

The Newsletter About Reforming Economies

# Beyond Transition

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*The study by Institute of Urban Economics in Moscow confirms that at-risk groups for poverty in Russia are households of nonworking retirees, large families, households with disabled members, poorly educated households, and those living in smaller cities.*

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## Good-bye Lenin (or not)?

### The effect of communism on people's preferences for redistribution

Alberto Alesina and Nicola Fuchs-Schuendeln

**P**references for redistributive policies differ significantly across countries. Do regimes differ solely because of the populations' different initial preferences for redistribution? Or is there a feedback effect from the regime on preferences? Post-war Germany offers an opportunity to analyze the effect of Communism on preferences. Our empirical analysis, based on more than 18,000 year-person observations, reveals that the effects of Communism on attitudes towards the role of the government are large and long lasting. It will take one to two generations for the preferences of former East and West Germans to look alike.

From 1945 to 1990, Germany was split into two parts for reasons that had nothing to do with Germans' individual preferences, desire for separation, or diversity of visions. Because the political and economic systems have been the same in the eastern and western parts of Germany since reunification in 1990, and were the same before 1945, West Germans constitute a meaningful control group for East Germans. Therefore, comparing the differences in attitudes, beliefs and political preferences for market capitalism and the role of the state after the reunification can give us a clue on the effects of having lived for 45 years under a Communist regime.

For our analysis, we use data from the German Socio-Economic Panel, an annual household panel. We use the original sample established in West Germany in 1984 (11,400 year-person observations), and the sub-sample covering the territory of the former GDR (7,000 year-person observations) for two years, 1997 and 2002. In both years, respondents were asked about their preferences regarding the role of the state in different areas of social security, namely in providing financial security for families, the unemployed, elderly, sick, and people requiring long-term care. Two additional questions were designed to capture respondents' beliefs on the role of alternative driving forces for success in life: individual effort versus luck and/or social conditions.

The main explanatory variable is a dummy that takes on the value of 1 if the respondent lived in East Germany before reunification, regardless of current place of residence. We control for the age, gender, marital status, labor force status, and occupation of the respondent, the number of children, and the number of adults in the household, as well as annual household income.

#### East Germans have stronger preferences for an active state role

Our analysis shows that an East German is significantly more likely to have preferences for state intervention than a West German, even after controlling for household income. In 1997, being from the East increased the probability of favoring state intervention by between 14 and 16 percentage points, compared to being from the West.

#### 20-40 years needed for preferences to converge

However, East Germans are becoming less pro-state over time: Between 1997 and 2002, the probability of favoring state intervention for an East German declined by between 2.5 and 5.8 percentage points. Assuming that convergence is linear, we estimate that it will take roughly between 20 and 40 years, or one to two generations, for Eastern and Western preferences fully to converge.

- *Age effects.* In the West, the older are progressively less pro-state than the young, a pattern also observed in the US. However, in the East the exact opposite is true. The quantitative implications of the age effects are large. While an East German born after 1975 is only between 3 and 11 percentage points more likely to be in favor of government redistribution than a West German of the same age, the difference increases to between 21 and 49 percentage points for people born before 1945. The obvious interpretation of this strikingly different age pattern between East Germans and West Germans is that while age tends to make individuals less pro government in West Germany, this effect is more than compensated for by the fact that elderly East Germans have lived longer under communism.

- *Decomposition of change over time.* Is the above-mentioned decline in East Germans' preferences for redistribution between 1997 and 2002 simply a result of a shift in the cohort composition, or of changes in personal preferences? By including in the regression only individuals who answered the relevant questions in both 1997 and 2002, we are able to conclude that approximately two thirds of the convergence arises from an actual change in preferences, while approximately one third arises from a shift in the composition of the cohort.

- *The effect of Communism: poverty or preferences?* The poor tend to favor government intervention more than the rich. Yet the fact that East Germans have on average lower household income does not explain our results; they are robust to the inclusion of current household income, expected household income, and the share of household income currently coming from government sources. In addition to personal income, however, there might be an aggregate income effect; individuals living in regions poorer than average may prefer government intervention because of the active redistribution from richer to poorer regions. By including average per-capita income and unemployment rate of the state of residence, as well as transfers received or paid by the state, we find that up to one third of the "East effect" can be explained by the fact that the East became poorer during Communism and is now a net beneficiary of redistribution within Germany.

- *Migration and preferences.* East Germans are certainly not a homogeneous group: 7% of them in our sample have

migrated to the West. When checking for differences among East Germans, we find that East Germans living in the West favor government intervention more than "native" West Germans, although only half as much as East Germans who remained in the East. The latter could mean either a faster convergence of preferences of East Germans who moved to the West, or a self-selection — the group might have had lower preferences for state intervention to begin with. Note, e.g., that the average age of Eastern respondents who moved to the West is 34, while the average age of Eastern respondents who stayed in the East is 45. All the convergence in preferences between 1997 and 2002 is driven by East Germans who stayed in the East. The preferences of East Germans who moved to the West do not change significantly between 1997 and 2002. Again, there are several possible explanations for this phenomenon. It could be that the preferences of East Germans who moved to the West converged initially, but that they reached their new steady-state level by 2002. In this case, we should likewise not expect full convergence for East Germans staying in the East. On the other hand, it could be that those East Germans who moved to the West not only had different preferences at the time of migration, but that their preferences also exhibit different convergence patterns.

#### Why do former East Germans favor state intervention?

A possible answer to the question above is that East Germans are used to thinking, partly under the influence of Communist ideology, that it is "society's fault" if people are poor, unemployed or in need of help. Thus it is society's (i.e. the state's) obligation to take care of these problems.

The probability of believing in the importance of social conditions for individual fortunes is 10 percentage points higher for an East German than for a West German. Older East Germans are more likely to believe in social conditions as a major determinant of individual fortune than younger East Germans, which is an effect of having lived longer under the Communist regime. In the West, the age effect goes in the opposite direction, but is not significant. Moreover, East Germans believe less than West Germans in an important role of luck. In other words, East Germans seem to believe much more than West Germans that an individual's life is defined by social conditions, which is a basic tenet of the Marxist way of thinking. However, even after controlling for beliefs regarding social conditions, former East Germans believe in state intervention more than former West Germans.

#### Conclusions

Our analysis demonstrates that East Germans believe significantly more than West Germans that the state should be responsible for the financial security of various vulnerable social groups, namely the unemployed, the sick, the elderly, families, and people in need of care.

According to our results, it will take about one to two generations (20 to 40 years) for the average East German to have the same views on the role of the government as a West

German has. The differences in attitudes will disappear due to the combination of two forces:

- the death of the elderly and the coming of age of individuals born after reunification; this accounts for about one third of the convergence;
- real change in the preferences of individuals; this accounts for the remaining two thirds of the convergence.

We find that the difference in preferences between former East and West Germans is largely due to the direct effect of communism: ideological indoctrination, e.g. via public schools and TV, or an intrusive public sector, to which people became accustomed. An indirect effect of Communism lies in making former East Germany poorer than West Germany, and therefore more dependent on redistribution.

An implication of the above is that the 1990 political shock in Germany has had, perhaps, much deeper and longer lasting consequences than the widely studied economic shock associated with the reunification. A country like former West Germany, with an already generous welfare state, heavy labor and goods market regulations, etc., which many believe needs trimming, has received an influx equivalent to 25% of its population, composed of people inclined towards an even more extensive role for the state. This will make any political reforms aimed at trimming the welfare system especially difficult. Those who believe that Germany's economic outlook will look brighter if certain "structural reforms" are carried out should be especially concerned.

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