high rates of infant mortality and child poverty give reason for concern.

Several factors have a great effect on whether or not a person is becoming vulnerable to poverty and social exclusion, and therefore it is crucial that the governments address these determinants. The size of households is directly associated with poverty, and larger households tend to have a higher risk of poverty throughout the region. This in particular refers to households with many children and pensioners.

Child poverty is a worrying issue in all three countries. The percentage of persons living in poor households is disproportionately higher for children compared with the whole population and much higher than for pensioners. The country reports from Azerbaijan and Georgia assume that children from IDP households are in a particularly disadvantaged position due to the lack of economic opportunities, access to education, bad housing etc. Besides children, the presence of elderly in a household also increases the incidence of poverty. Throughout the region, unemployed face a significantly higher risk of poverty and exclusion than employed. However, we can also see that being employed does not necessarily prevent poverty and the number of working poor remains high in all three countries. Poverty rates among household heads with higher educational attainments are lower throughout the region.

The majority of IDPs remains poor and vulnerable. Most of them do not have regular and adequate sources of income and are heavily dependent on state transfers. In addition to this, their housing conditions are often still abominable, and last but not least they are not sufficiently integrated into the host societies.

Despite a considerable GDP growth in the 2000s in all three countries, poverty and social exclusion still remains a key challenge for a large part of the population in Southern Caucasus. In particular in Georgia economic growth did not translate into a considerable decrease in poverty. Further to this, low spending in key social policy sectors led to deficits in the different dimensions of human well-being which are reinforcing each other: Due to increasing education costs and out-of pocket payments in health care, the part of the population with low income has limited access to health care and education. In turn, low educational attainments and bad health status diminish the opportunities to get access to employment etc.

Furthermore, employment in all three countries is highly vulnerable due to the high shares of agriculture and small-scale informal activities in total employment. Poverty, material deprivation and social exclusion are widespread in rural areas, and subsistence agriculture in most cases can be considered as hidden unemployment and as a coping strategy against poverty. Besides these regional disparities, some groups face a higher risk of poverty, for example the unemployed, pensioners, families with three or more children, IDPs and other population groups that have a disadvantaged position in the labour market. Again, low level of benefits and low coverage of social assistance and social security schemes contribute to this vulnerability.

Targeted social assistance programmes clearly have mitigated the poverty incidence in all three countries. However, it is also obvious that poverty alleviation programmes need to combine measures in different policy fields such as the economy, employment, education and social protection, as well as combine cash benefits with benefits in kind.

In order to minimise the risk of inter-generational poverty, early childhood support, and other measures which support the education of those at risk of poverty, should be strengthened. The creation of jobs outside the agricultural sector offering decent working conditions is clearly another crucial element in the direction of poverty reduction. Along with this, entrepreneurship should be clearly supported through the abolition of institutional and legal impediments, in particular for SMEs, and combined with training measures for future entrepreneurs.

Further to this, measures to support the (re-)integration of the unemployed into the labour market and to prevent young people from unemployment should be strengthened. In particular, a considerable increase of active employment measures, combined with a comprehensive design and targeting, is recommended. It is important that IDPs as a specially vulnerable group are integrated in the respective employment and educational programmes and gain better access to already partly existing measures such as support for small businesses and professional retraining measures, education vouchers etc..

In conclusion, it is obvious that all three countries should undertake more efforts to address the main determinants of poverty. Due to the fact that low benefits and low coverage of social assistance schemes and social protection schemes could not eradicate extreme poverty, combining them with minimum income schemes should be considered. In particular in rural areas where families lack income in cash, minimum income schemes could contribute to providing access to basic services such as health and education. Besides, in order to address the main determinants of extreme poverty, the introduction of child benefit programmes which include a progressive component and therefore target big households could be another option.

Pensions

Before the split of the Soviet Union, pension systems in Armenia, Azerbaijan and Georgia were designed according to a common "socialist" model. Public pensions generally were pay-as-you-go financed and benefits based on the years of service and the income of the last years before retirement. There were no occupational or private pensions. Benefit entitlement was characterised by low retirement age. Average replacement rates were low and determined by the length of service and the salary during the last 12 months before retirement. Another overall characteristic of the pension systems was the absence of index-linked pensions, leading to a devaluation of pensions over time, especially compared to wage development. In addition, typical elements of the socialist pension system were those providing minimum protection – a minimum pension or flat-rate basic amount. Over the years, because pensions were not index-linked, flat-rate elements overlaid the income-related factor so that a significant number of pensioners were drawing the same amount of pension. The amount of the pension was determined more by the year when the person became a pensioner than by the former working career. Pensions of the same age cohorts were characterised by low differentiation. Although social security systems in socialist countries were employment-based, restricted to the working population, the communist obligation to work, resulting in high labour force participation, meant that pension systems were characterised by a broad coverage similar to universal schemes

Today, pensions in the Southern Caucasus are low and average replacement rates are even lower than those in Belarus, Moldova and Ukraine. The income position of pensioners is a concern throughout the region. Pensions are not sufficient to ensure a decent living and pensioners often depend on family support or are obliged to work in order to survive. The need for pension reforms in the long run is widely acknowledged.

With regard to financial sustainability, the region faces ageing populations due to declining fertility and emigration. Fertility rates are comparatively high in Azerbaijan, but lower and at the same level as other Eastern Partnership countries in Georgia and Armenia. There is, however, a remarkable difference in life expectancy, which is much higher in the Southern Caucasus than Belarus, Moldova and Ukraine or the Baltic States. The old-age dependency

ratio in the Caucasus is expected to increase by 2030 and get close to the EU average. This will put a strain on the financial sustainability of the pension systems, even if replacement rates and the overall share in pension expenditures is low compared to neighbouring countries. In the medium term, the high level of informality of the labour market and low coverage, which result in much higher system dependency ratios, is a matter of concern throughout the region.

Thus, although the current share of pension expenditures in GDP is low, the future financial sustainability is considered as a particular challenge in the region. Pension reforms have responded to ageing societies by increasing the retirement age and the intention to introduce funded elements in the pension system. The challenge of the informal sector and a consequently weak contribution base is acknowledged and attempts have been made to increase formality by lowering taxes and social contributions or, for example, simplified registration procedures for the self-employed. Georgia has opted for a tax-financed pension system and has considerably lowered income taxes, resulting in a universal coverage of the pension system. It remains to be seen whether policies to increase coverage in Armenia and Azerbaijan will succeed in higher coverage rates.

Compared to a number of other CEE countries, where pensioners were rather well protected during the transition phase, the relation of pensions to average wage and national official poverty thresholds in Southern Caucasus illustrates that pensioners are in a weak position. Nevertheless, in particular since 2004 and 2005 pensions have been increased in real terms to close the gap between the poverty line and pensions. In all three countries pension increases have been carried out ad hoc and were not linked to higher pension claims of new pensioners. Thus the income position of pensioners is rather determined by (and vulnerable to) governmental ad hoc decision than by systemic changes in the pension scheme. The inadequacy of pensions is an unsolved issue and is reflected in a comparatively low share of pension expenditures in GDP in all countries. While pension adequacy is considered in the reform concept outlined for Armenia, the envisaged pension reform in Azerbaijan and the current system in Georgia leaves many open questions with regard to the future income situation of pensioners. This in particular refers to the pensions of women. Currently, pensions are more or less the same for men and women, but the gender pay gap is high. Armenia and Azerbaijan consider implementing pension reforms which link pensions to a larger extent to previous earnings. Given the income difference and lower retirement age for women in Azerbaijan, the impact of pension reforms on women needs to be considered in particular. Against the background of pension schemes which refer strongly to previous lifetime earnings, lower retirement ages for women will result in lower pensions.

Access of pensioners to health care is an important aspect when assessing the adequacy of pensions, taking into account the high incidence of poverty among pensioners. In all three countries access to health care is limited and the share of private co-payments is high in international terms. Furthermore, the need for health care often increases with age. With regard to long-term care for the elderly, a social service infrastructure to support those elderly persons who are in need of care seems to be largely absent, and the only form of social support for pensioners appears to be the disability pension. Thus, pensioners are dependent on informal family support in case they are in need of long term care.

The high life expectancy in the region might be a reason why – in contrast to many other CIS countries – the Southern Caucasus countries succeeded in increasing the retirement age. All three countries have increased the retirement age in the last decade. Given the low retirement ages in the ex-Soviet countries and the political difficulties of increasing the retirement age in many Western, Central and Eastern European countries, this political achievement is rather remarkable. The countries of the Southern Caucasus addressed the issue of raising the retirement age earlier than e.g. Belarus, Moldova and Ukraine or the Russian Federation. Still, early retirement options have been comprehensive in the past, often granted as certain privileges or linked to professional groups. These privileges were abolished in Georgia in 1989. In Armenia the existing schemes of long service pensions and privileged pensions are currently under review. An important exit pathway in this respect in

all three countries is the disability pension, which plays a considerable role in Azerbaijan and Armenia. Thus, in order to bring statutory and effective exit ages closer together, it seems that the system of disability pensions needs to be reviewed with regard to its incentives and targeting mechanisms while providing disability pensions to those in real need.

In conclusion, pension systems in the three countries are characterised by low replacement rates and do not ensure a decent living for pensioners. Demographic challenges are considered the main driver of pension reform. Given the low share of pension expenditures in GDP, however, it is questionable whether the main challenge for the Southern Caucasus in the long run is in fact financial sustainability and whether the political discourse gives sufficient attention to adequacy of pensions beyond a mere protection against poverty.

Health care

Armenia, Azerbaijan and Georgia look back to system and institutional uniformity in regard to their health care systems before 1990. The health care system in all three Caucasus countries was organised according to the Soviet Semashko system. The guiding principle of this system was access to universal and free medical services at primary, secondary and tertiary levels of care for the entire population. This tax-financed system was an integral part of the centrally planned state economic system with centralised five-year and annual planning of resources and personnel. The economic and political collapse, partly accompanied by violent conflicts, and a dramatic fall in gross domestic product (GDP) after achieving independence had serious consequences in the already poor state of health of the respective countries' populations.

The health status of the population in all three Caucasian countries was traditionally among the best in the former Soviet Union. The decrease of life expectancy in all three countries for a short period due to armed conflicts has been steadily reversed since 1995 and is high in comparison to Belarus, Moldova and Ukraine. The gender gap in life expectancy at birth in favour of women is about 6 years. Also, infant and maternal mortality rates have been improved considerably in recent years in all three countries. The most common causes of death in all three countries are cardiovascular diseases, respiratory diseases, cancers and tumors and accidents. Tuberculosis has remained a widespread disease. Armenia, Azerbaijan and Georgia belong to the countries with the highest incidence of cases of multidrug-resistant tuberculosis. HIV/AIDS cases and new cases of HIV infection are being registered in all three countries.

In regard to health system performance indicators, all three countries show a low outpatient contact rate. The underdeveloped status of primary health care has its roots in the Soviet era. Primary health care services still provide, in most cases, poor quality. To avoid two visits and payments first to a generalist and then to a specialist, most patients pass over this level of care and self-refer to secondary or tertiary services as the first contact point. In general, consultation of medical services is often delayed or even forgone, and purchasing of medicines is not in all cases affordable due to financial barriers.

The health care systems in all three Caucasian countries are financed by the state budget (general tax revenues), private funds and international/donor aid, while private out-of-pocket payments for health services and pharmaceuticals dominate in all of them. Out-of-pocket payments on health account for approximately 50 to 70 % of total health expenditure in Armenia, Azerbaijan and Georgia. Out-of-pocket payments in Armenia, Azerbaijan and Georgia as the principal payment source reduce the affordability and accessibility of health care services for the majority of the population. As a result many people, particularly the poor and chronically ill, tend to postpone seeking treatment, and often do not have the means to pay for preventive care, either. This fact is reflected in low medical consultation rates. Georgia has one of the lowest annual outpatient and inpatient admission rates in the WHO European Region. The big share of out-of-pocket payments as a poverty trap throws the relevant constitutional principles of universal access to health care services and equity into

question. An appropriate measure to reduce the incidence of out-of-pocket payments could be raising salaries of health personnel on the one hand and broadening the circle of services to be provided as Basis Benefit Package and its receivers on the other hand.

Indeed, there is a big inequity in access to health care in all three countries. Counteracting inequity in the health care system is therefore another main challenge. Inequity is especially visible in access to services, due to differences in provision of health care between urban and rural areas. In addition to rather limited health facilities and services provided in rural areas, these facilities are in most cases subject to unequal funding. However, as already mentioned, the biggest barrier in access to health care remains its private funding in the form of out-of-pocket payments. A further inequality is the coverage of only a small part of the population by national health insurance funds in the case of Georgia.

The course of institutional changes in the health sector differs significantly. While Armenia and Azerbaijan follow a more or less similar course of a public-financed health care system, at least for a part of services, Georgia struck a new path following a nearly totally privatised health care system with national insurance coverage only for the poorest part of the population.

However, the health care system in the Southern Caucasus countries of Armenia, Azerbaijan and Georgia is not considered to have high priority in the allocation of funds across the various sectors of the state budget. Only a small share of the state budget is destined for public health care expenditure, leading to out-of-pocket payments, both formal and informal. This form of health care funding now constitutes a considerable part of the total health care expenditure in all three countries, leaving access to health care services restricted to particular social strata, and to the general populace only when acute treatment is indispensable. All three countries still have to deal with severe underinvestment in secondary and tertiary health care sectors, which results in accelerating decay of buildings and obsolete equipment. There is still a long way to go to achieve acceptability for the family doctor model acting as gatekeeper of further levels of care. In summary, not only the percentage of public health expenditure as a proportion to GDP should be increased, but a systematic vision for health care systems, including health promotion and public awareness approaches, is also required to follow reform efforts already underway.

Although some strict regulations to improve the quality of health care services were introduced during the last two decades in Armenia, Azerbaijan and Georgia, there is little demonstrable success. Overall quality of health care in these three Caucasian countries has remained low, leaving room for discussion as to whether ensuring minimum standards or focusing on quality measures should be first prioritised. In addition, assurance of quality of care goes hand in hand with strengthening patients' rights. Adaptation of health accreditation systems for service providers, continuous further education for health professionals and application of patients' rights in case of medical errors would ensure quality in health care.

In summary, health care systems do not ensure equal access and are characterised by low quality. Public spending on health care is extremely low. The main challenges for the coming years will be to improve population equity and access to health and long-term care services, to improve quality of care and health care delivery, as well as to reduce out-of-pocket payments.