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From Second Economy to Informal Sector: The Russian Labor Market in Transition

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Abstract

The evolution of the labor market in Russia is traced from its socialist antecedents to the emergence of an informal sector somewhat different from that observed in many other countries. In Russia, the informal sector to date has actually offered higher income potential than much employment in the official (state) sector, and thus employment in the informal sector has tended to correlate not with poverty, but with wealth. Thus, the informal sector has an important "safety net" aspect as it offers an alternative source of income. Although scant data preclude in-depth analysis, qualitative indicators are examined in the chapter.

II. Soviet legacy and pre-transition developments

4. The labor market in Russia during the Soviet period could be characterized as a "quasi-market" in that planners were not able to control both labor demand and labor supply, although they were able to influence labor demand more directly. Enterprise managers and individuals displayed considerable ingenuity in evading and subverting the strictures of central planners, and without these pervasive illegal arrangements, the command economy system probably would have collapsed much sooner. Arrangements to evade the plan were so common that term "second economy" is used to denote that both the production side as well as the consumption side (black market exchanges) were involved. The second economy was defined by Grossman (1982) as any activity for direct private gain, and any activities undertaken in recognition of their illegality.

5. Indeed, illegal machinations (such as trading inputs outside the limits in the plan) on the production side were actually essential in permitting enterprises to produce output in the heavily constrained environment produced by the central planning rules. In fact, most so-called "dysfunctional" managerial behavior was tolerated because it enabled managers to actually get output produced.² Although most emphatically a part of the second economy because of their illegality under Soviet law, such behaviors are excluded in this paper because they constituted the normal (if not legal) job duties of the individuals thus employed in the state sector.

6. However, other illegal activities undertaken at state-sector jobs should be considered part of the second economy/informal sector; in particular, the pilfering of material inputs from SOEs, the "theft" of time when used for private gain, and the accepting of bribes in order to fulfill normal job responsibilities (i.e. to change linen in a hospital, to actually sell a good to someone in retail trade). Additionally, the exchange of goods among private individuals for profit was also illegal (but pervasive) under the Soviet system, and such flea markets and informal exchanges among neighbors, etc. comprise part of the second economy/informal sector.

7. The legal labor market was a mixture of market intervention (central planning) and quasi-market arrangements. On the demand side, the number of vacancies was constrained by the annual plan for each enterprise/economic unit.³ The enterprise annual plan specified staffing levels and qualification requirements for positions, and typically the labor component

² The primary example is trading inputs outside of the plan allocations. Most enterprises had one or more staff informally called "expeditors" (tolkach) who arranged such deals, using company time and resources. Barter and cash (from slush funds) were used, as was simply the accumulation or calling in of favors (blat).

³ There were six basic types of economic units in the command economy system: the state owned enterprise or production association (SOE); the state farm (sovkhos); the collective farm (kolkhoz); private plots (called private subsidiary agriculture); cooperatives (re-introduced in the USSR in 1989; somewhat akin to a limited-partnership private business); and both legal individual labor activity (registered artisan, artist, craftsman) and illegal economic activity (the second economy). Annual plans were drawn up for SOEs, state farms, and collective farms.

was based on past precedent and a fairly mechanical application of (in essence) fixed coefficients in the case of increased output requirements. Enterprise managers legally had no decision-making power to increase or decrease staffing.⁴ Aggregate labor demand was thus the sum of individual enterprise requirements as determined by central planners.

8. On the macro level, Gosplan also drew up a labor balance for the entire population to assess whether sources (able-bodied aged adults) approximated uses. Given the differing demographic profiles of the republics, the Central Asian republics were in labor surplus, while the industrialized European republics were in labor shortage. In Russia, labor was relatively short in the Far East, due to the combination of high demand for skilled labor at the Siberian oilfields, and a low population base.

9. Labor supply decisions were not subject to direct control in that individuals were free to leave a job (voluntary quits). However, labor supply was indirectly controlled by central planners in several ways. Arguably the most important legal restriction was the labor book system⁵ in conjunction with the propiska (resident permit) requirement, whereby central planners limited the number of residents in urban areas. Closely related to this was the pervasive shortage of housing. One of the most important non-cash benefits provided to workers by large enterprises was access to enterprise-constructed housing stock. Central planners also indirectly influenced labor supply by controlling the ability of individuals to improve their human capital. The number of places at technical schools, universities, and graduate training was determined by central planners, including the allocation of places among various disciplines.

10. Labor force participation rates were very high for women, partly due to a generous system of maternity grants, benefits, and leave. Jobs had to be kept open for a woman on maternity for at least a year, even though maternity benefits were not necessarily paid in full.⁶

11. Although central planners controlled the labor demand side and substantially influenced supply, labor mobility was quite high, averaging approximately 15 percent annually (Commander, Liberman and Yemtsov 1993). According to official statistics, turnover in industry (comprising the bulk of employment) increased from 12.6 percent in

⁴ Except for the widely reported "Shchekino experiment" in which the managerial staff of a very large chemical enterprise were allowed to shed excess labor.

⁵ All work activity of an individual had to be recorded in a labor book. Since imprisonment (and nature of offense) was also recorded in the labor book, it could be difficult for convicts or political prisoners to find employment after incarceration.

⁶ The maternity benefit system is more fully described in World Bank (1994).

1985 to 14.1 in 1990 and to 14.8 in 1991 (Narkhoz Rossii 1992, p. 130).⁷ This high rate of turnover was partly due to limitations inherent in central planning, which tended to produce a mismatch between actual demand and skills. Skilled labor was in particular demand, and accounted for most mobility decisions.

12. Although enterprises were constrained on staffing by the plan, predictably enough, resourceful enterprise managers were able to manipulate the system to attract skilled laborers even if the plan did not so mandate. The most common illegal practices included manipulation of the skills classification of a particular worker to justify a higher salary, the fictitious retention of low skills individuals on the payroll (after death or retirement) to produce the planned skills mix for the enterprise staff, and the maintenance of a slush fund to pay for "emergency" overtime for borrowed workers in order to meet a plan target. Most of these practices were tolerated by the center because they enabled the enterprise to produce.

13. For this paper, the informal labor market is defined as private plot agriculture plus labor supplied or demanded in the second economy/informal sector.⁸ Due to changes in legislation in 1989-90, some forms of labor activity became legal and thus moved out of the standard definition of the second economy. However, most of these can still be classified as the informal sector (e.g. individual labor activity).

14. Individuals typically interacted with the informal labor market in two major ways: as consumers who purchased or sold scarce items na levo (on the side) and as suppliers of illegal labor. Under the Soviet system, individuals were not free to sell their labor services to the highest bidder. Work was viewed as both a right and a privilege, and individuals who could not demonstrate that they were rightfully employed were subject to being charged with the crime of social parasitism. Legal constraints meant that individuals were not free to moonlight nor were they able to start their own businesses or to be self-employed (until 1989). The primary exception to the general prohibition against self-employment was the existence of private plots (see below) of agricultural land.

15. The most widespread form of illegal labor occurred in the construction industry, where crews would work on private housing construction (on private plots or for groups of urban dwellers who banded together to build a cooperative (i.e. private) apartment house) on the weekends and evenings. These illegal construction workers were called shabashniki (from the vernacular for "sabbath" as relaxation/free time).

⁷ For construction, corresponding percents were 18.6, 17.9 and 19.0 in 1985, 1990, and 1991 respectively. For automobile transport workers, corresponding data were 16.4, 16.2, and 17.7 percent. For water transport workers, data were 18.1, 15.2, and 16.9 percent respectively (Narkhoz Rossii 1992, p. 74). In 1991, industry accounted for 30.4 percent of total employment, construction comprised 11.5 and "material sphere" combined with non-material sphere transport and communication totaled 7.8 percent of employment (World Bank. Statistical Handbook 1993, p. 508). Data for labor turnover in industry only are presented as economy-average turnover in Standing (1994).

⁸ Labor services used by enterprises to exchange inputs outside of the plan limits (the tolkach) are excluded.

16. Other forms of illegal labor were piece-work, repairs, tutoring, private practice medicine, poaching, moonshine, handicrafts, etc. In general, individuals were permitted to undertake most of these activities as long as they were not paid for their labor services or were specially registered with the authorities. Legal reform in 1986-88 ("Law on Individual Labor Activity"), ("Law on Cooperatives"), and in 1990-91 ("Law on Enterprises," "Fundamentals of Employment Legislation") meant that individuals became much less restricted in terms of moonlighting, self-employment, and providing labor services for remuneration. In particular, the 1986 "Law on Cooperatives" meant that individuals for the first time since the New Economic Policy (1921-1928) had the right to start up private businesses.⁹

17. This burst of legislative liberalization led to what some observers termed a "new Soviet labour market" (Standing 1991) as individuals had far greater scope for private activity. In particular, activity in private cooperative businesses mushroomed (Table 1). These "producers' cooperatives" were intended to be either the full-time employment of staff, or moonlighting/part-time employment. Under the original legislation, a person with a full-time state sector job was limited to membership in only one producers' cooperative. Because so many people chose to moonlight, employment estimates for cooperatives are problematic. World Bank figures for Russia exclude dual-job holders (Statistical Handbook 1993), and are based on revised official statistics.¹⁰ Also, there was anecdotal evidence of under-reporting of cooperative employment, and the substitution of family members as registered workers in place of the actual moonlighter. Although increasing rapidly from a base of zero, cooperative employment remained low, at less than 4 percent of the labor force.¹¹

18. Once the illegal but "normal" activities of enterprise managers and staff to procure inputs, etc. are excluded, the most important sector for the informal labor market was agriculture until the advent of cooperatives (private business) in 1987. Until a change in legislation in 1992, Russian agriculture was divided into state farms, collective farms, interbranch agricultural organizations, and private subsidiary agriculture. Private subsidiary

⁹ These were in essence limited partnership private businesses, but were termed "producers' cooperatives" for semantic considerations as private business was considered too radical a term at the time. Typically, the adjective "producers'" was dropped. Confusingly enough, state retail trade outlets in rural areas were also called cooperatives--"buyers' cooperatives"--but these were not private businesses.

¹⁰ Previous official statistics included dual-job holders (moonlighters).

¹¹ This is an approximation due to the uncertainty of cooperative employment figures (which may include double-counting due to moonlighters) and due to the absence of the "labor force" concept in Soviet statistics. Soviet statisticians used the definition "labor resources" to encompass employment, students, religious workers, homemakers, military personnel, and the unemployed (Heleniak 1990). The latter were assumed to be negligible until 1992. To approximate labor force, religious workers were added to total employment and unemployment was ignored.

agriculture was the term used to describe private plot activity.¹² The Bank has estimated that about 1.5 percent of total full-time employment in 1991 consisted of people who were registered as working full-time on their private plot. This figure does not include estimates of labor time (person-years) spent on private plot activities, which were considerable.

III. Transition period

19. During the transition period (December 1991 to present), the scope of the informal sector widened as many activities formerly regarded as illegal (second economy) became either more legitimized or simply more overt, while increases in taxation, particularly due to foreign exchange taxation and income tax "bracket creep" caused by high inflation, created incentives for more private and newly privatized businesses to join the traditional informal sector via tax evasion.

A. Context

1. Agricultural Reform

20. Land reform and agricultural reorganization transformed this system more on paper than in reality; "according to a presidential decree of December 1991, farms were required to register by the end of 1992 as limited liability partnerships, open or closed joint stock companies, agricultural producers' cooperatives, or associations of peasant farms" (Brooks and Lerman 1994). Subsequently, farms were permitted to re-register as "new charter" collective farms, and by end-1992, 78 percent of large-scale socialized farms had complied with the registration requirement. However, 90 percent of agricultural land remained in collective ownership, but in some areas, the concentration of private farms is large enough to begin to have some impact on local markets (Brooks and Lerman 1994). Of the 10 percent of land in private ownership at the end of 1992, 3.9 percent was in private family farms averaging 43 hectares, with the remainder in private plots averaging 0.28 hectares.

2. Commercial legislation and crime

21. By 1992, new forms of business organization had become widespread, with joint-ventures, joint-stock companies, commodity and stock exchanges (*birzhi*), semi-private, and newly privatized companies competing with the (by this point) "old" private cooperatives. Registered employment in cooperatives declined by an estimated 40 percent from January to July 1992 (Commander, Liberman and Yemtsov 1993), and the number of registered cooperatives sharply decreased from 134,594 at the beginning of 1991 to 74,377 on 1 January 1992 (*Narkhoz Rossii 1992*, p. 74). State sector employment decreased slightly from 1986 to 1990, with especially large declines in 1991-93 (approximately 10, 13.8, and

¹² Workers of state farms and workers and employees of industrial and other enterprises also had a right to a small private plot, albeit at sizes less than those allocated to collective farmers. In urban areas, plots were typically allocated outside of city limits and people would often build a summer house (*dacha*) on their land.

13.5 percent respectively) as shown in Table 1.

22. With the breakup of the Soviet Union in December 1991, the scope of the informal sector as well as crime and corruption greatly increased. Indeed, given the current legislative confusion, most private, privatized, and joint-venture companies conduct daily operations in "grey areas" of business law. First, the bankruptcy law is still not in force although it was signed by President Yeltsin in November 1992. To date, very few Russian SOEs have been declared bankrupt.¹³ This means that private businesses and individuals have no real recourse against debtors. Contract law (including provisions to ensure that contract obligations are honored) is to be regulated under the civil code (parts one and two). The first part of the civil code has been drafted and approved within the Russian government, and was submitted to Parliament in December 1993. The second part of the civil code, which covers different types of commercial transactions, is still being worked on within the government and will eventually be submitted to Parliament.

23. As a result of this legislative vacuum, and due to a general weakening of central control, Russia has experienced an explosion of criminal activity, with the mafia alleged to play a leading role in privatization of services in major cities.¹⁴ Corruption was always a characteristic of the command economy system,¹⁵ and prior to 1985, it was estimated that 30 percent of a government functionary's salary came from bribes (Sterling forthcoming, in Transition). Corruption widened in the pre-transition period, with the share of bribes in a government functionary's salary increasing to 50 percent (Sterling, forthcoming).

24. After years of official silence or denial, in 1990, the first official estimate of incomes accruing to the second economy in the USSR was published in an official statistical yearbook--rub 56.5 billion in 1989 (Sotsial'noye razvitiye SSSR 1990, p. 121). Non-official sources put the figure much higher, e.g. 150 billion rubles or 20-25 percent of USSR national income (Nash Sovremennik 1990). This compares with an estimated 17-18 million people involved in the second economy in the USSR, or 13 percent of total (legal) employment (approximately 6 percent of the USSR population) (cited in Samorodov 1991). Arguably, the second economy has increased in size, but estimates remain quite imprecise. For example, in 1991, Sterling suggested that the size of the second economy was 25 percent of GDP (which is simply the upper bound of the Nash Sovremennik figure), increasing to "one-third to one-half" of national income in 1992. For 1992, Oxford Analytica estimated that the organized crime component of the second economy comprised rub 130-150 billion,

¹³ Instead, inter-enterprise arrears continue to accrue.

¹⁴ Sterling, forthcoming, as excerpted in Transition, April 1994.

¹⁵ With especially major corruption scandals occurring during the Brezhnev years (e.g. cotton in Uzbekistan, gold misappropriation from Central Asia). Indeed, Yuri Andropov's major focus was an anti-corruption drive, which was diluted but continued by Gorbachev.

which is less than one percent of 1992 GDP (rub 18,063 billion).¹⁶ However, the Ministry of Security and the Ministry of Internal Affairs were reported to predict in 1992 that the mafia would control 40 percent of GDP "in the near future" ("Mafia", FBIS-USR-92-158).

25. A major challenge to measuring the scope of the second economy has been the rise of criminal gangs and a pronounced change in the nature of illegal transactions. Prior to 1991, most of the second economy "crimes" were more in the nature of exchanges of goods and services between individuals, but by 1992, major organized crime operations such as counterfeiting had become prominent (Box 1), and financing/banking crimes had emerged. In particular, rules on the use of foreign currency were often illegally abrogated, and loans were extended when recipients clearly did not meet eligibility requirements.

Second Economy 1989: (in billions of rubles)	
Illegal side earnings	14.6
Theft of state property	4.9
Moonshine vodka	23.0
Illegal resale profits	10.3
Illegal wage payments	0.1
Personal income tax evasion	1.4
Bribery	1.0
Narcotics, prostitution & smuggling	1.0
Poaching, timber theft, misc.	0.2
Total	56.2

Economic Crime in First 9 months of 1993

Theft	48,329
Thefts by misuse of job position	30,742
Thefts by swindling	4,115
Bribery	3,654
Violation of foreign currency rules	4,480
Illegal trading	3,425
Counterfeiting	3,651
Total Economic Crimes	86,214

Sources: Sotsial'noye razvitiye SSSR. 1990. p. 121 and "Economic Crime..." FBIS-USR-93-142.

26. Not all second economy incomes are due to organized crime; the

1. Changing Definitions of the Second Economy

Goskomstat USSR estimate delineates private sales of stolen gasoline, poaching, and pilfering from state enterprises as well as narcotics and prostitution. In general, the service sector of large cities is heavily controlled by the mafia in the sense that service providers must give over a monthly payoff of protection money to ensure that restaurants are not set on fire, kiosks not upset, customers not intimidated, etc.

27. The term "mafia" in Russian is used loosely to denote not only organized crime, but

¹⁶ This estimate is clearly too low.

official corruption and favoritism (Oxford Analytica, May 26, 1994 and April 6, 1993). Although the urban service sector remains a primary activity of organized Russian crime, recent Western and Russian press reports suggest widespread diversification into international drug running and counterfeiting. Counterfeiting of bank avisos and checks amounted to rub 300 billion in 1992, with so many of the counterfeit avisos originating in the Chechen republic that these fake certificates are called "Chechen money" (Oxford Analytica, May 17, 1993).

28. Mafia assassinations have become so blatant that mafia activity has been widely reported in the Western press. Contract killings became a focus of concern in 1993 when 10 directors of commercial banks (mostly in St. Petersburg) were executed by the mafia, and the Moscow stock exchange was closed for a day to commemorate the latest slaying (Washington Post, December 7, 1993). The total number of contract killings was reported to have increased from 100 in 1992 to 250 in 1993 (Oxford Analytica, May 26, 1994).

29. Bribery and corruption have grown markedly during the transition, and Yeltsin launched a major investigation into corruption in 1993 (commission headed by N.I. Makarov, deputy prosecutor general). The corruption probe was entangled with politics, and actually emerged in response to critics of Yeltsin who had accused him of corruption (Oxford Analytica, August 24, 1993). Major focus of concerns about corruption have been the illegal export of raw materials (particularly petroleum and nonferrous metals, and banking and financial crime (illegal capital flight, illegal lending, and illegal foreign currency operations). The Makarov commission focussed on illegal export activities and made a preliminary report in June, and followed this was a comprehensive report in September ("Makarov Commission Report" FBIS-USR-93-122). The Makarov commission cited estimates of the Ministry of Foreign Economic Relations that exceptions to export taxes amounted to US \$ 2.2 billion, and the Commission suggested that most exceptions were granted illegally. The corruption allegations were displayed prominently in Yeltsin's decision to remove Vice President Aleksandr Rutskoy from office in September 1993 (Oxford Analytica, September 2, 1993).

30. Bribery and corruption are a particular problem for the economy, though, on less exalted political levels. By increasing the cost of business, they present a special burden to entrepreneurs and contribute to the "gray areas" of the informal sector in which entrepreneurs must operate. Bribery and corruption are concentrated in urban areas, with certain economic regions of Russia experiencing higher rates of bribery than others (notably Moscow in the central region and the north Caucasus and Volga areas; Box 2). Private sector manufacturers in St. Petersburg viewed bribes to obtain loans or discounts as a normal cost of doing business (Webster and Charap 1994). This raises an interesting definitional and psychological question. Technically, entrepreneurs who remit their taxes faithfully and who abjure from bribes or payoffs to criminal gangs should be considered as part of the formal private sector. However, anecdotal and survey evidence overwhelmingly suggest that very few, if any, private sector entrepreneurs can evade payment of bribes or protection money. In Moscow, owners of private kiosks could expect to pay the local mafia group (the city is divided into areas of influence for approximately 20 gangs) protection money of US \$50

Russian criminologists make a distinction between crimes in office, the abuse of official position, and bribery. Crimes in office and abuse of official position comprise theft through misappropriation, falsification of records, or other means, and bribes are said to precede or follow such thefts.

Regional Distribution of Crimes of Officials & Bribes

	Total Crimes	Bribes	Percent Increase*
Northern	586	132	25.7
Northwestern	535	174	22.5
Central	2,045	707	24.9
Volga-Vyatka	478	174	40.3
Central Chernozem	703	235	54.6
Volga	1,017	370	45.1
Northern Caucasus	1,458	498	33.9
Urals	1,253	344	30.3
Western Siberia	1,383	356	33.3
Eastern Siberia	528	115	42.0
Far Eastern	691	148	5.0

Source: "Economic Crime..." FBIS-USR-93-142.

2. Regional Distribution of Bribes, First Nine Months of 1993

monthly, and US \$30 of this sum is said to be funneled by the mafia to local officials as bribes (Oxford Analytica April 6, 1993).

31. Given that private sector businesses do not appear to be able to avoid some illegal activities in order to operate, can a formal private sector actually be distinguished from the informal sector in Russia? Certainly, popular perceptions do not draw a distinction between illegal informal activities. "Indeed, many Russian citizens assume that anyone who appears to be wealthier than average is involved in illegal dealings" (Oxford Analytica, May 26, 1994). Actually, hostility to private wealth and the equating of it with criminality is an extremely old manifestation in the Russian collective consciousness, dating back to well before the Revolution (Braithwaite 1990), but recent growth in crime and corruption (and lack of commercial legislation) have given greater impetus to this characterization.

B. Trends in the informal labor market

32. The lack of official data on employment and the informal sector and the unsuitability of the RLMS or the World Bank enterprise surveys to provide detailed information on the informal sector has meant that estimates of the informal labor market are unobtainable.

Some qualitative information from the RLMS can be used to characterize the informal sector, but the low level of reported informal sector activity raises some questions about the willingness of respondents to be fully candid when describing activities that were considered to be illegal for so many years (recent changes in proposed legislation notwithstanding, considering the incompleteness of legislative reform).

33. Corruption and crime complicate the characterization of the informal sector in Russia, and make obtaining accurate data even more problematic. For example, even surveys conducted with the help of foreign technical assistance can fail to surmount the stigma and fear attached to informal activities. In the RLMS, only 315 out of 13,356 individuals aged 14 or above (2.3 percent) answered affirmatively to a very broadly worded question about individual economic activity. The question included working on a private agricultural plot as well as operating a private taxi, etc. as examples of private economic activity. However, 60 percent of all households stated they had access to private land, and 58 percent of households provided ruble estimates of in-kind or marketed earnings from private plot production, while private plots have been a legal aspect of Soviet agriculture since collectivization (1929).

34. Other surveys have estimated even higher participation in private plot activities. For example, individuals who either grow their own food directly or help friends or relatives comprised 72 percent of survey respondents in Russian cities, while 29 percent of Russian urban residents were reported as spending several hours a day growing food (Rose and Tikhomirov 1993).

35. Participation in 1993 in the informal sector (defined as "monetized and uncivil unofficial economies") was estimated at 27 percent of survey respondents "working in the second economy" and 35 percent receiving payments due to tips or connections (Rose 1994, Table 2). Most (81 percent) of the respondents reported spending time growing their own food or doing their own repairs.¹⁷ Additionally, 37 percent reported the exchange of free favors and 27 percent regularly provided free help to friends and relatives.

36. It is difficult to interpret the differences among these various surveys. The "New Russian Barometer" is a short and broadly gauged survey, with special focus on public opinion questions. Perhaps respondents were more likely to feel comfortable admitting to informal activities to a public opinion pollster than to the Russian Goskomstat interviewers. On the other hand, some of the results from the "New Russian Barometer" seem to be a bit extreme. For example, Rose and McAllister (1993, p. 27) find that money income "does not influence a family's ability to get by" because the estimated coefficient for money income is not significant. There are a number of questions raised by the specification.¹⁸ First, "getting by" is not clearly defined in Rose and McAllister (1993), but may consist of

¹⁷ However, in Rose and McAllister (1993) this share is reported to be only 51 percent.

¹⁸ For example, it appears that only one regression was run and the reported adjusted R squared was only 0.02. It seems that further work on the model specification would be in order.

response "never," "rarely" and/or "often" to a set of questions about doing without items such as heating, food, medical treatment, etc. (Rose 1994). Second, other "standard" influences on household welfare are also found to be insignificant; namely the presence of children in the household, the household size, age of household members, marital status, location, or educational attainment. About the only typical influence found to be significant is whether the respondent was male, and the number employed in the household. Since the number employed in the household was found to be significantly correlated with getting by, but money income was not, further work on the model's specification is in order.

37. Of the 8,069 jobholders in the RLMS sample, only 3.4 percent (276) admitted to holding a second job (moonlighting), even though this has been legal since 1991.¹⁹ On the other hand, in a different survey, Russian enterprises polled estimated that 20 percent of their labor force had secondary private sector jobs (not necessarily informal sector jobs; Commander, McHale and Yemtsov 1993). Approximately 22 percent of the workforce of surveyed enterprises worked at primary jobs in "newly privatizing" firms, with 10 percent classified as private sector, defined to comprise the "old" private sector (cooperatives) and newly created private businesses (Command, McHale and Yemtsov 1993).

38. An estimate of the number of secondary job holders (moonlighters) could help shed light on the fact that official unemployment has remained low. Open unemployment in Russia has been limited by a variety of factors: the cumbersome unemployment registration process; the unwillingness of firms to shed labor for a variety of factors (soft budget constraints, forward expectations of either future bailouts, increased production or both, persistence of traditional rigidities due to production technology and social consciousness of enterprise managers); and the use of real wage cuts, short-time, and wage arrears to adjust wages instead of employment as a response to severe output declines. Registered unemployment figures are presented in Table 2, and it should be noted that approximately 70 percent of the registered unemployed are women.

39. The official unemployment rate is based on only those registered as such by the Russian employment service, although Goskomstat Rossii has recently begun publication of a "potential unemployment rate." RLMS survey information revealed that the actual unemployment rate was approximately 6 percent²⁰ while the Bank's enterprise survey in Moscow suggested an unemployment rate of 5-6 percent in mid-1993 (Commander, McHale and Yemtsov 1993).

40. Estimates of the numbers of workers on short-time (i.e. reduced hours in a working day or week) and of the number of workers on forced vacation are shown in Table 3. Workers on short-time receive less pay than the normal salary because of their reduced

¹⁹ In 1991, 3.5 percent of those employed in the state sector were reported to have a secondary job (but the basis of this figures is unclear; Commander, Liberman and Yemtsov 1993, p. 29).

²⁰ Calculated by Kalpana Mehra from the Bank's Round One RLMS data set.

hours, while workers on forced "vacation" may receive partial salary or no salary at all.²¹

41. The combination of the registered unemployed, short-time workers, and workers on forced vacation represents a pool of individuals likely to be especially attracted to the informal sector, or to already be working in it. On January 1, 1994, this pool totaled nearly 7 million people and was comprised of 989,500 registered unemployed; 1,070,800 workers on short-time; and 4,858,200 million on forced vacations.²² Goskomstat Rossii calculations suggested that the pool was wider in March 1994, with 4.4 million categorized as actively looking for work (i.e. "unemployed according to ILO standards") and another 4.4 million underemployed (presumably on short-time or forced vacations) for a "potential" unemployment rate of 11.7 percent (March 1994 statistical bulletin, p. 76).²³

42. Such an unemployment/underemployment based concept excludes moonlighters, which could range from 3 percent to 20 percent of registered employment,²⁴ as well as those employed full-time on private plots and, increasingly, in private farms and in private business.²⁵ Estimating private plot employment was always difficult, and with the proliferation of legal private farms, has become even more problematic in the absence of official statistics. Private business statistics are very difficult to assess due to ambiguities in the use of the term "private" which can just as readily designate a large state-owned enterprise undergoing privatization as well as a new business formed by local venture capital. "(Labour) flows into and out of the private sector remain something of a black box" (Commander, McHale and Yemstov 1993, p. 20).

43. An increasing problem for primary job holders (and their dependents) is the inability of state-owned enterprises to actually pay wages. Financially pressed enterprises have

²¹ Information is not published on the breakdown between partially-paid and non-paid workers on forced vacations. The standard table of short-time and forced-vacation workers was not included in either the February or March 1994 statistical bulletin.

²² The data on forced vacations are an estimate based on official information provided for person-days and the average length of vacation.

²³ Goskomstat Rossii relied on the old definition of "labor resources" in the derivation of this figure (proceeding from the active-age population and subtracting full-time employed). This is not the ILO methodology in that it includes full-time students, who would normally be excluded from the labor force regardless of how much they expressed an active job search. The treatment of homemakers and the uniformed military is also unclear.

²⁴ Moonlighting could be much greater or less than these limits drawn from two very different survey pools. In particular, the 20 percent figure is based on an enterprise survey and clearly those on short-time or forced vacation are much more likely to hold an additional job.

²⁵ Preliminary survey data do not illuminate this issue much. Of the 8,069 respondents in round one of the RLMS who stated they had a full-time job, only 3.7 percent identified the ownership of their workplace as "private individuals." Of the 276 respondents who admitted to holding a secondary job (3.4 percent of full-time job holders), 21 percent (58 individuals) worked in private business for their second job.

increasingly resorted to the accumulation of wage arrears (Table 4) by delaying salary payments. Wage arrears represent amounts owed to workers, and obviously suggest an incentive for workers to take on secondary jobs in the informal sector.

44. With these caveats in mind, it is suggested that the number of people potentially involved in the informal sector ranges from 8 to 10 million, or approximately 13 percent of able-bodied aged adults. Actual involvement could be either less (to the extent all unemployed or underemployed individuals would be willing to work in the informal sector) or more (to the extent that no allowance has been made for outright criminal activity).

45. The informal sector has the potential to provide an important safety net function as a significant source of additional income. In the RLMS, secondary job holders earned, on average rub 2,038 as compared to primary wages of rub 3,597, or nearly 57 percent of the average wage (Table 5).²⁶ Secondary job earnings tended to be negatively correlated with poverty status; in other words, poor and very poor households were less likely to have access to secondary wage income just as they were much less likely to have access to primary wage income. Profits from entrepreneurial activity (such as ownership or co-ownership of a cooperative) were strongly associated with non-poor status; of the 99 entrepreneurs in the RLMS sample, 87 of them lived in non-poor households. Thus, the private sector provided a route to wealth, and not merely a safety net function in the RLMS sample.²⁷

46. One surprising result from the RLMS is that women entrepreneurs have a higher mean profit level than men, indicating the heterogeneity of the informal sector.²⁸ A study of private sector manufacturing entrepreneurs in the St. Petersburg area did not have the high proportion of females noted in the RLMS, with only one female entrepreneur identified (Webster and Charap 1994). Lawlessness and corruption were deemed to be major problems for the St. Petersburg entrepreneurs. "Illegal practices were rampant and costly. Bribes reportedly were required to obtain leases, lower raw material prices and lock in contracts" (Webster and Charap 1994, p. 5). However, the entrepreneurs in this sample were spared the worst of mafia attention because they were involved in manufacturing, and the mafia was reported to be interested mainly in trading companies.

47. Women appear to be at a significant disadvantage in some other aspects of the informal sector. Women's wages in secondary employment and women's earnings from individual

²⁶ Caveat. These sections are based on the uncleaned round one with the UNC created variables. The figures presented in Table 5 and in text ff. may vary slightly once the programs are rerun on the cleaned data.

²⁷ The RLMS survey instrument (questionnaire) does not provide detailed questions about entrepreneurial activity that would enable one to determine whether the activity occurred in the informal sector (e.g. a business evading taxes) or in the legalized private sector (in a fully law-abiding cooperative). Thus, entrepreneurial activity in the RLMS has been lumped into the informal sector without making this important distinction.

²⁸ Entrepreneurs in the RLMS sample may be in the traditional informal sector or they may be legally registered (and tax-remitting) owners of cooperative or other private businesses. The RLMS data do not allow for discrimination.

labor activity were less than half of men's, while their formal sector (primary job) earnings were approximately 63 percent of men's (Table 5).

48. Individual labor activity ranges across activities with very low levels of remuneration (e.g. piece-work) and some activities with high levels of income (e.g. private medical services, or using a private automobile as a taxi in a major metropolitan area). Men involved in individual labor activity tend to live in non-poor households (70 percent), while women involved in individual labor activity tend to live in poor or very poor households (43 percent).

Trends and prognosis

49. The RLMS results suggest a possible trend in the development of the informal sector in Russia. With the elimination of legal barriers against private business, early entrants into the "cooperative" sector were able to earn high incomes in secondary jobs. To some extent, the growth of crime and corruption has eroded potential profits, but returns remained very high relative to state sector employment for successful entrepreneurs. The "high tech" or "highly connected" private businesses in the informal sector are likely to remain a source of high income, until legislative reform has advanced enough to clearly move most private businesses out of the "gray areas" of the system. Additionally, services are likely to be a growth sector in Russia (Easterly, deMelo and Ofur 1993), presenting more opportunities for the private/informal sector. At the same time, some types of informal sector employment is clearly associated with low income levels. As structural reform continues in Russia, the informal sector may become more bifurcated, and the low returns to low human capital segment may very well increase in scope, especially when open unemployment becomes more widespread.

50. This dual aspect of the informal sector is likely to have a differential impact on women and men, since women have less time available for secondary employment. Time use tables for the RLMS population demonstrate that women have less time available for both primary and secondary employment than men do because of household and childcare duties, which are disproportionately undertaken by women (Braithwaite and Mehra, forthcoming).

51. However, one aspect of informal sector activity, the private plot, has become even more important in maintaining the real consumption of households. In-kind consumption of private plot output is an important contribution to real consumption in a highly inflationary environment. The presence of a private plot is an important factor in determining a household's poverty status, with plot access correlating strongly with a lower likelihood of poverty (Foley 1994). This "safety net" aspect of the private plot in the informal sector will likely retain its significance until well after macro stability has been attained.

52. Anecdotal evidence suggests that the informal sector is not uniformly distributed across Russia's regions, nor can it be characterized as exclusively urban since it comprises private plots, which are predominately (although not exclusively) a rural phenomenon. In

particular, the North Caucasus oblasts of Russia are said to be regions with particularly active informal sectors, due to cross-border transactions (smuggling) with Armenia, Georgia, and Azerbaijan.

Conclusions

53. The informal sector in Russia is in transition, along with the rest of the economy and society. The slow pace of implementation of legislative reform has led to an environment of high uncertainty for the private and informal sectors. It is actually difficult to differentiate the informal sector from the formal private sector because of the lack of commercial legislation. Without separating the formal private sector from the informal, it can be observed that (formal and informal) private sector activity has to date provided significant returns to those entrepreneurs able to run the gauntlet of obstacles to set up and maintain profitable private businesses.

54. Private plots have become one of the most important hedges against poverty available to non-entrepreneurial households in the highly inflationary Russian economy. Income from secondary jobs has tended to correlate with non-poor status for a household, reflecting the large returns to entrepreneurial activity. In this sense, the informal sector has a safety net aspect in that it has offered additional sources of real income to households.

55. Further evolution of the informal sector into a pattern more like that observed in many developing countries is likely to occur as legislative reforms are implemented. In such a case, a dual informal sector may evolve, with the lower income segment gradually eclipsing the high returns area (which will become formalized and legalized).

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Table 1. Russia: Employment, 1985-93.

	Private Sector (Total) 1/	Cooperatives	Individual Labor Activity	Private Subsidiary Agriculture	Private Farms 2/	Private Businesses 3/	State Sector	Mixed Forms 4/
(In thousands at end of year)								
1985		...	24	714			68,253	
1986		...	26	705			68,570	
1987		67	102	740			68,418	
1988		380	128	900			67,921	
1989		1,171	126	968	0		66,692	
1990	3,856	2,566	128	1,022	7	133	62,198	
1991	4,404	2,489	342	1,078	83	412	55,689	
1992	10,400	2,200	...				48,000	12,800
1993	14,200						41,500	14,400

Source: Goskomstat Rossii, Narkhoz Rossii 1992, Narkhoz Rossii v 1992.

1/ Sum of cooperatives, individual labor activity, private subsidiary agriculture, and private businesses. Data for 1992-93 from Goskomstat Rossii bulletin (No. 12, 1993); no breakdown provided. Data for 1992 calculated as sum of cooperatives plus "individual and entrepreneurial sphere" (from Narkhoz Rossii v 1992, p. 123) equaled 5,700.

2/ New classification due to agricultural reform.

3/ New classification introduced by Goskomstat Rossii w/o explanation (see Statistical Handbook 1993, p. x).

4/ Leased enterprises and semi-privatized enterprises.

Table 3. Russia: Unemployment, 1991-94.

		Job-seekers	Registered unemployment	
		Total	of which:	
			Receiving	
			unemployment	
			benefits	
(In thousands, at end of month)				
1991	June	239.9	...	...
	July	350.5	16.1	1.9
	Aug.	382.6	25.3	4.3
	Sep.	420.9	35.0	5.9
	Oct.	473.7	51.4	7.8
	Nov.	503.9	63.7	9.5
	Dec.	468.5	61.5	11.9
1992	Jan.	484.6	69.0	18.1
	Feb.	554.2	93.1	32.8
	Mar.	615.8	118.2	52.2
	Apr.	696.3	151.0	74.0
	May	742.9	176.5	89.3
	June	779.4	202.9	107.7
	July	842.8	248.0	139.9
	Aug.	886.2	294.2	174.1
	Sep.	921.1	367.1	219.4
	Oct.	982.2	442.4	266.8
	Nov.	1,011.4	518.0	317.2
	Dec.	981.6	577.7	371.3
1993	Jan.	1,028.9	628.4	411.4
	Feb.	1,080.1	692.2	461.1
	Mar.	1,095.8	731.3	496.9
	Apr.	1,100.8	750.6	514.3
	May	1,054.9	740.4	498.8
	June	1,003.2	717.0	470.9
	July	988.6	716.8	460.5
	Aug.	978.8	713.9	456.3
	Sep.	968.6	706.0	449.2
	Oct.	994.2	728.4	461.8
	Nov.	1,055.6	779.2	498.5
	Dec.	1,084.5	835.5	550.4
1994	Jan.	1,164.6	893.6	707.7
	Feb.	1,266.5	989.5	793.6

Source: Goskomstat bulletins.

russhort.xls

Table 3. Russia: Short-Time and Forced Vacations, 1993-94.

	Total	Industry	Transport & Communications	Construction	Science & Scientific Services
(In thousands of workers and employees)					
Short-Time (Incomplete work-day or work-week)					
1-Apr-93	949.5	746.9	34.1	108.0	56.3
1-Jul-93	924.7	771.0	21.9	118.0	10.2
1-Oct-93	1,070.8	897.6	129.5	23.2	20.4
1-Jan-94	1,557.0	1,329.3	138.9	66.6	19.4
(in percent of registered employment)					
1-Apr-93	2.8	3.8	0.7	2.2	3.2
1-Jul-93	2.8	4.0	0.4	2.3	0.6
1-Oct-93	3.3	4.7	2.6	0.5	1.2
1-Jan-94	...	7.2	2.8	1.4	1.2
Forced Vacations					
1-Apr-93	1,907.7	...	...	...	...
1-Jul-93	2,828.9	2,271.9	331.8	159.4	48.0
1-Oct-93	3,681.5	2,987.0	204.3	393.7	80.9
1-Jan-94	4,858.2	3,909.7	275.8	579.2	93.5
(In average days per worker)					
1-Apr-93	...	...	...	...	...
1-Jul-93	...	19.0	15.0	16.0	20.0
1-Oct-93	...	25.0	20.0	17.0	26.0
1-Jan-94	...	31.3	19.6	17.7	30.0

Sources: Goskomstat bulletins and Narkhoz Rossii v 1992, p. 146.

Table 4. Russia: Wage Arrears, 1993-94.

	Total	Industry	Construction	Agriculture
(In billions of rubles, stock at beginning of month)				
1993 Jan	28.8	15.1	7.9	5.8
Feb	43.4	22.0	10.5	10.9
Mar	52.2	26.5	12.5	13.2
Apr	64.3	34.9	13.5	16.0
May	51.4	27.5	11.2	12.7
Jun	101.2	58.8	22.7	19.7
Jul	...	...	...	...
Aug	...	...	...	...
Sep	262.7	130.7	60.1	71.9
Oct	382.0	183.2	77.5	121.4
Nov	583.6	267.1	109.9	206.6
Dec	...	...	...	...
1994 Jan	766.2	364.0	115.2	287.0
Feb	1,681.3	933.6	284.4	463.3
Mar	1,978.5	1,044.2	371.4	562.9
(Index of arrears deflated by CPI [Jan 1993 = 100])				
1993 Jan	100.0	100.0	100.0	100.0
Feb	120.8	116.8	106.6	150.7
Mar	121.0	117.2	105.7	152.0
Apr	125.3	129.7	95.9	154.8
May	84.5	86.2	67.1	103.7
Jun	138.8	153.8	113.5	134.1
Jul	...	...	...	...
Aug	...	...	...	...
Sep	189.9	180.2	158.4	258.1
Oct	231.1	211.4	170.9	364.6
Nov	303.0	264.5	208.0	532.7
Dec	...	...	...	...
1994 Jan	299.9	271.8	164.4	557.9
Feb	594.6	629.7	366.6	813.5
Mar	651.4	655.8	445.8	920.3

Sources: Goskomstat Rossii bulletins and author calculations.

Table 5. Russia: Mean incomes from the RLMS, 1992.

	Total 1/ 2/	Non-poor Households 3/	Poor Households 3/	Very Poor Households 4/	Men	Men Non-poor	Men Poor	Men Very Poor	Women	Women Non-poor	Women Poor	Women Very Poor
Wages 5/												
N	7,838	6,247	1,337	253	3,846	3,070	648	128	3,991	3,177	689	125
mean	3,597	4,083	1,822	968	4,423	5,040	2,155	1,088	2,801	3,159	1,509	845
standard deviation	3,589	3,801	1,477	1,202	4,156	4,362	1,699	1,262	2,714	2,877	1,148	1,129
Secondary job wages												
N	266	233	29	4	139	124	14	1	127	109	15	3
mean	2,038	2,190	1,018	555	2,753	2,951	1,131	870	1,255	1,325	912	450
standard deviation	3,112	3,272	1,173	256	3,943	4,123	1,236	...	1,470	1,520	1,144	180
Individual labor activity												
N	293	184	51	57	131	92	21	18	161	92	30	39
mean	4,109	5,699	1,460	1,406	5,929	7,402	2,453	2,751	2,616	3,996	765	785
standard deviation	10,178	12,402	2,466	3,134	12,577	14,591	3,262	4,491	7,443	9,515	1,390	2,048
Profits 6/												
N	99	87	7	5	62	54	5	3	37	33	2	2
mean	32,603	37,070	0	520	29,909	34,318	0	400	37,116	41,573	0	700
standard deviation	127,833	135,849	0	716	111,516	118,993	0	693	152,904	161,594	0	990

Source: Calculated from round one of the RLMS.

Notes:

- 1/ Total with observations out of the RLMS sample.
- 2/ Defined as households with total income greater than the poverty line (UNC definitions temporarily).
- 3/ Defined as households with total income less than the poverty line, but greater than 50 percent of the poverty line.
- 4/ Defined as households with total income less than 50 percent of the poverty line.
- 5/ After-tax wages of the preceding month (inflation problem to be corrected).
- 6/ Monthly profit of self-declared "entrepreneurs."

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