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**Kyrgyzstan**  
A Case Study of Social Stratification

Vladimir Mikhalev and Georges Heinrich

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A Case Study of Social Stratification

**Vladimir Mikhalev and Georges Heinrich**

September 1999

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## ABSTRACT

Kyrgyzstan is one of the poorer countries undergoing transition from a centrally planned to a market economy. Unlike its neighbour Uzbekistan, Kyrgyzstan followed a rather radical reform strategy, introduced liberal macroeconomic reforms and large-scale privatization. Having laid major foundations for a market economy these reforms have entailed high social costs and profound changes from largely egalitarian social structures to greater inequality and social stratification. Major social consequences of the transition include a decline in living standards for the majority, the appearance of unemployment, radical shifts in distribution of assets, increases in earnings inequality, changes in the welfare system associated with decline in major social benefits. These factors lead to re-ranking of relative income positions and social status of many social and professional groups. One of the most important outcomes has been increasing social distance between the 'winners' and 'losers' of the reforms.

This paper analyses the process of social stratification and the social structure emerging in Kyrgyzstan in the course of transition. Macroeconomic policies, privatization, agrarian reforms and changes in social security regime are considered as determinants of social stratification together with other factors, such as social networks (the role of community and clan relationship), ethnicity, the strength and role of institutions.

This paper further focuses on income inequality and examines transformation of the old and characteristics of the new social classes and groups: the new elite, the middle class and the poor. This analysis is based on original 1993 KPMS and 1997 LSMS data. One of the major conclusions of the study is that the country needs a strong income redistribution policies addressing the very high level of inequality and massive poverty which present a major challenge to successful transition and sustainable development.



# 1 INTRODUCTION

Since the start of the transition to the market, the Central Asian Republic of Kyrgyzstan has cemented its reputation with the international community as a consistently liberal economic reformer and an upholder of democratic government in the southern part of the FSU. Kyrgyzstan is a small country with a population of only 4.6 million people spread out over an area of 199,900 sq. km. It borders with China in the East, Tajikistan in the South, Kazakhstan in the North and Uzbekistan in the West. With a GDP per capita of US\$ 2,250 in 1997 – adjusted for purchasing power parity – Kyrgyzstan falls into the range of the least developed countries.

The evolution of the social structure in Kyrgyzstan under economic transition is determined on the one hand by the common heritage shared with the other Republics of the FSU and, on the other hand by the Asian dimension deeply rooted in the history and oriental culture of the Kyrgyz people. The legacy of over 70 years under Soviet socialism in this Central Asian country coexists with these specific Asian cultural, political, ethnic, and demographic attributes. In this context, the transformation process differs substantially from developments in the European part of the FSU and, even more so, from those in Central Europe. At the same time Kyrgyzstan significantly diverges from South and East Asian societies due to higher industrial potential and human capital than that initially found in China, Korea, India, or Vietnam. Particularly significant were achievements in human development that are characteristic of the FSU. At the point of independence in 1991, most human development indicators in Kyrgyzstan were notably higher than those in countries with comparable levels of GDP per capita (Table 1).

Kyrgyzstan adopted many elements of the transition strategy pursued by Russia. The problems the country encountered in the process of transformation of its 'administrative command system' into a market economy are also in many respects similar. At the same time there are some fundamental differences seen both in economic performance and social development. In a small country like Kyrgyzstan some radical reform measures were easier and quicker to implement than in Russia, which is inherently more difficult to govern because of its sheer size and complex federal-regional relationships. The demographic structure of Kyrgyzstan is also significantly different from Russia and the East European countries: the local population is generally younger, the birth and population growth rates are higher and the average family size is larger.

TABLE 1  
KYRGYZSTAN: HUMAN DEVELOPMENT INDICATORS

	Kyrgyzstan		Developing countries		Industrial countries	
	1990	1995	1990	1995	1990	1995
Life expectancy at birth (years)	68.8	67.9	62.8	62.2	74.5	74.2
Adult literacy rate (%)	93.0	97.0	65.0	70.4	...	98.6
Real per capita GDP (PPP \$)	3,114	1,927	2,170	3,068	14,440	16,337
UNDP human development index	0.689	0.633		0.586		0.911
Annual population growth rate (%)	2.2	1.8	2.3	2.1	0.8	0.7
Crude birth rate	29.1	26.0	30.0	26.1	...	12.6

Source: UNDP, *Human Development Report*, 1993, 1998.

Reforms in Kyrgyzstan are much facilitated by the assistance from international donors who are particularly active in this country considered as more committed to democratic market oriented reforms than its Central Asian neighbours. At the same time Kyrgyzstan is much poorer than Russia and does not possess the same natural riches as nearby Uzbekistan or Kazakhstan. Kyrgyzstan is a mountainous country with a rather small area of arable land. Already at the time of the Soviet Union, it had one of the lowest levels of income per capita of all the republics and was largely dependent on financial transfers from Moscow. The loss of subsidies from the all-union budget exacerbated the severe shock suffered by the local economy after independence in 1991 and consequently resumption and sustainability of economic growth, poverty alleviation and social development were more difficult than elsewhere.

The Kyrgyz Republic represents a particular archetype of economic reform characterized by a radical liberal approach implemented in a Central Asian context. The purpose of this paper is to evaluate the social outcomes of this archetypal reform strategy and to assess its impact on social stratification. Section 2 of the paper provides an overview of the social structure prior to transition. Section 3 discusses key components of economic reform, such as privatization, changes in the labour market, agricultural reform and social

sector adjustment as major factors of social stratification. Section 4 analyses the main features of the evolving social structure and characterizes the social groups on the different levels of the social hierarchy: the upper classes, the middle class and the poor. The final section outlines policy priorities for social integration and social cohesion. The analysis is based on various statistics available from Kyrgyz government sources, the UNDP, IMF and data from the 1993 Kyrgyzstan Multipurpose Poverty Study and the 1997 Living Standards Measurement Survey.<sup>1</sup> To a large extent the observations made here are also based on the personal experience gained by the first author as a World Bank adviser on social policy reform to the Kyrgyz Government in 1997-1998.

## **2 PRE-TRANSITIONAL SOCIAL STRUCTURE**

Like the other Central Asian societies, Kyrgyzstan is predominantly rural with a majority of the local population working in agriculture. At the same time the country has a further specificity distinguishing it from areas of traditionally developed crop cultivation, in the first place Uzbekistan. The indigenous Kyrgyz population was historically occupied in nomadic animal husbandry. This predominant type of economic activity precluded transition to a settled life and impeded the formation of class divisions and government organization. Instead, clan and tribe associations formed the backbone of the social structure. Clan based self-organization served as a means of collective survival under conditions of scarce economic resources – pasture lands and livestock, and the absence of settled communities and common statehood. The strength of tribe kinship was based on the need for collective labour and common use of land, as well as for joint defence

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<sup>1</sup> The Kyrgyz Republic National Committee on Statistics together with World Bank and the Research Triangle Institute of North Carolina have designed and implemented a comprehensive representative survey for measuring the standard of living in the republic. The first survey, the Kyrgyzstan Multipurpose Poverty Survey (KMPS) was carried out in 1993. This effort was followed up starting in spring 1996 by four rounds of the Living Standard Measurement Survey (LSMS) implemented in spring 1996, fall 1996, 1997 and 1998. The survey is based on a representative sample of approximately 2,000 households and a very extensive questionnaire. This enormous source of information on various aspects of economic and social life has yet to be explored in depth by researchers. The analysis in this paper represents one of the first efforts to rigorously examine the 1997 LSMS survey kindly provided by the Kyrgyz National Committee on Statistics. We also acknowledge assistance of the Poverty and Human Resources Division of the World Bank, which kindly provided the 1993 KPMS data.

against outside threats. Due to that clan organization proved sustainable over centuries and helped to preserve ethnic and cultural integrity of the Kyrgyz people (UNDP 1997: 44). At the same time distinctions by origin from different clans rather than social classes or status survived over generations and through seven decades of Soviet socialism.

Thus until the beginning of the twentieth century no apparent social stratification emerged in the Kyrgyz society. No substantial changes in the local social organization occurred with the advent of Russian imperial rule. Changes of a revolutionary nature began from the early years of the Soviet regime. In a uniquely short period of time Kyrgyz nomadic tribes were converted to a settled way of life and forcibly assembled into collective and state farms. Such enforced transformation suppressed their traditional economy and way of life (Zhukov 1996: 125). The Soviet system introduced modern forms of production and increased the regulating role of the state. The country underwent industrialization and urbanization with the bulk of the industrial labour force, technicians and professionals coming from Russia and other Soviet republics. These processes of modernization involved part of the indigenous population, which moved to the cities and engaged in the urban economy. However, no noticeable working class emerged from the Kyrgyz (UNDP 1997: 12). The proliferation of education led to the formation of a national intelligentsia.

Despite a very deep transformation under socialism the Kyrgyz society managed to preserve much more of its traditional features than in other parts of the FSU. Like everywhere in the socialist world it remained an egalitarian society with no clear class distinctions. The majority of the population remained rural and consisted mainly of the Kyrgyz kolkhoz-sovkhoz peasantry, which preserved a great deal of nomadic customs cultivated over generations. Kolkhoz type collective property did not change the traditional nature of property relationships, because the kolkhozy and sovkhozy were in essence clan-based (UNDP 1997: 46). The urban population was largely Russian speaking working class. The composition of government bureaucrats and the intelligentsia was mixed, mainly Russian or other Slavic but also an increasing number of national cadres. As in other Soviet Republics nationality policy provided for a balanced selection of ethnic Kyrgyz to managerial and governmental positions including the top ranks of the nomenclatura. This process affected the formation of the indigenous ethnic elite, which occupied upper levels of government and party structures. It also let traditional clan relationships

and practices extend to the higher levels of social hierarchy and influence the local system of government.

### **3 ECONOMIC TRANSITION**

A strategy to transform the Kyrgyz economy into a market system was adopted in full swing in 1992, immediately after the break-up of the Soviet Union. From the very start the newly independent Republic followed a radical approach to economic restructuring. Kyrgyzstan is widely regarded as the most active and consistent reformer in Central Asia. During the initial stage of the transformation, the government liberalized prices for most goods and services, introduced a national currency (som), eliminated export duties, substantially reduced import tariffs, and removed most capital controls. Structural and institutional reforms included privatization, restructuring of the financial system and the development of market-friendly legislation. By 1998 over half of the industrial sector had been privatized, a two-tiered banking system had been created with new private banks operating in parallel to state banks. The land reform redistributed part of the kolkhos owned lands to private individual farmers. Substantial progress had been made in the area of tax and budgetary reforms (IMF 1998: 5, 6).

Economic and social sector reforms carried out in Kyrgyzstan led to fundamental changes in peoples' lives. The system of centralized planning and subsidization of both producers and consumers was eliminated. Along with the removal of price controls, wages, other incomes, and the majority of economic activities, including foreign investment, were deregulated. The social conditions of the Kyrgyz population changed dramatically: opportunities and incentives for independent economic activities, secondary employment and self-employment were created. The labour force was reallocated to the service, commercial and financial sectors. Private sector educational and public health institutions and other social and cultural services began to emerge.

At the same time the economic and social costs of the transition from plan to market were exacerbated by the disruption of economic links with the rest of the FSU. These difficulties revealed themselves in an unprecedented fall in output and living standards. Real GDP shrunk by 59 per cent between 1991 and 1995, industrial output by over 65 per cent, and agricultural production by over 30 per cent. Inflation initially surged to four

digit levels (Table 2). The collapse in production and high inflation caused a considerable decline in real wages and the appearance of mass unemployment. Real incomes fell by 60 per cent in 1992, 8.2 per cent in 1993, 21.8 per cent in 1994, 11.3 per cent in 1995 and 18 per cent in 1996.

TABLE 2  
KYRGYZSTAN: ECONOMIC INDICATORS

	1991	1992	1993	1994	1995	1996	1997	1990-97
Real per capita GDP (annual percentage change)	-10.3	-16.6	-13.2	-20.2	-6.0	4.7	7.2	-29.7
Consumer price inflation	108.6	920.5	1211.5	278.0	38.9	28.3	...	185261*
Private consumption	-17.6	-42.6	-18.1	-13.2	-16.2	-2.3	-1.8	-63.1*

Source: World Bank. *World Development Indicators, 1999; PlanEcon Review and Outlook for the Former Soviet Republic, September 1997.*

In order to shore up the flagging economy the Kyrgyz government adopted a rigorous package of macroeconomic stabilization measures following recommendations by the international financial institutions. Starting in 1994, these measures yielded successful results in slowing down inflation and stabilizing the national currency. Real GDP started to increase in late 1995 and exhibited steady growth through 1996-1997. The rate of inflation has fallen to a manageable 20 per cent per annum. Yet in 1998 the Kyrgyz economy was affected perniciously by the consequences of the Russian crisis. Economic growth slowed dramatically to only 1.8 per cent. The agricultural sector stagnated and industrial production increased by 4.5 per cent, due only to the output of the Kyrgyz-Canadian gold joint venture.

Stabilization and the resumption of economic growth could not noticeably offset the severe social consequences of the economic crisis of 1991-1995. A 6.3 per cent increase in real incomes in 1997 was wiped out in 1998. Real wages amount to less than one third of their pre-reform level (IMF 1998: 98). The economic difficulties of the population in 1998 were

exacerbated by the spread of massive wage and pension arrears which skyrocketed to 720 million som (about US\$ 24 million).

The radical structural reforms had a profound impact on the social structure. Of the major components of the reform package, privatization, the emergence of a new labour market model, the restructuring of agriculture and changes in the social transfer system had a particularly profound influence on social stratification.

### **3.1 Privatization**

Privatization in Kyrgyzstan essentially followed the Russian model. It proceeded in two distinct stages. The first phase (1992-1993) consisted of the privatization of small enterprises in the consumer services, retail trade, and construction sectors. The State Property Fund was established to manage this process. Several methods were used to transfer property to private owners: leasing, joint-stock company formation, competitive bidding, auction, sales to individuals, and sales to a worker collective (Roberts *et al.*, 1998). Vouchers were distributed to Kyrgyz citizens allowing them to exchange coupons for enterprise shares or housing. Almost one half of public enterprises were privatized in the first stage (about 4,500 in number). However these were mainly small, easier to sell firms, of which 26 per cent were sold directly to the worker collective, 21 per cent to private individuals, 20 per cent through competitive bidding, and 18 per cent were transformed into joint-stock companies (Koichuev 1996: 176). These results were nevertheless widely regarded as unsatisfactory as they were believed to reflect the outcome of a bureaucratic campaign to meet 'plan targets' without due care for its real contents.

In 1994 the government extended the mass privatization programme (MPP) to 1,300 medium and large-scale enterprises. The new programme aimed at a wider distribution of ownership, greater transparency and equity of privatization, stimulating outside ownership and more effective enterprise management. Shares were sold through voucher coupon auctions to the public. Thus individuals and investment funds could convert their coupons into share ownership. By mid-1997 approximately two-thirds of medium and large-scale firms employing about 70 per cent of the industrial work force were sold. Furthermore in 1997, 4 to 15 per cent of shares of large monopolies were offered for sale to the public (IMF 1998: 33). The government retains control through majority ownership in large companies such as in the energy and utilities sectors and the national airline. The

EBRD estimates that by mid-1997 the private sector generated about 60 per cent of GDP – the highest share among Central Asian countries (EBRD 1997, Table 2.1).

Privatization on such a large scale is likely to entail far-reaching distributional consequences since it implies a massive transfer of assets and capital incomes. The ideological thrust behind privatization, as in other transitional economies where it was undertaken on a large scale, was to make everybody a property owner. The real outcome however proved to be very different from how privatization was initially conceived and publicized.

In Kyrgyzstan employees have acquired the majority of privatized capital stock at a symbolically low price: 38 per cent of industry, 78 per cent of construction, and 56 per cent of transportation (Rumer 1996b: 59). However, the distribution of company shares among employee collectives did not turn them into owners of their enterprises. Despite the large number of individuals who became shareholders, the quantity of shares as well as their value is so small that none of the workers were a real property-owner (Koichuev 1996: 181). The actual owners are firm directors and managers who received substantial blocks of shares initially and later on bought out more shares from their employees at bargain prices. Collectivization through voucher sales in essence turned out to be privatization by firm managers. In some particularly profitable enterprises (e.g. fur processing factories) the personal share acquired by management is over 50 per cent while that of the employee collective is negligible (Koichuev 1996: 185). Thus property distribution in such a way worked in favour of a tiny 3 to 7 per cent of the population producing an important, heretofore unknown, source of social inequality (Rumer 1996a).

Further inequalities were exacerbated through the consolidation of economic positions of government bureaucrats in charge of monopolies remaining under government control (a most well known analogue being the Russian Gazprom). In the Kyrgyz case, the incorporation of Kyrgyzenergoholding (electric energy company), Kyrgyzgasmunaizat (gas company), and Kyrgyz aba zholdoru (national airline) into state holdings served the interests of the upper levels of state bureaucracy – the technocratic, financial and administrative elites. It gave them enormous economic power and ways to amass considerable personal wealth. To a certain extent their monopoly positions benefited all enterprises and employees forming parts of the corporation. In general, however, the



change of economic status of large companies under state control contributed to rapidly increasing inequalities.

The distribution of property income is highly skewed in favour of well-to-do households. Fewer than 10 per cent of Kyrgyz households receive positive property income. In 1993, over 70 per cent of the property income went to households in the top half of the expenditure distribution and the top two deciles appropriated over 25 per cent of all property incomes. In 1997, the share of households receiving property income has decreased relative to 1993. The concentration of property incomes among well-off households increased: households in the top half of the expenditure distribution received over 75 per cent of all property incomes. However, a larger share of these property incomes appear to be distributed to medium-wealthy households, the share of property income going to the top two deciles falling to just below 20 per cent. This may be interpreted as evidence for the emergence of an entrepreneurial middle-class.

### **3.2 Changes in the labour market**

With the transition to the market centralized controls over labour, which previously extended from decisions on employment and wage levels to permitted types of activities and their location, ceased to exist. Privatization drastically reduced the number of firms where labour was managed directly by the government. The decline in output led to major reductions in employment and considerable redistribution of labour by sector and type of economic activity. Simultaneously there has been a downward adjustment of real wages and a considerable increase in wage differentials by industry sector and occupation. All these processes have had a profound impact on social structure through changes in employment, occupational and income status of a vast number of people.

During 1991-1995, total employment in the economy decreased by 6 per cent and only began to increase again slowly in 1996. Official unemployment statistics, arguably an unreliable gauge, show rapidly growing unemployment: from 4.1 per cent in 1994 to 7.8 per cent in 1996. Data from the 1997 LSMS, obtained by interviewing respondents and defining as unemployed a person not currently working and seeking employment, yield an unemployment rate of 11.1 per cent, up from 7.1 per cent in the 1993 KMPS. Unemployment in Kyrgyzstan is clearly associated with loss of social status and very often leads to extreme poverty. Since less than half of the unemployed register with the employment services the majority of them are cut off from any kind of social support by the State.

But for the registered unemployed who receive benefits, the assistance is insufficient to protect them from poverty, as the benefit rate does not reach even half of the estimated poverty line.

In reality, job status has changed for a much larger proportion of workers than is reflected in unemployment statistics. Underemployment has become nearly as widespread as open unemployment. Many employers are reluctant to resort to mass lay-offs and workers are unwilling to quit jobs voluntarily, preferring to keep their work record for future pension claims and access to work-related social benefits which were available to them prior to the reforms. As a result workers have to take involuntary unpaid leave or accept shorter working hours, with a corresponding drop in earnings. Hidden underemployment amounts to roughly 9 per cent of all workers in industry (MLSP 1998: 76). Bearing this in mind, recent World Bank estimates put the unemployment rate (including underemployment) at 18 per cent in rural areas and 21 per cent in urban areas (IMF 1998: 12).

Considerable social mobility, both upward and downward, is associated with the changes in employment structure by sector and type of economic activity. Privatization has led to a sizeable reduction in the share of the labour force employed in the public sector and growth in private sector employment. In 1991-1996 the share of public sector employment has declined from 74 to 27.5 per cent. Thus the majority of the Kyrgyz population is now employed outside the public sector. This does not, however, entail automatic change of type of employment, occupation or job status. In fact, privatized firms did not much alter their behaviour. Like their counterparts in state firms, private sector employees also suffer pay reductions. More importantly, the emergence of new private sector firms has social implications: a new social class of entrepreneurs emerges and business activity becomes more widespread.

A large-scale reallocation of labour resources across economic sectors has occurred. The decline of industrial activity has led to a decrease in industrial employment while at the same time, agricultural employment has increased. In 1990-1996 the employment share in industry and construction fell from 27.9 to 14.6 per cent while the share of agriculture increased from 32.6 to 46.8 per cent (Table 3). The expansion of rural economy employment at the expense of the urban industrial sector is a trend characteristic of Central Asia in general, and Uzbekistan and Kazakhstan in particular (Klugman 1998: 67; Klugman and Scott 1997: 130).

TABLE 3  
KYRGYZSTAN: EMPLOYMENT BY SECTOR  
(as per cent of total employment)

	1990	1997
Industry	19.1	10.2
Construction	8.7	3.4
Agriculture	32.6	48.0
Forestry	0.2	0.3
Transport	4.5	3.9
Communications	0.8	0.7
Retail trade & catering	5.0	10.2
Information & computational services	0.3	0.0
Housing & communal services	2.1	1.4
Health & physical welfare services	5.0	6.0
Education	11.0	5.6
Culture & art	5.3	5.0
Science & scientific services	2.0	0.8
Insurance services	0.4	0.4
General administration & defence	2.4	0.5
Other	0.6	3.6
Total employment (in thousand of workers)	1,749.9	1,689.3

Source: IMF (1998: 100); IMF (1999: 91).

The employment share of the consumer service sector has also been expanding from 6.6 per cent in 1990 to 9.3 per cent in 1996. As a result of these reallocations of labour, the industrial working class, which was not very numerous even before the reforms (compared to other Republics in the FSU) shrunk, a process accelerated by the emigration of Russians (and other ethnicities of European origin) which formed the majority of urban industrial workers.<sup>2</sup> Within the industrial sector jobs requiring higher

<sup>2</sup> During the period 1990-1993 net migration to Russia from Kyrgyzstan amounted to 175,400 or 4.1 per cent of the total population and 8.2 per cent of labour force (Zhukov, 1996: 113). Subsequently in 1994-1996 net emigration totalled 81,700 people or another 2 per cent of the population and 4.5 per cent of the labour force. As a result the Russian and other European (in the first place German, Ukrainian and Jewish) population decreased in 1990-1997 from 1,197.2 million to 848,300, or from 27.6 per cent to 18.5 per cent of the total country population. The most massive was emigration of ethnic Russians whose population in Kyrgyzstan decreased by one quarter, from 917,600 to 698,100.

qualification experienced larger cuts. Consequently, the share of highly qualified workers and professionals declined relatively more rapidly than that of workers with fewer qualifications.

An important new development relative to the pre-transition period has been the extensive spread of self-employment. Self-employment embraces farmers, owners of small enterprises, persons engaged in individual economic activity and family workers. This type of (statistically accountable) employment accounted in 1996 for 14 per cent of the economically active population (MLSP 71). This phenomenon is closely interrelated with the informalization of the economy. A majority of the self-employed in Kyrgyzstan represent the subsistence sector, generating very low incomes barely sufficient for survival. Only a small fraction of this group are real entrepreneurs, but even those operate largely in the informal sector. There are an estimated 1 million workers (over half of the economically active population) outside the official employment statistics, consisting of 350,000 agricultural workers, 300,000 in the informal private sector, and 350,000 subsistence farmers (IMF 1998: 12).

In addition to the observed decline in real wages, the de facto collapse of the wage economy and the considerable deterioration of the social position of the employed population, profound changes in wage formation have resulted in extremely diverse wage movements by sector, industry and occupation, contributing to the rise in wage inequality. The most striking phenomenon is that of the very low wages paid in the state budgetary sector, notably in education, research, social, cultural and health care services. The gap between wages in industry, on the one hand, and wages in education, culture, and health care, on the other, increased from 1.5 times in 1990 to 3 times in 1997 (Table 4). At the other extreme, earnings in the banking and insurance sector – a rapidly expanding albeit very underdeveloped area of new private entrepreneurship – are quite high. Salaries there are four times higher than in education or health services and 2.8 times the economy-wide average. The income situation of low paid workers is considerably worsened by massive wage arrears, which persist despite attempts by the government to solve the problem.

Another striking development of the transition is that professionals and engineers (who were traditionally underpaid) have suffered even more. Their wages have fallen to levels which are on average 1.2 to 1.3 times lower than those of low-skilled workers, due particularly to the very low

TABLE 4  
KYRGYZSTAN: AVERAGE WAGES BY ECONOMIC SECTOR  
(as a per cent of total average wage)

	1991	1997
Average wage	100.0	100.0
Industry	122.3	173.8
Agriculture	94.3	54.7
Forestry	59.4	46.6
Transport	97.7	112.5
Communications	106.3	145.5
Construction	120.6	140.6
Trade & communal catering	85.1	77.8
Supplies	...	118.5
Procurement	...	85.7
Computing services	102.0	139.5
Real estate	...	78.7
Commerce	...	118.0
Geology, meteorology	...	169.3
Other sectors of material production	...	76.9
Housing & communal services	80.0	95.8
Health & physical welfare services	76.0	56.6
Education	76.6	61.0
Culture	69.7	57.9
Art	71.4	53.3
Science & scientific services	109.7	114.4
Banking & insurance services	190.3	283.8
Government	112.6	131.5
Minimum monthly wage	43.1	12.1
Average pension	112.3	45.1

Source: IMF (1998 and 1999).

earnings of teachers and medical staff. The majority of professionals are employed in the budgetary sector, which has the lowest pay levels. However, even in the private sector professionals do not earn much more than blue collar workers, reflecting the tradition of underpayment for high skills. Top managers form a group, which has considerably benefited from economic independence, granted by the new status of their enterprises, both state-owned and privatized. Managers' salaries are on average 2.5 to 4 times higher than the wages of their employees.

The generalized erosion of wages has stimulated the emergence of other sources of personal incomes, which have become available with the

development of new forms of economic activity. Statistical information suggests that real per capita money incomes are increasing faster than real wages. The share of wages in overall personal incomes decreased from 55.1 per cent in 1994 to 33.4 per cent in 1997. Wage data does not reflect an accurate picture of the overall income situation since many workers supplement their earnings through secondary employment mainly in the informal sector. It is important to bear in mind that labour compensation in a form other than wages may be underestimated in statistics, as they are very difficult to monitor. Their weight may be even higher than that suggested by the above figures. Furthermore workers often receive substantial additional income from their primary employer, such as payments in-kind which is difficult to quantify but may account for up to 20 per cent of the base wage (IMF 1998: 12).

### **3.3 Agricultural reforms**

Over 65 per cent of the Kyrgyz population live in rural areas most of whom are engaged in farming and animal husbandry. Therefore development of the agricultural sector and agricultural reforms undertaken by the government have a far-reaching impact on the social position of the majority of the population. Kyrgyzstan has embarked on the most radical market-oriented land reform in Central Asia. Beginning 1993, the government distributed long-term land lease contracts, liberalized agricultural prices, and privatized agro-industries. In 1995, land-use rights were distributed for more than half of all the land. Finally in 1998 a new law introduced private land ownership, a revolutionary step for the entire Central Asian region.

In 1996 there were over 38,000 individual farmers holding 13 per cent of the agricultural land, including 33.6 per cent of the total arable land, 9.3 per cent of pastures, 24 per cent of total cattle, 26.4 per cent of sheep and goat herds, 30.9 per cent of horses, 14.1 per cent of poultry and 3.1 per cent of pigs (UNDP 1997: 6). The land that has not been allocated to individual farmers is generally under the control of state or collective farms of various forms. There were 48 state and 673 collective farms in 1997 producing about 17 per cent of total agricultural output. Two thirds of farmers still work at state or collective farms and only one third became individual farmers (IMF 1998: 35). The new private farms faced serious difficulties in obtaining machinery, seeds and fertilizers, as well as access to credit and marketing channels. In addition, most of the individual land holdings distributed are too small for economically viable production. According to LSMS data only 4.6 per cent of rural households have land holdings of over

5 hectares. The size of plots of one third of households ranges between 0.2 and 1 hectare, which is hardly sufficient to produce marketable farm output.

Thus individual farmers produce less than one third of agricultural output. The economic position of larger collective farms however is not much better. The economic crisis had a severe impact on agricultural production and the rural economy as a whole. The agrarian sector lost much of its state subsidies and preferential credits. All farms faced a sharp rise in the prices for equipment, fertilizers, electric energy and fuel and simultaneously acute marketing problems caused by depressed consumer demand and import competition. In some collective farms wages have not been paid for years.

Economic difficulties pushed a substantial number of the rural population into subsistence farming on their household plots (which should be distinguished from farmland distributed to farmers from former collective farms). This subsistence form of production has become the most typical form of activity for the bulk of the rural and a substantial part of the urban population. In 1997, it yielded 54 per cent of all agricultural output. However the amount of income generated by this activity per household is generally so low, that it only allows few rural families to get out of poverty. In 1997, 53 per cent of rural households were poor (Heinrich 1999).

### **3.4 Changes in social transfer system**

The social transfer system has important repercussions for the income positions of an important share of the Kyrgyz population. In 1997, 13.2 per cent of all personal incomes derived from pensions and other social benefits. There are 544,300 pensioners in Kyrgyzstan, or 12 per cent of the population. In addition 829,800 people (18.1 per cent of the population) were receiving means-tested welfare benefits in 1997. Almost the entire population relies on publicly provided education, health care, and subsidies for housing and utilities.

The share of social transfers in GDP in Kyrgyzstan is similar to that prevailing in other transitional economies. Annually, approximately 8 per cent of GDP are spent on pensions and unemployment, medical, disability, and poverty relief benefits. This figure is higher than in developing countries with similar levels of GDP per capita but lower than in East European transition economies. However, as a result of the economic crisis, inflation and budgetary problems, the real value of all social transfers has tumbled and eroded the livelihood of people depending on these benefits.

The high burden social expenditures imposed on the state budget did not leave room for much-needed increases in the level of social protection. The lack of financial resources was exacerbated by poor fiscal discipline and a poor collection record, particularly among the rural populations who, while remaining recipients of the bulk of benefits, have greatly reduced their contributions to the pension system, unemployment insurance and the general tax system.

### **3.5 The rise in inequality**

As already mentioned previously, the pre-transition distribution of incomes in Kyrgyzstan was relatively egalitarian. This changed dramatically following the liberalization of prices and wages, the inflation-induced erosion of real wages and social transfers and the redistribution of assets from privatization. Kyrgyzstan witnessed an unprecedented polarization of incomes and wealth: the spread of mass poverty on the one hand and the concentration of wealth in the hands of a small elite.

The Gini coefficient of household expenditure, which stood at only approximately 0.30 during the pre-transition period 1985-1990 shot up to 0.47 in 1993 (Table 5). This is twice as high as the Gini for the most egalitarian Western economies (e.g., Finland, Norway, and Luxembourg) and also substantially higher than the Gini in the least egalitarian Western societies (USA, United Kingdom) and Russia. In fact, the extent of inequality in Kyrgyzstan is comparable to that prevailing in some developing countries which are known to have the most uneven distributions of income in the world (e.g., Argentina, Philippines). The spending of the very rich households was 15 times higher than that of the poorest households. The poorest 50 per cent in Kyrgyzstan accounted for only 17 per cent of all household expenditures in 1993, while the richest 10 per cent accounted for almost one third of all expenditures. This is evidence for an extremely skewed distribution of resources and deprivation on a large scale for the poorest members of society.

By 1997, the Gini coefficient had fallen to 0.42, still one of the world's highest. There is evidence that the decrease in inequality was mainly driven by an improvement in the situation of the poorest households relative to their better off counterparts while at the same time, wealth became even more concentrated in the hands of the wealthiest. The relative improvement of the situation of households located at the bottom end of the expenditure and income distribution may be attributed to the introduction of the Unified



TABLE 5  
DISTRIBUTION OF HOUSEHOLD EXPENDITURES, 1993-1997

	1993		1997	
	per capita	equivalized <sup>3</sup>	per capita	equivalized
Gini coefficient	0.47	0.46	0.42	0.40
Percentile ratios				
p90/p10	15.3	14.6	6.2	5.7
p75/p25	3.8	3.8	2.7	2.6
Decile shares				
1st	0.72	0.76	2.21	2.67
2nd	2.03	2.16	3.30	3.64
3rd	3.49	3.57	3.47	4.35
4th	4.81	4.95	4.27	4.70
5th	6.26	6.43	5.22	5.95
6th	8.08	8.32	6.67	6.73
7th	10.27	10.39	7.70	8.53
8th	13.43	13.54	10.41	11.06
9th	18.62	18.54	15.18	14.88
10th	32.30	31.44	41.56	37.48

Cash Benefit (UCB) system. Under this programme, a single welfare payment targeted at poor households only replaced several cash transfer payments with wide coverage but poor targeting.

The same factors that account for the initial upward surge in inequality are also responsible for the spread of mass poverty. A small segment of the population amassed considerable wealth through speculative intermediary commercial activities and profiteering from consumer price increases under monopoly conditions and initial scarcity of many goods. The redistribution of the former state property during privatization, large-scale tax evasion especially among the high-income groups engaged in private business activity and, last but not least, the criminalization of many aspects of economic life further contributed to the social stratification. Thus, the fact that the new opportunities offered by the emergence of the market economy were disproportionately seized upon by a select few, in the process leading

<sup>3</sup> Equivalent expenditure is computed as follows:  $eq\_exp = \text{household expenditure} / (\text{nb\_adults} + 0.70 * \text{nb\_children})^{0.90}$ .

to a polarization of the income structure, contributed far more to the rise in poverty in Kyrgyzstan than the fall in GDP. A similar phenomenon has been noticed in the case of Russia (Milanovic 1998: 87-92). Under these conditions of very high income and asset inequality, poverty relief can only be successful if it is placed within a framework of effective income redistribution.

#### **4 EMERGING SOCIAL STRUCTURE**

In this section, information from the 1993 KMPS and the 1997 LSMS is used to assess the determinants of and changes to the social structure in the Republic of Kyrgyzstan during the transition to the market. The 1993 KMPS and the series of LSMS surveys carried out between 1996 and 1998 represent the best available source of information about social change in Kyrgyzstan. However, caveats apply. The recorded income information typically suffers from measurement and recall error. Some income sources, like property incomes, are customarily underreported while income obtained from illegal or semi-legal activities may not be reported at all. For these and other reasons (see Ackland and Falkingham 1997) household expenditure is often preferred to income as a proxy for household wealth. Expenditure exhibits a more stable path over time than income, as households may save or dissave and the expenditure information is adjusted for auto-production and consumption by households, which is not a negligible consideration in the Kyrgyz context. For this reason, the information presented in this section is typically based on expenditure rather than income data.

Despite the greater constancy over time of household expenditure, it may still fluctuate considerably over time, especially in conditions of fundamental economic change. Membership in a certain social class, however, is not only acquired through position in the income distribution but also through the proprietorship of items symbolizing the belonging to this particular class like, for instance, the ownership of real estate and the possession of certain consumer durables. For this reason, a wealth index<sup>4</sup>

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<sup>4</sup> In order to create the wealth index, a subset of questions from the 1993 and 1997 surveys are identified that are typically positively correlated with household wealth. These items include housing quality (e.g., access to hot water, access to an indoor toilet, access to a telephone), possession of durable goods (e.g., car, colour television, video recorder), land ownership, ownership of real estate and ownership of financial

has been created in order to complement the information derived on the basis of the household expenditure data.

Kyrgyzstan started the transition from a relatively egalitarian position but rapidly transformed into a highly polarized and stratified society with limited scope for social mobility. Asked in 1993 whether they expected to be better or worse off during the following twelve months, 23 per cent of households expected to be better off in the future, 39 per cent expected no significant change and 38 per cent expected to be worse off. Strikingly, the uncertainties surrounding the process of fundamental economic and social change appear to have been so pervasive that attitudes towards the future were undifferentiated by social position: similar proportions of rich and poor people expected to be better or worse off in the future.

The capital Bishkek is the centre of economic and commercial activity and the power-base of the Kyrgyz elite. This pre-dominant position was cemented during the transition. Households living in Bishkek are significantly better off than households living elsewhere in the country. In 1993, the average expenditure of Bishkek households was 50 per cent higher than the national average and in 1997 it was a staggering 100 per cent higher. At the same time, the situation in rural areas, home to the bulk of the impoverished population, became more desolate.

The composition of the Kyrgyz elite did not change very much relative to the pre-transition period and some of its members, for reasons outlined earlier, even succeeded in increasing their wealth and consolidating their social status. In addition, education, which previously was bearing little relationship to social status now became an important vehicle of social mobility and an important factor in determining social class (Table 6). Table 6 traces the relationship between household spending and education of the household head. In the first column, the highest degree obtained by the head is described, column two provides the distribution of educational attainment of the head for all households and columns three and four

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instruments and savings (e.g., bonds, stocks, bank account with commercial bank, foreign bank account). A point is awarded to the household for each affirmative answer and the wealth index is simply the unweighted sum of the points scored by each household. The obtained score is then transformed into a five-point index. One may interpret each point on this scale to represent a social group: the deprived, the poor, the middle class, the upper middle class and the elite. Although this measure may be criticized for being too crude, the index provides a faithful predictor of social status and exhibits a high correlation with the expenditure-based social status measures.

TABLE 6  
EDUCATION OF HOUSEHOLD HEAD AND EXPENDITURES, 1993-1997  
(as per cent of total average household expenditure)

1993			
Highest education obtained	frequency	per capita	equivalized
Vocational courses	18.51	108.5	108.1
Vocational school, no diploma	7.59	104.5	103.5
Vocational school, diploma	33.88	92.6	93.4
Technical school	8.66	101.4	101.4
Higher education	31.36	96.1	96.2
1997			
Highest education obtained	frequency	per capita	equivalized
No formal education	11.67	79.4	79.0
Incomplete secondary education	12.32	91.9	90.8
Complete secondary education	34.08	85.9	87.3
Professional/technical school	9.60	99.8	100.1
Technical college ('technikum')	16.41	119.2	118.5
Higher education	15.92	140.7	139.1

contain the relative expenditure levels by education group. In 1993, almost one third of household heads had benefited from higher education. Higher education is not, however, associated with higher levels of household spending. Households with highly educated heads spend, in fact, less than an average household and considerably less than households with lower educated heads. This situation is reversed in 1997. Households with heads, who have received vocational education only, with no particular qualification, are significantly worse off than households where heads have received more education. Households with heads that have benefited from tertiary education collect a substantial expenditure premium, i.e. they spend almost 40 per cent more than an average household. Thus, while in 1993 high levels of education appeared to be a hindrance rather than an asset in providing social status to the bearer, the transition process appears to have significantly contributed to the valorization of human capital.

Accumulation of human capital significantly enhanced the earnings potential of highly educated young people and they increasingly formed the new local business elites and the new professional middle class. This new class of young and dynamic entrepreneurs predominantly operating in the

service industries is among the main winners from the transition to the market. Notice, however, that this form of upward mobility was observed on a much smaller scale than had been the case in e.g., Russia and Central Europe. This may be explained by the oriental specificity of the society and in particular the strength of the clan organization.

In addition, despite its radical reform agenda, market distortions are still pervasive in Kyrgyzstan. For this reason, marketable skills, education and innovative thinking do not necessarily go hand in hand with business success and the ensuing status gains. Many business opportunities are created through the conditioning of personal networks and clan connections. Rent seeking activities and monopolistic practices are pervasive, as are underground economic activities.

The social position of blue-collar workers, peasants and some professional groups who, for ideological reasons, had acquired social status and influence under communism was eroded. Their loss of social status and influence was compounded by loss of income and many of them entered protracted spells of poverty. In addition, pensioners and the disabled, who previously received adequate protection against adverse contingencies, lost not only their income but also many of their privileges (e.g., access to health care). These societal groups, along with the newly created underclass of the unemployed, stand out as the main losers from the transition to the market.

On balance, the number of losers appears to clearly outweigh the number of winners from the market-oriented reforms. There are fewer winners in Kyrgyzstan than for instance in the Central European transition economies. However, its radical reformist approach to manage economic change has provided a framework for rewarding ambition and entrepreneurial spirit and thus created a scope for social mobility and re-ranking – but also instability – unknown to its Central Asian neighbours. The large-scale migratory movements of the Russian and ethnic German population groups also substantially affected social mobility and re-ranking. These had previously formed the backbone of the professional and working classes and their replacement by ethnic Kyrgyz leads to further changes in occupational and social status.

Regrettably, as elsewhere in the CIS criminalization of the society has interacted with social developments in Kyrgyzstan. While crime has flourished in general, a new threat stems from the proliferation of drug-

related crime (Rumer 1996a: 63). Kyrgyzstan has become a major drug transportation route from Afghanistan and Gorno-Badakhshan in Tajikistan to the city of Osh in the Fergana valley in southern Kryrgyzstan, and from there on to the CIS and Europe. For a considerable number of people involved drugs trade sustains their livelihood, rendering the efforts by the law-enforcement agencies to stomp out these crimes even more perilous, and in vain. Some observers have even suggested the emergence of a 'Colombian' pattern, where a substantial part of the local population specializes in the cultivation and transportation of opium as their only viable alternative for economic activity (Zhukov 1996: 126).

Thus, despite the rapid modernization of Kyrgyz society, many traditional factors – personal networks, clan structure, rent seeking, the informal sector – continue to influence the social stratification process, hampering the emergence of a liberal, democratic and culturally diversified market economy. Notwithstanding, the process of modernization is clearly visible, especially in the capital Bishkek, and certainly exerts a powerful demonstration effect thus forcing social change.

#### **4.1 The upper class**

Casual observation suggests that the Soviet nomenclatura has successfully defended, and even strengthened, its position at the top of the social pyramid. The chairmen and directors of most 'national companies', holdings and investment funds emanated from the Soviet bureaucracy and political elite. Their power and resources were consolidated using their clan connections. Rumer observes that 'one gains the impression that the national wealth has been plundered during the process of privatization – and on a truly fantastic scale, spawning a whole new class of predatory 'bourgeoisie' (Rumer 1996b: 56). Consequently, vast resources have accumulated in the hands of a tightly knit network of government officials, their relatives, and close associates. This is confirmed by the information in Table 5 which already suggested that despite the overall reduction in inequalities in the Kyrgyz society, the rich became considerably richer between 1993 and 1997.

The former nomenclatura is joined at the top by a small group of successful businessmen and entrepreneurs. Using the 1993 KMPS and the 1997 LSMS, one may trace the background and the sources of the new-found wealth of this latter group. They are usually well educated, active in the manufacturing or service sectors – particularly trade and banking – of the economy, and they live in Bishkek. It is much more difficult, however, to

identify observable characteristics – personal, labour force or other – of the old-established elite but informal evidence, again, suggests that they are the high-level government bureaucrats, enterprise directors and bankers.

Estimates of the size of this group of extremely wealthy persons vary and depend on the definition employed. Under no circumstances does the elite, however, encompass more than 5 per cent of the population. In fact, while the richest 10 per cent of Kyrgyz households account for approximately 40 per cent of total household expenditures in Kyrgyzstan in 1997, the top 5 per cent alone account for over 30 per cent of all expenditures. In addition, they are the largest property holders in the form of equity shares and real estate. They enjoy high-quality housing and have access to a wide variety of luxury durable consumer goods. Despite its small numbers, evidence of the high-life led by Kyrgyzstan's elite is abounding in the streets of Bishkek with a noticeable number of luxury Western cars and mobile phones. And here and there springs up the occasional impressive house, in the midst of a general slump in construction, to offer a sharp contrast to the poverty-stricken surroundings.

The composition of the upper class has also been affected in other ways by the economic and social transformation. As a result of the emigration of ethnic Russians and Germans, the Kyrgyz elite has been consolidated. Those Russians who stayed on in Kyrgyzstan after independence generally suffered a substantial loss of status, regardless of their initial social position. At the same time, generational changes occurred at the level of the elite. The transition to the market and the ensuing privatization of state property and creation of business opportunities has promoted the upward mobility of the young descendants of the old-established nomenclatura. For them it became easier than under Soviet rule to reach high social positions and wealth, using their enterprise and human capital. Nomenclatura networks and family ties remain an essential precondition to enjoy a privileged position in society.

In a country where criminal activity thrives, security is a major concern for the elite. Their security is often guaranteed by pledging loyalty to government officials and sharing profits with them. All businesses, from small kiosks to large enterprises, depend on these informal links with state officials on matters of taxation and customs regime. Through this channel government officials acquire an active stake in the conduct of the general economic activity. An anti-corruption campaign that began in December 1998 has shed light on a substantial number of dubious deals involving

government officials. According to Kyrgyz Prosecutor-General Asanbek Shirshenaliyev, in the past five years, 383 government officials have been dismissed from their posts on corruption charges. This included the arrests in December 1998 of several deputy ministers.

## **4.2 The middle class**

Identification of the middle class in the Kyrgyz context is not a straightforward task. The middle class is typically an urban phenomenon, yet over 60 per cent of the Kyrgyz population live in rural areas. And, while poverty estimates vary, between 40 and 50 per cent of all households in Kyrgyzstan are thought to be poor. Thus, the middle class can be expected to be much smaller than is the case in Western countries and the European transition economies. In addition, it may be useful to distinguish between middle-income middle class households and the upper middle class. The former group is composed of households that are not poor but remain in a precarious situation. Small losses of income may result in them entering poverty. In the latter group, one finds households in secure income positions who are more likely to experience upward rather than downward social mobility.

On the basis of expenditure data and the previously introduced wealth index, one may conclude that about 30-35 per cent of Kyrgyz households belong to the middle class, of which one third approximately make up the upper middle class.

Middle class households spend on average 70 per cent more than poorer households. The upper middle class, in turn, spends an additional 30 per cent more than the middle-ranking middle class. Asset ownership and possession of durable goods provides additional support for this classification scheme.

The lower middle class is generally composed of households that became disenfranchised as a result of the transition but avoided a full-scale descent into poverty. They include families where the head of household remained employed but where the head and other family members supplement the income through secondary activities, farmers with larger landplots and livestock holdings who achieve good levels of productivity as well as pensioners who returned to work. In this group, one also finds many employees in the budgetary sector who had to accept real wage cuts as a result of the government's austerity package. These include junior civil servants, teachers and doctors.



The middle class is on average well educated. In 1997, over 50 per cent of middle class household heads have received more than secondary education. This is unsurprising, given the good average educational achievement record of Kyrgyzstan, a positive legacy of the Soviet period. However, the abundance of a well-educated labour force and the fact that the 'new economy' creates jobs at a slower rate than they are destroyed in the 'old economy' means that adequate employment opportunities do not exist for all of these highly qualified individuals. As a result, many of them accept jobs for which they are over-qualified or they engage in subsistence self-employment activities, degrading their skills in the process and adversely affecting their potential for upward social mobility.

Upper middle class households concentrate, just like the elite, in the manufacturing and the service sector. They work as professionals, managers or small entrepreneurs. They also concentrate more heavily in new enterprises e.g., joint stock companies, joint ventures or private enterprises rather than in state-owned enterprises. Approximately 15 per cent of the upper middle class households engage in non-agricultural self-employment or entrepreneurial activity. While this is a relatively high percentage, it is significantly less than for upper class households (25 per cent). The spread of these activities appears to be hampered by the unwieldiness of the tax system, administrative harassment, crime and economic instability. The upper class, through their closeness to the political elite and their greater wealth may indeed be better prepared to deal with the heavy regulation that is entailed by entrepreneurial activity.

### **4.3 Poverty and the poor**

With a GDP per capita in the region of US\$ 2,000 per annum, Kyrgyzstan is a poor country. Resources are distributed very unequally, a process exacerbated by the transition to the market. As a result, large parts of the Kyrgyz population are impoverished. The elimination of widespread poverty arguably poses the greatest challenge to the pro-market reforms while its existence may threaten the success and sustainability of the reform drive.

It is very difficult to assess the true extent of poverty in Kyrgyzstan and the existing evidence is conflicting. In addition, measurement and methodological problems are pervasive (Ackland and Falkingham 1997).

In 1989, before the beginning of reforms, 33 per cent of households in the Kyrgyz Household Budget Survey received a monthly per capita income

below 75 rubles, the official Soviet poverty line. In the 1993 KMPS, 45.5 per cent of households are identified as poor, a marked increase from the pre-transition poverty level. According to LSMS data, 51 per cent of households were poor in 1997, a further 5.5 per cent increase. The International Monetary Fund estimates a 40 per cent poverty rates for 1993, and almost 50 per cent in 1996 (IMF 1998: 12). These estimates are later revised upwards: 54 per cent of poor in 1993 and 70 per cent in 1996 (IMF 1999: 12). Thus, poverty in Kyrgyzstan appears to be high and rising.

This latter claim – that poverty is rising – is disputed by Heinrich (1999). Using several poverty lines while paying particular attention to the problem of intertemporal comparability of these poverty lines and using a range of equivalence scales to adjust the expenditure information for economies of scale in consumption, strong evidence is put forward that poverty fell by approximately 5 per cent between 1993 and 1997 and that less than 50 per cent of households remained poor in 1997. The results also demonstrate the importance of correcting expenditure data for household composition. Average household sizes in Kyrgyzstan are very large relative to Western households and precluding the existence of economies of scale in consumption is clearly unreasonable, when the results show that even small adjustments may fundamentally alter the conclusions. In addition, the inequality analysis suggested that expenditure levels of the poorest households had increased in 1993-1997 relative to their better off counterparts, possibly as a result of the introduction of the Unified Cash Benefit. For the assessment of poverty in Kyrgyzstan, this implies a decrease not only of the simple headcount of poverty but also of the severity or intensity of poverty.

Poverty in Kyrgyzstan is heavily concentrated in rural areas. In 1997, over 50 per cent of rural households were poor but less than 20 per cent of urban households. The mountain oblast of Narynskaya is the poorest region, with a poverty incidence of over 80 per cent. Poverty is also concentrated in agrarian regions of the Southern part of the country. These are Osh and Djalal-Abad Oblasts where the proportion of poor residents reaches 50 and 62 per cent respectively. The capital Bishkek exhibits the lowest poverty rate: less than 10 per cent of households living there are poor.

The spread of mass poverty to mountainous and remote areas is largely due to the limited opportunities for productive farming and a drastic decline in livestock holdings. Rural development is further hampered by the absence of productive and social infrastructure. Rural areas thus experience a mass

outflow of population, primarily among the youngest and most industrious. Poverty alleviation in these areas requires large injections of state support, to date by far inadequate. Measures for the development of local infrastructure and social services need to be combined with cattle breeding and crop cultivation (vegetables) so as to satisfy the basic needs of the local population.

Poverty is typically correlated with unemployment and is high in areas where unemployment is high. Areas of high concentration of poverty are single-firm towns, which developed around a single big now defunct enterprise. Thus, the majority of the local population became unemployed. Poverty relief in these areas requires the restructuring of large enterprises and, more importantly, job creation in the SME sector.

Poverty in Kyrgyzstan extends to all the major socio-demographic groups. This includes the traditionally vulnerable groups e.g., the unemployed, pensioners and those unable to work but also households of working-age, able-bodied persons who pursue an economic activity. Table 7 shows that households with a retired or unemployed head in 1997 spend 10 per cent less than an average household. Households with a working head, on the other hand, spend slightly more than an average household. This figure masks, however, the enormous dichotomy that exists between workers.

TABLE 7  
ECONOMIC STATUS OF HOUSEHOLD HEAD AND EXPENDITURES, 1997  
(as per cent of total average household expenditure)

Economic status	Frequency	Per capita	Equivalized
Working	58.80	101.9	103.0
Retired	24.66	91.7	89.2
Unemployed	11.13	91.2	92.5
Other	5.41	135.7	132.0

The erosion of state welfare support has negatively affected the livelihood of old-age pensioners, many of whom return to work in the informal subsistence sector of the economy, the disabled and families with large numbers of dependent children. As a result, the majority of children in Kyrgyzstan grow up in poverty and are unable to acquire adequate skills and levels of human capital, in the process adversely affecting the long-run growth potential of the economy.

While households depending on public transfers for their income are disproportionately at risk from poverty, many households engaged in gainful economic activity are also poor. Therefore, strategies to relieve poverty are much more complex than just to increase the number of working households.

In 1997, over 85 per cent of households derived substantial income from earnings and a further 40 per cent derived substantial income from farming activity. Yet, 35 per cent of households with earnings and over 50 per cent of households with agricultural income were poor (Heinrich 1999).

In the absence of an effective social safety net, many households rely on help from friends and relatives. In 1997, 23 per cent of households received a significant amount of private transfers, up from 14 per cent in 1993. Many households – especially pensioners – rely on the farming of private plots in order to procure minimal amounts of food. In urban areas subsistence-oriented economic activities include petty trading of foodstuffs, fruit and vegetables or cigarettes in open markets or the street. However, such subsistence activities are inaccessible to the most vulnerable groups in society: urban female-headed households, rural pensioner-headed households, and households with many children (Ackland and Falkingham 1997: 98). The inability of the transfer system to provide sufficient help to these households means that they form a socially immobile and severely deprived underclass.

The extent and possible implications of the poverty problem have now been correctly recognized by policymakers and poverty alleviation has risen to the top of the political agenda with the adoption in 1998 of the National Programme for Poverty Alleviation (ARAKET). The structure of poverty suggests that effective poverty alleviation can be achieved by a coherent set of labour market policies including wage policy and active labour market policies, the removal of administrative barriers to the creation of small enterprises and support for households in rural areas, mainly under the form of improved infrastructures.

## **5 POLICY IMPLICATIONS FOR SOCIAL COHESION, STABILITY AND DEVELOPMENT**

Kyrgyzstan has successfully overcome the inertia of central planning. It has stabilized the macroeconomy and initiated the development of a new institutional structure. However, radical economic reforms have failed in delivering higher living standards to the bulk of the population and the transition has resulted in a large increase in poverty. Only a small segment of the population managed to take full advantage of the new opportunities that the market economy offers. This had led to a considerable worsening of the distribution of income and wealth and has contributed to the rise in poverty. The reduction of inequality and poverty has become a key objective of economic and social policies while social integration and cohesion have become major preconditions for sustainable development.

The policies to fight poverty should primarily focus on promoting economic stability and developing the key sectors of the national economy. Particularly important is the development of the agricultural sector, which employs almost half of the labour force. As almost three-quarters of the poor live in rural areas, increased efficiency in agricultural production, aided by the development of rural infrastructures is likely to considerably improve the fate of the rural population.

In the short-term, the consolidation of economic stabilization and the resumption of growth are priorities. Attention should therefore be paid at preventing poverty from spreading and scarce transfers should be devoted to eradicate poverty under its most acute forms. Poverty reduction on a larger scale should commence in the medium term as the benefits from economic growth are shared out to all strata of the society.

Strategic goals to improve living standards and reduce poverty may be achieved by a combination of social policies aimed at improving labour productivity and appeals to the personal responsibility of citizens for their well-being with social assistance targeted only at vulnerable groups.

Active social policies should aim at providing economically gainful employment and improving the structure, quality and competitiveness of labour. These measures include employment programmes, mitigation of unemployment, fostering of entrepreneurial activity and support to small businesses and the farming community.

The promotion of gainful employment as the main source of welfare improvements requires corrections to the distorted wage structure. Employment should guarantee an adequate remuneration and particular

attention should be drawn to the level of the minimum wage and the wages of employees in the budgetary sector, many of whom are very poor.

The creation of equal opportunities requires investment in human capital. This is especially true for the poor. A high priority should therefore been given to essential commodities and services such as housing, education and training, medical care, and basic cultural goods and services.

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