

# **EU Enlargement and Its Impact on the Social Policy and Labor Markets of Accession and Non-accession Countries**

Sofia  
2003

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The Center for Economic Development (CED) is a Bulgarian non-governmental research institute in the area of economic policy, established in 1997. Our goal is to support the economic development of Bulgaria through encouragement of public debate on economic issues and development of economic policy options.

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# Introduction

The project “EU Enlargement and Its Impact on the Social Policy and Labor Markets of Accession and Non-accession Countries” is a research and advocacy program to develop the national labor market policies and social security systems for mitigating the tensions and social costs related to labor migration and free movement of workers in accession and non-accession countries. Another important goal of the project is to examine the impacts of EU labor migration policy towards accession and non-accession countries and to suggest measures with respect to labor market and social policies to mitigate possible negative effects, transferring knowledge, experience, skills, and lessons learned between NGOs from Bulgaria, Slovakia, Estonia and FYR Macedonia.

In more details the project objectives are:

- To link counterparts and build networks between the regional labor and migration policy and opinion makers in Bulgaria, Slovakia, Estonia, FYR Macedonia and other countries across the region in order to develop common system and mechanism for preventing the illegal immigration from non-accession to accession countries, and from accession and non-accession countries to EU member states. These measures will facilitate and accelerate the enlargement process and the integration of the accession countries to the European Union.
- To identify the factors, creating political, economic and social instabilities and affecting the flexibility of national labor markets.
- To develop an appropriate social and migration policy for Bulgaria, Slovakia, Estonia and FYR Macedonia in order to mitigate the tensions and social costs related to the economic consequences of the new EU borders for accession and non-accession countries.
- To promote and develop effective governmental social, labor and migration reform agendas in Bulgaria, Slovakia, Estonia and FYR Macedonia.
- To transfer knowledge on Bulgarian, Slovakian, Estonian and Macedonian experience on the labor and migration issues and the best practices of the European Union, taking as an example the most affected EU countries, such as Germany, Italy, France, the United Kingdom, and Spain and Portugal (as countries which had to overcome the same challenges joining to the European Union in 1986).
- To work with local labor unions and employers' organizations in order to identify their strengths and weaknesses and to improve their capacities to respond the needs of the affected groups before and after accession to the European Union.
- To promote and assist the social dialogue between government, business, public, media, and NGOs.
- To raise public awareness and advocacy on the social price of EU enlargement and its impact on the labor markets of accession and non-accession countries.

The Center for Economic Development in Bulgaria is a project coordinator. Our project partners are the Center for Economic Development in Slovakia, PRAXIS Center for Policy Studies in Estonia and the Euro-Balkan Institute in FYR Macedonia. The project granted by Freedom House in Budapest started in December 2002 and was finalized at the end of May with a Policy Forum in Sofia where local consultants from Bulgaria, Slovakia, Estonia and FYR Macedonia, engaged in the implementation of the country reports, presented the findings from their research and their recommendations regarding the labor market

and social policy in their country in the light of increased labor mobility.

EU enlargement is a unique process. Ten Central and Eastern European Countries are going to become full member states of the European Union in May 2004 and thus they would benefit from the increased investment opportunities, the access to the Internal Market of the Union and from the access to the new technologies, the Structural funds and the Union Employment Initiatives aimed at making the European economy "the most dynamic and competitive economy in the world, based on knowledge" till 2010. It is the target set in the Lisbon Agenda and it is a great chance for the new future member states to join the efforts of the Union.

The four observed countries Bulgaria, Slovakia, Estonia and FYR Macedonia are in a different situation regarding the EU accession process. Slovakia and Estonia are going to enter the Union in May 2004. They are in the "first" group of countries on the list of EU accession. During the European Council Assembly in Copenhagen (12-13 December 2002) it has been decided Bulgaria to enter the Union in 2007 if the country succeeds in implementing the accession criteria till then. FYR Macedonia, on the other hand, is the first country from the so-called Western Balkans region that has signed the Stabilization and Association Agreement, in April 2001, and so far only Croatia has done the same. FYR Macedonia is in the "third" group of countries on the list for EU accession and the main challenge of FYR Macedonia on its path to EU integration is achievement of political stability and economic growth first.

Although these countries are in a different situation regarding the EU accession process, they all share common problems in the area of labor market and social policy. Since the start of the transition period labor markets in Bulgaria, Slovakia, Estonia and FYR Macedonia have changed significantly. As compared to the pre-transitional period when the centrally planned economies enjoyed full employment coupled with hidden unemployment now labor markets in the observed countries suffer from low labor force participation and low employment rates, high unemployment rates, large share of long-term unemployed and youth unemployed among the unemployed, low skilled and low educated unemployed, high regional disparities in labor market performance, more affected by unemployment women than men,

more affected by unemployment ethnic minorities and other socially disadvantaged people than the rest people and high level of grey economy. The main reason for this unfavorable labor market situation in the observed countries can be found in the rapid changes in the economic environment as a result of the transition process to market economies, which has caused destruction of lots of jobs in agriculture and industry and great shift of the labor force to the service sector. Another very important reason for the high unemployment rates is the lack of right education and qualification of the unemployed in correspondence to the labor market demand.

The main apprehensions of the current member states regarding the forthcoming enlargement of the European Union are related first and foremost with the fear that the lower levels of salaries and social protection in the future member states, as compared with the levels of the current member states, will lead to great redistribution of the investments and the employment in the Union and to massive internal migration flows. The fear from the so-called "social dumping" in the European Union provoked broad debates and resulted with the European Commission's proposal to the accession countries of a transition period before the full liberalization of the free movement of workers within the European labor market. Current EU member states are much more worried of the opportunity third-country nationals to enter their labor markets through the territory of the accession countries and thus causing serious distortions to their labor markets and affecting the wage levels and comparatively high living standard of the European citizens. EU accession countries should develop appropriate national labor market policies and social security systems in order to guarantee the successful and flexible functioning of their labor markets and social security systems and to mitigate the tensions and social costs related to labor migration and free movement of workers in the European Union.

Bulgaria, Estonia, Slovakia and FYR Macedonia should lay particular stress more on the active labor market policies for solving the problems in the field of labor market and labor mobility than on passive labor market policies. They should implement special measures for ceasing the brain-drain process and creating favourable socio-economic conditions for professional realization of the young people in their own countries. Raising the educational and qualifica-

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tion levels of the labor force is a guarantee for the labor supply to correspond to the labor demand. “Long-life learning” programs are of great importance for making the labor force in the observed countries competitive to the labor force of the current EU member states.





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# **CHAPTER ONE:** **Country Reports**



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CENTER FOR ECONOMIC DEVELOPMENT, BULGARIA

**EU Enlargement and Its Impact on  
the Social Policy and Labor Market  
of Bulgaria**

*Sofia, 2003*



# 1. Macroeconomic Picture and Stage of EU Accession

## 1.1. Macroeconomic Background

**Bulgaria's economic development** after signing of the Currency Board Agreement in 1997 is characterized by fiscal stability, low inflation, continuous GDP growth, stable and liquid banking sector, developing but still inefficient in terms of operation capital market, and unbalanced labor market.

Major objectives of 2002 **fiscal policy** included maintenance of balanced budget, low budget deficit, and fiscal stability. First summarized data about the 2002 fiscal program reveal that budget parameters have been fulfilled. According to preliminary data, **the deficit realized** amounts to BGN 218.3 m, or 0.7 percent of GDP, with planned deficit amounting to BGN 257.3 m, or 0.8 percent of GDP. Annual economic growth is expected to exceed latest official estimates of 4.2 percent.

Despite the more pronounced price raise in the beginning of 2002, prices generally increased at a declining pace throughout the year, compared to the two previous years. **The average annual inflation** is 5.8 percent, and **the accumulated inflation for the year** (December 2002 compared to December 2001) amounts to 3.8 percent, which is the lowest figure since 1999. **Food prices taken on an average annual basis** are by 4.2 percent lower in 2002 compared to 2001. There is however a material average annual growth of non-food prices (+10.4 percent) and of service prices (+11.4 percent).

In 2002 **the total amount of the state and state-guaranteed debt** decreased by BGN 2 600 m, dropping down to BGN 18 180 m at year-end.

**Restructuring and privatization of the state sector** continued in the past 2002 with a view to establish efficiently operating private property and

to attract more foreign direct investments to the economic sector. Yet a conclusion can be made that 2002 was the most unsuccessful year for Bulgarian privatization since 1995. According to data by the Privatization Agency, only 275 privatization transactions were signed as at 31.12.2002 and the annual plan was fulfilled at 41.4 percent.

In 2002 there was not any considerable improvement of the **conditions for development of the small and medium-sized business in the country**. The trend of absence of well-directed tax policy in support of small and medium-sized business, which is Bulgaria's major employment source, continued in 2002 and reveals a need of further governmental efforts along these lines. Government support to small and medium-sized enterprises was manifested in the first place in the National Strategy for Encouragement of SME Development in Bulgaria 2002-2006 accompanied with a Working Program, which was approved by the Council of Ministers on March 28, 2002. The Strategy contains seven basic priorities, which focus on developing stable and transparent regulations for SMEs; implementing a policy to improve the financial environment; promoting the introduction of modern technologies and contemporary business models in the sector; improving the access of SMEs to foreign markets; efficient information and consulting services; and implementing a policy to improve the conditions for development of the business in a regional aspect.

**The state of the banks** in Bulgaria remains stable, with excellent measures of capital adequacy and liquidity, and well-functioning banking supervision. However, the banking system of Bulgaria remains insignificant in terms of the amount of assets and the share of provided loans in GDP. According to BNB data, as at end of December 2002 banking system

assets amounted to BGN 14 557 124 thousand and deposits amounted to a total of BGN 11 282 160 thousand. Loans to the non-government sector manifest a clear upward trend throughout the year, with new loans negotiated by commercial banks in 2002 amounting to a total of BGN 5 189.7 m, whereas in 2001 these amounted to a total of BGN 3 084.21 m (registering a growth of 68.27 per cent).

A couple of positive trends were observed in the **capital market** in 2002 - exchange trade in compensatory instruments started, the SOFIX index registered an upward trend, market capitalization increased. Nevertheless, the role of the capital market in Bulgaria's financial sector remains insignificant.

The 2002 volume of **foreign direct investments** reached only USD 458 m, registering a drop by USD 354.9 m compared to 2001. The 2002 structure of foreign investments differs from that in 2001 in the higher volume of proceeds from privatization (a higher number of relatively small transactions), the higher amount of payments under inter company loans (as a result of foreign investors' retaining new investments with simultaneous payment of old loans) and the higher (nearly 6 times) amount of reinvested profit. Given the instability of world economy and international financial markets, the scarcely known and under-regulated Bulgarian market with rather weak financial intermediation system and a judicial system subjected to justified criticism do not create conditions to attract significant volume of foreign direct investments.

The past **year 2002 can be characterized as a year of transition in Bulgarian social policy** and a striving to achieve better economic and social policy coordination in the next years. According to data from labor force surveys, in 2002 unemployment levels are lower compared to the previous year but exceed 2000 levels. Nevertheless, unemployment registered a downward trend throughout the year. Labor market policy and social assistance are the two key areas where the Government should focus their attention. In the 2003 budget funds for social payments and curbing unemployment increase by nearly BGN 900 m compared to 2002. The relative share of social expenditures in the 2003 budget is 38 percent of total non-interest bearing payments or around 14 percent of GDP. The new social policy approach implies more active measures to decrease

unemployment, a differentiated approach to every unemployed person, consistent fiscal decentralization in the social area, and obligatory assessment of the social effect of all economic measures implemented in the country.

## 1.2. Stage of EU Accession

**2002 negotiations for Bulgaria's accession to EU** resulted in 23 temporarily closed chapters. Bulgaria closed 6 chapters by the end of the Spanish Presidency (30 June 2002) and another 3 during the Danish Presidency (1 July – 31 December). The 2002 Regular Report of the Commission on the Progress of Bulgaria stated for the first time that Bulgaria is a functioning market economy. The 2001 assessment classified Bulgaria as a country close to the functioning market economy.

**Table 1. Monitoring of Bulgaria's EU accession negotiations**

Chapter	Status (31 December 2002)
1 Free Movement of Goods	Temporary closed
2 Free Movement of People	Temporary closed
3 Freedom to Provide Services	Temporary closed
4 Free Movement of Capital	Temporary closed
5 Company Law	Temporary closed
6 Competition Policy	Open
7 Agriculture	Open
8 Fishery	Temporary closed
9 Transport Policy	Open
10 Tax Policy	Temporary closed
11 Economic and Monetary Union	Temporary closed
12 Statistics	Temporary closed
13 Social Policy	Temporary closed
14 Energy	Temporary closed
15 Industrial Policy	Temporary closed
16 Small and Medium-Sized Enterprises	Temporary closed
17 Science and Research	Temporary closed
18 Education and Training	Temporary closed
19 Telecommunications	Temporary closed
20 Culture and Audiovision	Temporary closed
21 Regional Policy	Open
22 Environment	Open
23 Consumer Protection	Temporary closed
24 Justice and Home Affairs	Open
25 Customs Union	Temporary closed
26 Foreign Relations	Temporary closed
27 Common Foreign and Security Policy	Temporary closed
28 Fiscal Control	Temporary closed
29 Fiscal and Budgetary Issues	Open
30 Institutions	Temporary closed
<b>Total chapters closed</b>	<b>23</b>

Source: Center for Economic Development (2003): Bulgarian Economy in the Fourth Quarter of 2002. Bulgarian Economy in 2002 (Summary), Agency Economica Ltd.

The European Council in Copenhagen (12-13 December 2002) adopted important to Bulgaria decisions. Bulgaria will become EU member in 2007, provided that by that time it fulfills the membership criteria. The road map given by the European Commission sets clear goals for Bulgaria and enables the country to determine its own pace in the process of EU accession. It is indicated in the conclusions of the European Council in Copenhagen that “finalization of the negotiations for accession with ten candidate countries accelerates the perspectives for accession of Bulgaria and Romania as part of the same irreversible enlargement process”.

## 2. Labor Market

### 2.1. Current State: Factors and Problems

The restructuring of Bulgarian economy after 1989, with a view to create efficiently functioning market economy able to cope with the competitive pressure of market forces in the Single Market of the European Union and get successfully integrated in the global economy, outlined a couple of negative trends in the labor market in recent years. These are manifested first of all in the heavy unemployment, the rather low standard of living, the large share of the shadow economy amounting to 25-30 percent of GDP according to expert estimates, the increasingly higher deficit in the Pensions Fund which does not allow to reduce the social security and tax burden and to increase pensions, as well as the social isolation in a still unfavorable economic environment.

There are a couple of negative factors, which have an impact on the labor market flexibility. These include:

- Heavy unemployment among people of older age as a result of the demographic aging population process and the higher retirement age required to get pension rights.
- Mass layoffs as a result of structural and privatization processes in the economy and of social security, education and healthcare reforms.
- Loss of skills and working habits as a result of labor force reorientation from the industrial to the agriculture sector in search of an escape strategy.
- Low education and qualification level of the unemployed, which requires considerable financial resources to meet the needs and requirements of employers.
- Large share of permanent unemployed who have

lost their working habits, which impedes their adaptation to the work force demand on the labor market.

- The low income levels of the population and the rather low standard of living make university students and pensioners actively look for jobs and employed persons look for a second job.
- Implementation of new technologies in production which also results in lower number of the employed and unbalanced labor market.
- The large shadow economy share and the heavy tax and social security burden, which result in poor collection of State Social Security contributions, thereby impeding payment of pensions to current pensioners, generating social tension and discouraging bona fide payers.
- Large share of disabled people in Bulgaria in recent years, which requires special incentive measures for employment of underprivileged people and their successful integration in the labor market.

**Demographic trends** in Bulgaria have an unfavorable impact on the labor market performance. The aging of the population and the negative natural increase have a negative impact on the proportion of working-age population to the number of the pensioners, which together with the high unemployment rate and high gray economy share leads to low collection of the social security contributions to the Social Security and therefore to ever increasing deficit of "Pensions" fund, covered by a state budget subsidiary.



**Table 2. Demographic indicators**

	2000	2001	2002
Population, as of 31.12, number	8 149 468	7 891 095	7 845 499
Life expectancy, total, years	71.7*	71.8**	71.8***
Life expectancy, female, years	75.3	75.2	75.3
Life expectancy, male, years	68.2	68.5	68.6
Average age of the population, years	39.9	40.4	40.6
Population under, at and over working-age, total	100.0	100.0	100.0
Population under working-age, %	16.8	16.3	15.9
Population at working-age, %	58.3	59.2	60.1
Population over working-age, %	24.9	24.5	24
Total fertility rate (per 1000 people)	9.0	8.6	8.5
Death rate (per 1000 people)	14.1	14.2	14.3
Natural growth (per 1000 people)	-5.1	-5.6	-5.8

Note: \* Data refer to the period 1998-2000

\*\*Data refer to the period 1999-2001

\*\*\*Data refer to the period 2000-2002

Source: National Statistical Institute

According to December 2002 statistical data, Bulgaria's **economically active population** is 48.4 percent of the population at 15+ age. The country's **manpower reserve** amounts to 509.3 thousand people at the age between 15 and 64 years, who do not actively look for jobs. A conclusion follows that Bulgarian labor supply is not optimized, which is a result of both low payment rates, which discourage national labor force supply, and labor force education and qualification which do not fully meet employers' requirements.

Structural and privatization processes result in **labor force reorientation from the public to the private sector**. In 2001 the employed in the private sector accounted for 60.3 percent of total employment and only a year later their share increased to 62.6 percent. The share of the employed in the public sector dropped down from 39.5 percent in 2001 to 37.2 percent in 2002. **Small and medium-sized enterprises are the basic national employment source**. They account for around 99 percent<sup>1</sup> of total enterprises in the country (enterprises having 250+ employees are included) and their share in total employment is 50.7 percent. Bulgarian Government appreciates their significant role

in solving the unemployment problem, but the trend of failing to implement a well-directed policy to encourage small and medium-sized businesses and to promote employment continues. Measures adopted to reduce administrative barriers and to facilitate the access to loans are certainly important for the sector, but there is also a need to improve the coordination of the different government institutions directly concerned with the implemented policy for promotion of the SME sector, which would improve the efficiency of their actions. According to the labor force survey conducted by NSI in December 2002, the service sector accounts for more than half of the employed (58.6 percent), industry - for 32.8 percent, and agriculture - for 8.5 percent only.

The basic labor market problem is **the high unemployment level**, which, according to Employment Agency data, is 16.27 percent as of December 2002. There is slight improvement compared to December 2001 (17.87 percent), but it is insufficient for the effective operation of Bulgaria's labor market. According to the labor force survey, in December 2002 the number of unemployed was even higher – 16.8 percent of the economically active population. The lower unemployment level registered at the end of 2002 is a result of the new measures implemented by the Ministry of Labor and Social Policy and of the social policy in the labor market area, and namely the launch of a couple of national programs (From Welfare Benefits to Employment, Beautiful Bulgaria, JOBS, Support for Retirement, etc.) which constitute active measures to fight corruption and promote employment. Their objective is to restore the working habits of the unemployed; to create employment; to provide retirement support for unemployed persons who need 12 months of additional social security length of service to get the required points and age to acquire a right to a pension from the State Social Security System; to create temporary employment and training in construction and tourism, and last but not the least, to promote the economic development in regions with heavy unemployment by creating stable environment in support of small and medium-sized enterprises which are the basic national employment source.

A very important unemployment problem is **the large number of the long-term unemployed (for one or more years)** in the country, who account for 65.8 percent of the total number of unem-

<sup>1</sup> Agency for Small and Medium-sized Enterprises: Report on SMEs in Bulgaria 2001-2002; www.asme.bg

ployed (December 2002 Labor Force Survey). These people have lost their working habits and need special measures to improve their qualification and to get retrained in accordance with current employers' labor force demand. The fact that the share of long-term unemployed in the total number of unemployed increases every year raises concerns. In 1999 long-term unemployed accounted for 52.5 percent of the total number of unemployed, in 2000 – for 58.6 percent, in 2001 – for 63.2 percent, and in 2002 – for 65.8 percent.

**The high youth unemployment rate** in the country is another embarrassing fact in the field of unemployment. In 2002 15.8% of all unemployed are youth people aged between 15 and 24. Although ever since 1997 the youth unemployment is continuously falling, its rate in the country is still very high. The reason for this unfavorable fact lies in the lack of practical experience of the youth, which requires an adequate state interference for encouragement of the entrepreneurs to provide internships for the youth.

**Table 3. Youth unemployment**

	1997	1998	1999	2000	2001	2002
Youth unemployment (age group 15-24) as % of total unemployment	20,7	16,9	17,3	15,5	14,4	15,8

Source: National Statistical Institute and own calculations

**The education level of the unemployed** in Bulgaria allows to be assessed the conformity level of the education provided in the country, which determines the labor supply, and the requirements and needs of employers, which determine labor demand. According to the Labor Force Survey, in December 2002 11.9 percent of the unemployed have higher education, 53.3 percent have secondary education, and 34.8 have primary and lower level of education. The education structure of the unemployed reveals a need of further investments in human capital to enable the unemployed to meet labor market needs and make the labor market and effectively operating one. A glance back a few years ago reveals since 1997 a continuous growth of the share of unemployed with higher education (1997 – 8.4 percent, 1998 – 8.5 percent, 1999 – 8.0 percent, 2000 – 8.9 percent, 2001 – 11.2 percent, 2002 – 11.9 percent) and secondary education (1997 – 50.7 percent, 1998 – 50.7 percent, 1999 – 52.5 percent, 2000 – 53.1

percent, 2001 – 54.6 percent, 2002 – 53.3 percent) in the total number of unemployed and decrease of the share of unemployed with primary and lower education level (1997 – 40.9 percent, 1998 – 40.8 percent, 1999 – 39.5 percent, 2000 – 38.0 percent, 2001 – 34.3 percent, 2002 – 34.8 percent). The conclusion is that in Bulgaria educated talented people cannot get full realization at the labor market. This unfavorable trend is a result of both the low payment levels countrywide which ensure low standard of living and inability to get return of investments in human capital, as well as of the economic restructuring after 1989 which requires labor force retraining for successful realization in the service sector which in 2001 accounted for 46 percent of the total number of employed in Bulgaria.

**Income policy** is an integral part of labor market policy. Major priorities of income-related social policy include ensuring income growth, introducing flexible forms of payment - per hour, part-time, etc., as well as poverty monitoring, defining the poverty threshold and developing a national policy to overcome poverty. These objectives are laid down in the 2002 New Social Policy on the income of the population. In Bulgaria the minimum wage is determined on a national level. The nominal minimum wage registered a growth of 10 percent in 2002 (from BGN 100 in 2002 to BGN 110 (EUR 55) for 2003), however this increase is insignificant given the low starting basis. Minimum wages by sectors and professions are not determined yet to ensure fair labor force pay dependent on the competitiveness of individual economic sectors and on the labor demand and supply within individual professions, however such negotiations are expected to start in 2003 on the initiative of the Ministry of Labor and Social Policy. After the introduction in 2002 of minimum social security thresholds per sectors and professions on the basis of negotiations between the Government, the syndicates, and the employers organizations, Government intentions are to start since 2003 negotiation of real minimum wage levels per sectors and professions with a view to: ensure more equitable labor pay, raise the real income level and thereby ensure higher standard of living.

In terms of **the structure of total household expenditures**, the share of food expenditures remained traditionally high in 2002. At the same time, the prices of non-food goods and services registered

material increase in the previous year, which resulted in general increase of the electricity, telephone, water and maintenance expenditures of households. In this context the question of further restructuring and privatization of infrastructure sectors and their social acceptability in terms of their effect on prices and household expenditures is of particular concern.

According to the National Statistical Institute's data, in 2002 the average wage for the country of those employed under labor and service contracts was BGN 272 (EUR 136). The fact that the average wage in the public sector (BGN 321 (around EUR 160)) is higher than that in the private sector is very interesting. The positive first results of the introduction of minimum social security thresholds per sectors and professions and of the obligatory registration of labor contracts at NSSI since the beginning of 2003 generate optimistic expectations about possible lower social security and tax burden, but only the future can show whether the ruling will have the political will to do that.

The Consumer Survey conducted by NSI in January 2003 reveals more favorable changes in the financial situation of households and higher expectations about the next 12 months. In January 2003 consumers were more optimistic about unemployment in the next 12 months (the balance indicator registered a drop by 9.0 percentage points), mainly as a result of the active labor market measures implemented by the Ministry of Labor and Social Policy.

The survey of Bulgarian consumers calls for the conclusion that the Bulgarian standard of living registers a slow and unsatisfactory raise, which makes Bulgarians unable to pay for quality European goods. **UNDP's 2002 Human Development Report** characterizes Bulgaria as a state of medium human development, but the country is still far below the human development level of the Czech Republic, Estonia, Hungary, Poland and Slovakia, which are among the ten states to join the EU in 2004 - the fifth wave of EU enlargement.

## 2.2. Policies in the Field of Labor Market

The guidelines of the European Employment Strategy and the EU directives concerning equal treatment, labor force vocational training and other em-

**Table 4. Human development index 2002**

Country	Human development index	Ranking*	Status
Albania	0.733	92	Medium human development
<b>Bulgaria</b>	<b>0.779</b>	<b>62</b>	<b>Medium human development</b>
Croatia	0.809	48	High human development
Czech rep.	0.849	33	High human development
<b>Estonia</b>	<b>0.826</b>	<b>42</b>	<b>High human development</b>
Hungary	0.835	35	High human development
Kazakhstan	0.750	79	Medium human development
Latvia	0.800	53	High human development
Lithuania	0.809	49	High human development
<b>Macedonia</b>	<b>0.772</b>	<b>65</b>	<b>Medium human development</b>
Poland	0.833	37	High human development
Romania	0.775	63	Medium human development
Russia	0.781	60	Medium human development
<b>Slovakia</b>	<b>0.835</b>	<b>36</b>	<b>High human development</b>
Slovenia	0.879	29	High human development
Ukraine	0.748	80	Medium human development

Note: \*out of 173 countries

Source: UNDP; Human Development Report 2002

ployment-related issues are fundamental documents of Bulgaria's employment policy in a short- and mid-term perspective. The basic objective of labor market policy is to ensure effective labor market, which will guarantee higher employment level for the active population. The collateral objectives of Bulgaria's **employment policy**<sup>2</sup> set forth in the **New Social Policy Strategy** adopted by the Government in 2002 include:

- New individual approach to every unemployed person.
- Improving employability.
- Promoting entrepreneurship.
- Creating employment for underprivileged people.
- Training and retraining.

<sup>2</sup> Ministry of Labor and Social Policy: New Strategy in Social Policy, First chapter, EMPLOYMENT POLICY;  
<http://www.mlsp.government.bg/bg/docs/strategy/strategy-2.htm>

### 2.2.1. Active Labor Market Policies

The enforcement of the Employment Promotion Act (EPA) and the amendments to the Obligatory Social Security Code (OSSC) changed as of 1 January 2002 the active and passive labor market policies sources of financing.<sup>3</sup> **Active policies** are implemented by the Employment Agency; they cover measures regulated in EPA and are financed on an annual basis through Bulgaria's State Budget Act. Active policy funds cover costs of programs and measures targeting employment, vocational training, as well as the cost of the employment system.

**Table 5. National labor market employability improving programs (current and new projects)**

- National Program for Computer Training of Young People
- National Program to Improve Employability and Promote Entrepreneurship of young People
- National Program for Educational and Labor Integration of Young People Dropped Out of the Secondary Education System
- National Program for Education, Training and Employment of Roma People
- National Program for Employment and Environment Improvement Measures
- National Program for Alternative Employment of People Laid Off As a Result of the Privatization of Big and Monopolistic Companies
- National Beautiful Bulgaria Program

Source: Ministry of Labor and Social Policy

A couple of national programs, which are part of the active measures for labor market policy implementation, were launched in 2002. **The National Program From Welfare Benefits to Employment** was launched in October 2002. Its objective is to provide employment and social integration to permanent unemployed on welfare benefits by opening new jobs in socially useful activities. The pilot program was launched in 11 municipalities. It aroused great interest and in November it was started on a national level.

### The National Crop Protection - 2002 Program

was launched in July 2002. Its objective is to increase employment by opening additional seasonal jobs in crop preservation activities. The program targets with priority the long-term unemployed and laid off people from the Ministry of Defence and Ministry of the Interior systems. **The National Support for Retirement Program** was also launched in November. Its objective is to provide employment and retirement support to unemployed persons who need up to 12 months length of service to accumulate the required sum of social security length of service and age which gives right to a pension. **The Employment Promotion Act**, which took effect as of 1 January 2002, created preferential treatments, which the unemployed can make use of. These include:

- Getting a single sum of money instead of unemployment benefits, where the unemployed want to start up alone or in cooperation with other persons economic activity for production of goods or services.
- Making use of the opportunities provided under Art. 42 of the Act, which aim at encouraging the territorial mobility of unemployed persons.
- Getting access to loans through the Micro-credit Guarantee Fund up to the amount of BGN 15 000, under preferential conditions for start up or existing business (small enterprise) and on the condition of opening new jobs.
- Implementation of regional employment programs continued. Each program covers different micro-projects developed in accordance with regional needs and local social and economic specifics.

### Business centers and business incubators set up under the Employment through Business Support Project

are important tools to improve municipal business environment targeting the promotion of small and medium-sized enterprises, which are the basic national employment source. Basic services provided to the private business include: consulting, training, supply of useful business information, leasing schemes and technological support in 6 business areas – textile industry, alternative farming, tourism, furniture production, crafts and production of herbal cultures. Good 2002 achievements of the JOBS project resulted in a decision to expand

<sup>3</sup> Employment Agency (2003): Information on the State of Unemployment and Measures for Encouraging Employment in 2002

the project and set up business centers in another 10 Bulgarian municipalities, as well as to extend project validity by three years. The 2003-2005 JOBS strategy envisages national coverage of the business centers network, improving network efficiency, network institutionalization by way of a JOBS Association, and establishing new international contacts. The plan is to develop special initiatives targeting vulnerable labor market groups such as young people, Roma people, military people, and women. The project is expected to develop within Government's active employment policy the support provided to Bulgarian small business and to underprivileged social groups on the labor market.

The last two years witness higher share of labor market active measure costs at the expense of the share of passive measure costs. This is in conformity with the new social policy strategy to promote employment at the expense of the passive social protection of unemployed persons through welfare benefits and money.

**Table 6. Active and passive labor market measures for the period 1998-2002**

Year	1998	1999	2000	2001
Total expenditures	100%	100%	100%	100%
Active measures expenditures	31.2%	25.9%	17.8%	23.6%
Passive measures expenditures	57.5%	58.7%	78.2%	75.6%
Other expenditures	11.3%	15.4%	4.0%	0.8%

Source: Employment Agency

**Two new social measures** have been introduced since 2003 on the initiative of the Ministry of Labor and Social Policy (MLSP) and the National Social Security Institute (NSSI) - **minimum social security thresholds per sectors and professions and obligatory registration of labor contracts at the NSSI**. The objective of these measures is to create conditions for fair labor market competition, to improve the security of workers and employees, the collection of the contributions to the State Social Security funds and of tax liabilities to the budget, and last but not the least, to curb shadow economy in the country.

According to the survey "**The Size and Development of the Shadows Economies and Shadow Economy Labor Force of 22 Transition and 21 OECD Countries: What do we really know?**" of Friedrich Schneider<sup>4</sup> **the size of the shadow**

**economy** in transition countries registered increasing growth in the last 12 years. The average size of the shadow economy in the 9 CEE countries covered by the survey increased from 23.4 percent (of official GDP) in the period 1990-93 to 29.2 percent (of official GDP) in 2000/2001. The fact that in 2000/2001 Bulgaria was ranked second after Macedonia (45.1 percent of GDP) by size of the shadow economy among CEE countries with a level of 36.4 percent (of official GDP) generates concern. The high level of the shadow economy in Bulgaria repels foreign investors and impedes effective labor market functioning. **According to the above survey, in 1989/1999 30.4 percent of Bulgaria's active population (age 16-65) was employed in the shadow economy, which has a negative effect on the collection of social security and tax liabilities, lowers the trust in the pension reform and creates a burden for the state budget** to cover the increasingly higher deficit in the Pensions Fund.

**New measures fiscal results as of 27 March 2003 reveal** that in January 2003 payments to all social security and health insurance funds were by BGN 37.5 m higher compared to the same month of 2002. In February 2003 payments are by BGN 32.8 m higher compared to the same month of the previous year, and in March - by BGN 22.4 m higher compared to February 2002. **According to National Social Security Institute (NSSI)'s data, by March 27 payments to social security funds increased by BGN 92.7 compared to the same period of 2002**. Estimates show that in the first two months of 2003 the income for the purposes of social security of persons on labor and service contracts increased by nearly 10 percent compared to 2002. **The basic wage declared in existing labor contracts is by 4 percent higher compared to that reported by NSI for October 2002**. Luckily the fears of mass reappointment of workers and employees on positions and occupations of lower pay and lower social security thresholds and wages did not come true. According to NSSI's data, **38 000 of registered unemployed turned out employed under labor contracts and around 250 000 people came out of the shadow economy**.

**Another initiative of the Ministry of Labor and Social Policy involves**, starting from 2003,

<sup>4</sup> Professor Dr. Friedrich Schneider, Department of Economics, Johannes Kepler University of Linz, Altenbergerstrasse 69, A-4040 Linz Aufhof, Austria. Phone: 0043-70-2468-9210, Fax: 0043-70-2468-8209. E-mail: friedrich.schneider@jku.at

**Table 7. The size of the shadow economy in transition countries**

Former Soviet Union	Size of the shadow economy (in % of GDP)				Shadow economy labor force in % of working-age
	Average 1990-93	Average 1994-95	Average 1990-93	Average 2000/01	Population* 1998/99
1. Armenia	39.4	40.3	40.1	45.3	40.3
2. Azerbaijan	43.8	59.3	45.1	60.1	50.7
3. Belarus	34.0	39.1	35.6	47.1	40.9
<b>4. Estonia</b>	<b>33.9</b>	<b>38.5</b>	<b>34.3</b>	<b>39.1</b>	<b>33.4</b>
5. Georgia	43.6	63.0	45.1	66.1	53.2
6. Kazakhstan	32.2	34.2	31.9	42.2	33.6
7. Kyrgyzstan	34.1	37.2	35.2	39.4	29.4
8. Latvia	24.3	34.8	25.7	39.6	29.6
9. Lithuania	26.0	25.2	26.0	29.4	20.3
10. Moldavia	29.1	37.7	29.3	44.1	35.1
11. Russia	27.0	41.0	27.8	45.1	40.9
12. Ukraine	38.4	47.3	29.4	51.2	41.2
13. Uzbekistan	20.3	28.0	22.1	33.4	33.2
<b>Unweighted Average:</b>	<b>32.8</b>	<b>40.4</b>	<b>32.9</b>	<b>44.8</b>	<b>37.1</b>
Central and Eastern European Countries					
<b>1. Bulgaria</b>	<b>26.3</b>	<b>32.7</b>	<b>27.1</b>	<b>36.4</b>	<b>30.4</b>
2. Croatia	23.5	28.5	24.6	32.4	27.4
3. Czech Republic	13.4	14.5	13.1	18.4	12.6
4. Hungary	20.7	28.4	22.3	24.4	20.9
<b>5. Macedonia</b>	<b>34.5</b>	<b>40.3</b>	<b>35.6</b>	<b>45.1</b>	<b>35.1</b>
6. Poland	20.3	13.9	22.3	27.4	20.9
7. Romania	26.0	28.3	27.3	33.4	24.3
<b>8. Slovakia</b>	<b>14.2</b>	<b>15.2</b>	<b>15.1</b>	<b>18.3</b>	<b>16.3</b>
9. Slovenia	22.4	23.9	22.9	26.7	21.6
<b>Unweighted Average:</b>	<b>22.4</b>	<b>25.1</b>	<b>23.4</b>	<b>29.2</b>	<b>23.3</b>

Note: \* Working age population means population between the age of 16 and 65.

Source: Invited paper prepared for the Roundtable Conference: On the Informal Economy, Sofia, Bulgaria, April 18-20, 2002;

<http://www.csd.bg/news/bert/esentations.html>

### annual negotiations between syndicates and employers' organizations to determine minimum wages per sectors and professions,

which would improve labor market flexibility, and providing guarantees for higher living standard of the labor force in the future.

### The new social policy strategy envisages active business support measures with a view to combine the economic and social functions of the implemented labor market policy.

Starting from 2003, companies, which invest in regions of heavy unemployment (more than 50 percent of the average for the country), shall be exempt from profit tax for a period of 5 years. Where companies employ permanent unemployed at 50+ age, or partially disabled unemployed, they will pay lower taxes because the double amounts of the

wages and social security contributions for the employees belonging to the above groups will be deducted from the corporate profit prior to taxation, provided that such persons are employed for not less than a year.

Only around BGN 14 m (EUR 4 m) out of the BGN 20 m (EUR 10 m) planned under the **Micro-credit Guarantee Fund** program have been utilized. Over 1400 projects, which are expected to generate more than 3000 jobs have been approved.

### 2.2.2. Passive Labor Market Policies

**Passive policies** are implemented by way of measures for social protection in the event of unemployment and are financed from the new Unemployment Fund set up within the State Social Security (SSS) system since 2002. A positive change of labor market policy from payment of unemployment benefits to providing employment was observed in 2002. The purpose of this change is to create temporary employment, preserve the working habits of the unemployed and promote their entrepreneurial spirit and initiative.<sup>5</sup> According to Employment Agency's data, 2002 registered a drop down of the number of unemployed on benefits by 15.7 percent (from 161 864 in 2001 to 136 476 in 2002). The relative share of people on unemployment benefits in the average annual number of registered unemployed follows the downward trend of the average annual number of people on benefits, registering a drop by 3.4 percentage points compared to 2001.

Simultaneous implementation of measures to promote both labor force demand and supply involves a good economic-social policy balance. Subsidized employment is a successful temporary measure to conquer the heavy unemployment problem and improve Bulgaria's labor market flexibility, but it should be accompanied by a policy to promote the opening of permanent and efficient jobs

## 2.3. Challenges of EU Accession Regarding Labor Market Flexibility

Since 2000 Bulgaria develops in cooperation with the European Commission Joint Assessment of Employment Policy Priorities (JAP), which is reflected in the National Employment Strategy. **With a view to**

<sup>5</sup>Encouraging Employment Law, Published in Official Gazette, Issue 112 from 29.12.2001, in force from 1.01.2002, modification and supplement, Issue 26 from 21.03.2003

**Bulgaria's future participation in the European Social Fund, the country has the task to strengthen its administrative capacity**, to be able to plan, manage and assess in the future the co-financed programs of the European Social Fund, considering the European Employment Strategy, the National Action Plan for Employment and the Social Inclusion Process.

On 20 February 2003 European Commission published a report on the situation of the labor market in EU candidate countries, which revealed the great difference in the unemployment levels of the countries and the need of urgent measures to increase employment, mostly in the service sector, to improve the qualification level and to avoid reliance on agriculture and traditional industries. The objective of EC's report is to serve as guidelines for working out the national development plans of EU candidate countries, the employment and human resources policy, including a plan to utilize the European Social Fund. **According to the European Commission, there are four basic strategic priorities in the labor market area, to which EU candidate countries should pay special attention.** These include:

- Increasing labor supply and engaging a significant number of the active population in the labor market, as a precondition for economic and social development.
- Improving the employment level, which along with higher labor productivity is a key factor for strong economic growth, real equalization of income levels and achieving European employment targets set forth in the Lisbon and Stockholm strategies.
- Labor market operation should be dependent on economic restructuring and the labor market should enable people to manage economic reforms and transform their industries from obsolete into modernized ones.
- Improving the level of qualification and skills as a counterbalance of the aging labor force and future challenges resulting from the need to increase productivity within a competitive and enlarged single market.

**Labor market related issues are discussed in Chapter 13: Social Policy and Employ-**

**ment of the European legislation. Bulgaria closed temporarily this chapter on 22 April 2002.** This chapter covers areas where there is extensive secondary legislation at EU level, such as health and safety labor law and equal treatment of men and women, areas such as social dialogue, employment, and social protection where policies to harmonize national legislation on the basis of the Treaty establishing the European Community (EC). There is a need to develop a homogenous social framework in accordance with the principles and standards of the EC Treaty.

To harmonize some aspects of **labor law** at central level, EU has issued directives in the areas of: collective redundancy, protection of the right of employment in the event of new owner, employers' obligation to inform their employees about the conditions under which their labor contracts can be signed, guarantees for employees in the event of employers' bankruptcy, job description and organization of working time.

The Amsterdam Treaty added to Community's objectives in the social area the promotion of the **equality of men and women**. The implementation in practice of the principle of equal opportunities for men and women in all public activity areas is formulated in the **Community's Framework Strategy for Equality of Men and Women (2001-2005)**. Effective European legislation in this area includes guaranteed equal treatment under conditions of employment and holding a professional position, social security, systems of professional social security, maternity, protection of pregnant women, young mothers and suckling mothers.

The Amsterdam Treaty enabled the Community to combat **discrimination** in the field of employment, as well as in all other social and economic areas. Current EU legislation includes Directive 2002/43/EC, which prohibits racial and ethnic discrimination in the field of employment, education, social security and healthcare, access to goods, services, and home; as well as Directive 2000/78/EC, which prohibits discrimination in the field of employment on account of religion and beliefs, disability, age and sexual orientation.

The Single European Act (SEA) gave new orientation to social policy in the field of **health and safety of work**. European legislation contains directives

which fix minimum EU standards of health and safety in the workplace, which result in less accidents at work, less occupational diseases and less labor force injuries in EU Member States, and in higher employment level of the active population and more effective labor market, accordingly.

In the area of **employment** EU candidate countries should develop labor market policies, which would enable them to guarantee effective balance of labor force demand and supply at their domestic markets. Their new labor market policies, complying with the European Employment Strategy, must develop fact enough to allow full participation of the corresponding country in the Single European Market. Last but not the least, candidate countries must develop special policies and measures targeting unskilled active population to enable the latter to get successful realization at the labor markets of developed countries.

Effectively operating **judicial and administrative structures** are an important guarantee for the successful operation of labor markets in candidate countries, as well as for compliance with employment and social policy legislation.

Negotiations on Chapter 13: Social Policy and Employment have been temporarily closed. Bulgaria has been granted a transitional period till 31 December 2010 to implement tobacco growing legislation, particularly that about the maximum tar content of cigarettes.

The **2002 Regular Report on Bulgaria's Progress Towards Accession** states that Bulgaria must make further efforts in the areas of anti-discrimination, equal opportunities, labor law, health and safety at work, with a view to harmonize Bulgarian with EU social policy and employment legislation. There is a need to enhance social dialogue at national as well as at company and sector level with a view to negotiate fair payment levels and to ensure good conditions at work for the labor force. The scope of active measures targeting the labor market, and the number of the unemployed covered by vocational training programs is insufficient. There is a need to make these programs conformable to labor market requirements and needs with a view to guarantee successful integration of the unemployed in this labor market. It is important to review the benefit systems with a view to create incentives for the unemployed to actively look for jobs or start up their

own business. In view of the future management of European Social Fund activities after Bulgaria's accession to the EU, the Ministry of Labor and Social Policy must improve its capacity and cooperation with relevant authorities. The European Commission recommends to develop the socio-statistical schemes for poverty and social isolation in accordance with general EU social isolation indicators, with a view to take more effective future decisions to conquer social isolation and poverty, and to assess implemented measures. Bulgaria does not have yet a comprehensive anti-discrimination law or anti-discrimination authority for enforcement of such law.



## 3. Social Policy

### 3.1. Current State: Factors, Problems and Policies

Along with income policy and employment policy, which targets higher employment of the active population and effectively operating labor market, **Bulgaria's social policy includes three other policies - social security and industrial relations policy, social assistance policy, social dialogue policy.**

#### 3.1.1. Social Security

According to the 2002 New Social Policy Strategy, Bulgaria's priority **social security objectives** include:<sup>6</sup>

- Updated mechanisms to improve collection and increase proceeds in State Social Security funds.
- Gradual raise of all pensions with no increase of the social security burden.
- Higher pregnancy, birth and child benefits.
- Building an integrated information system for tax administration and NSSI needs.
- Promoting the development of the second and third pillar of the social security system.
- Improved labor legislation.

Bulgaria's transition to market economy, which required set up of effectively operating market institutions in all social and economic areas; demographic problems resulting from the aging population; heavy unemployment as a result of the restructuring and privatization processes called for **reform of Bulgaria's pension system**, which was entirely of a cost-covering type. Bulgaria's current pension model comprises three pillars: obligatory social se-

curity, complementary obligatory social security, and complementary voluntary social security. At this stage only the first pillar of Bulgaria's pension system is of a cost-covering type, i.e. collected social security contributions are entirely used to pay the pensions of current pensioners. The other two pillars operate on a capital principle. Social security contributions for State Social Security are distributed in 5 funds: Pensions, General Illness and Maternity, Accident at Work and Occupational Disease, Unemployment, and Non-Work Pensions. Contributions to the Non-Work Pensions Fund are made from the state budget, and those to the Accident at Work and Occupational Disease Fund are entirely for employers' account. The social security burden for all other funds is divided between the employer and the insured person in a proportion 75:25.

**Table 8. State social security fund contributions for 2002, %**

State social security funds - first pillar of the pension system	Total amount of social security contribution	Amount of social security contribution at employer's expense	Amount of social security contribution at the expense of the insured person
Pensions fund	29.0	21.75	7.25
General illness and maternity fund	3.0	2.25	0.75
Accident at work and occupational disease fund	0.7	0.7	0.0
Unemployment fund	4.0	3.0	1.0
Total:	36.7	27.7	9.0

Source: National Social Security Institute

The second pillar of the pension system (Supplementary Compulsory Pension Insurance - SCPI) consists of privately managed Universal and Occupational Pension funds (UPFs and OPFs) operating on capital principle. Insurance in a UPF is obligatory for

everyone born after 31 December 1959, and persons in first and second work category are insured in OPF. Collection of Supplementary Compulsory Pension Insurance contributions is centralized in NSSI, which then transfers collected contributions to individual accounts of the insured persons in the corresponding funds. The contribution to OPF for first and second category workers amounts to 12 and 7 percent of the income for the purposes of social security, accordingly. These contributions are entirely for employer's account. For insured persons born after 31 December 1959 NSSI transfers 2 percent of the Pensions Fund contribution to the UPF chosen by the corresponding person. Government intentions are to achieve smooth increase of UPF contributions at the expense of Pensions Fund contributions with a view to enable privately managed UPF to realize for the insured persons higher yield of social security contributions invested in profitable and low-risk financial instruments. Thereby every insured person can determine the desired risk/yield ratio by choosing alone a UPF.

The third pillar of Bulgaria's pension system comprises voluntary privately managed pension funds, which operate on a capital principle. Insurance in these funds is voluntary. Every insured person has the right to choose a voluntary pension fund and judge by himself the risk/yield ratio in the investment of his social security contributions.

At this stage Bulgaria has 8 pension insurance companies (Doverie, Suglasie, Allianz Bulgaria, ING, Newton Sila, Rodina, Bulgarian Pension Insurance Company, and Lukoil Garant – Bulgaria), each having a universal, an occupational and a voluntary pension fund. At the end of February 2003 the Commission for Protection of Competition allowed the take over of Bulgarian Pension Insurance Company by PIC Doverie, whereby since May 2003 there will be seven funds on the pension services market.

The **Commission for Prudential Supervision Act** was promulgated in Official Gazette, No. 8/28 January 2003 and took effect as of 1 March 2003. The new body integrates the State Commission for Securities, the Agency for Insurance Supervision and the State Agency for Social Security Supervision. The pension services market was hitherto supervised and controlled by the State Agency for Social Security Supervision. The new structure is expected to opti-

mize the administrative capacity and improve the management efficiency of Bulgaria's social security market.

**Bulgarian pension reform is well designed but difficult to implement on account of existing demographic problems, inefficient labor and capital markets and unsatisfactory real income level which does not encourage insurance in voluntary pension funds.**

Privately managed pension funds are still under strong government control aimed to protect the pension savings of people and reduce the social tension in the country generated by the transition to market economy. The new Social Code liberalizes somewhat the regime for investment of the funds of insured persons by private pension insurance companies. The share of funds for the purposes of social security, which can be invested in foreign securities with higher yield for the insured persons, is increased, but data about investments by pension funds as of November 2002 reveal that pension insurance companies still refrain from investments abroad and invest funds for the purposes of social security mainly in government-issued-and-guaranteed securities and in domestic bank deposits. Successful capital market operation and a higher real income policy would generate higher confidence in the Bulgarian pension system and would ensure satisfactory pension income for the insured persons. Bulgaria's level of pensions paid from the State Social Security is very low compared to other Central and Eastern European countries (USD 42 for 2001). This is a result of both the large share of Bulgaria's shadow economy and the poor collection of social security contributions by the National Social Security Institute. The two new measures implemented by the Ministry of Labor and

**Table 9. Average monthly retirement pensions in US dollars**

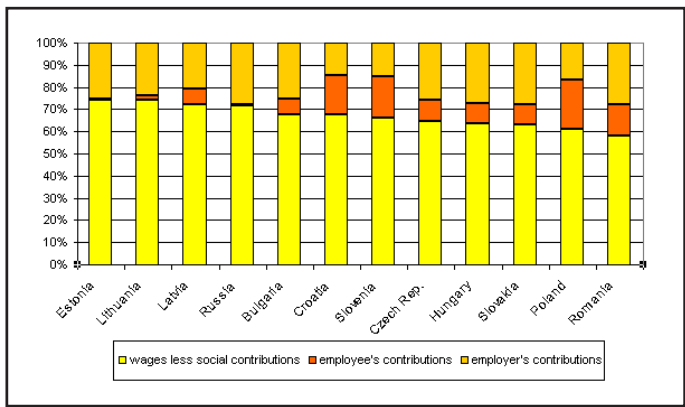
Country	1998	1999	2000	2001
<b>Bulgaria</b>	<b>35</b>	<b>36</b>	<b>41</b>	<b>42</b>
Czech rep.	139	167	160	176
<b>Estonia</b>	<b>80</b>	<b>95</b>	<b>82</b>	<b>85</b>
Hungary	122	125	117	134
Latvia	87	98	94	91
Lithuania	72	77	78	79
Poland	186	192	189	222
Romania	45	45	43	46
<b>Slovakia</b>	<b>118</b>	<b>109</b>	<b>108</b>	<b>111</b>
Slovenia	407	412	368	368

Source: Labor Costs in Central and Eastern Europe, CE-Research, <http://www.databasece.com/pension.htm>.

Social Policy and NSSI since the beginning of 2003 and concerning the introduction of minimum social security thresholds per sectors and professions and obligatory registration of labor contracts at the NSSI yield positive results and optimistic expectations for lower social security burden and higher pensions.

Bulgaria's State Social Security burden as a share of the cost of labor is close to the average level for CEE countries, but the social security burden for employers remains too high, which discourages small and medium-sized enterprises from creating employment. Government intentions are for smooth increase by 2009 of the social security burden for employees at the expense of that for employers, achieving in 2009 equal distribution (50:50) of the social security burden between employees and employers. The rather low wage level and the high unemployment level required to keep the employers/insured persons social security burden ratio at the level of 75:25 for another 2 years.

**Figure 1. Estimated share of obligatory social insurance contributions in cost of labour**



Source: Labor Costs in Central and Eastern Europe, CE-Research

### Major problems within the social security system include:

- Poor collection of social security contributions by NSSI, resulting in lower pensions.
- Increasingly higher deficit in the Pensions Fund, which is covered from the state budget.
- High social security burden which encourages inflow of labor force in the shadow economy.
- Discrimination of insured persons, because unlike all other insured persons, government officials and the military are insured for the account of the state budget.

- Persisting strong government restrictions on investments made by pension funds, which impedes the development of national complementary pension insurance.

Major objectives of the new Social Code which took effect since the beginning of 2003 are to create more legal guarantees for the funds of insured persons, to introduce new investment instruments for collected social security payments, to set up a mechanism to guarantee minimum rate of return on investments of obligatory pension funds and generally higher security for pension savings. As of end of 2002 pension funds assets amount to around BGN 310 m. This is a significant financial resource, which should be reasonably invested in the Bulgarian capital market thereby ensuring necessary funds to improve the competitiveness of Bulgarian companies.

**Table 10. Number of insured persons covered by the supplementary pension funds as of 30.11.2002 per pension insurance companies managed by the corresponding funds**

Pension insurance companies	Voluntary pension funds	Occupational pension funds		Universal pension funds
		I category	II category	
Total	478 521	16 653	138 193	1 115 494
Doverie AD	88 164	7 329	47 658	422 157
Suglasie AD	30 373	3 068	26 251	141 678
BPOD AD	34 344	1 053	9 939	98 745
SKPOK Rodina AD	19 227	692	5 372	61 054
Allianz Bulgaria AD	247 920	2 905	31 682	231 102
ING AD	14 293	515	4 974	89 851
Newton Sila AD	17 155	592	5 216	31 274
Lukoil Garant - Bulgaria* AD	27 045	499	7 101	39 633

Source: Social Security Supervision Department, FSC

**Table 11. Available net assets of supplementary pension funds as of 30.11.2002 per pension insurance companies managed by corresponding funds /BGN thousand/**

Pension insurance companies	Total	Voluntary pension funds	Occupational pension funds	Universal pension funds
Total	310 341	181 314	91 834	37 193
Doverie AD	75 843	28 172	34 217	13 454
Saglasie AD	28 449	7 233	16 566	4 650
BPOD AD	18 738	10 695	5 050	2 993
SKPOK Rodina AD	14 938	10 219	2 778	1 941
Allianz Bulgaria AD	129 988	97 718	23 818	8 452
ING AD	15 356	9 732	2 203	3 421
Newton Sila AD	5 598	2 619	2 091	888
Lukoil Garant - Bulgaria AD	21 431	14 926	5 111	1 394

Source: Social Security Supervision Department, FSC

### 3.1.2. Social Assistance

**Priorities of social assistance activities** laid down in the new Social Policy Strategy include: changing social assistance philosophy from welfare benefits to support for employment; creating a system of care standards for underprivileged people; improving the management structure of the social assistance system by fiscal decentralization and decentralization of central government, involving partners (municipalities, non-government organization, the business) in delivering social services to improve the quality of life; creating a quality control system for care and services delivered to children and old people.

In recent years the social assistance system registers shortage of funds for welfare benefits. Heavy unemployment in certain municipalities is one reason for the increasingly higher number of people on benefits. The large share of the shadow economy does not allow information about the incomes of persons and families on welfare benefits to be collected, which impedes the effective distribution of the funds for social assistance. Most institutions delivering social services have obsolete material equipment, conditions for civil control of the observation of human rights are not created. There is a need of stricter control of the payment of welfare benefits and of the investment costs of institutions delivering social services.

The Family Allowances for Children Act passed in March 2002 replaced the obsolete 1968 Decree to Encourage Births. Its objective is to guarantee more adequate target assistance. Amendments to the Act on the Protection, Rehabilitation and Social Integration of Disabled Persons were passed in December 2001. Their objective is to clarify the structure and membership criteria of the National Council for Rehabilitation and Social Integration (a Consultative Body at the Council of Ministers) and to determine the conditions for target assistance.

Amendments to the Rules on the Implementation of the Social Assistance Act approved by CoM's Decree No. 50/5.03.2002 enabled to provide in kind target heating benefits which are not used for the purpose for which they are given, and the amounts for the persons and families entitled to benefits, who use electricity for heating to be transferred directly by the municipal welfare services to the electricity distribution companies. These measures are aimed at higher control on granted welfare benefits.

**Important changes in the social assistance area** characterized the past 2002. The passed Act on the Family Allowances for Children and the Rules for the Implementation of the Act enabled more effective allocation of limited resources to the social groups in highest need of these resources, i.e. old people living alone, disabled people and single parents with children up to 3 years. Specific coefficients guarantee higher welfare benefits for these most vulnerable social groups. Consequently, the guaranteed minimum income of people between 65 and 75 age who live alone increased from BGN 40 to BGN 68 (EUR 34), and for those of 75+ age - BGN 80 (EUR 40). The guaranteed income for disabled people increased from BGN 48 to BGN 60 (EUR 30), and for single parents with children up to 3 years - from BGN 48 to BGN 60 (EUR 30).

The second positive element is the attempt to achieve coordination of labor market policy and social assistance and the changed mechanism of providing assistance to people of active age. Some of them will receive labor remuneration instead of welfare benefits (From Welfare Benefits to Employment) and will have guaranteed access to education and training programs. The Personal Assistant Project within the National Program from Welfare Benefits to Employment is expected to generate in 2003 assistance to more than 7000 families who take care of infirm or disabled persons. BGN 217 m (around EUR 109 m) is allocated from the state budget for this initiative of the Ministry of Labor and Social Policy.

**The philosophy of legislative changes in the social assistance area can be formulated as bringing more order and justice in state funds outlay, providing social assistance to people who really need it, and ensuring employment to socially assisted people of active age.**

**The survey Social Assessment of the Effect of Future Changes of Social Assistance** conducted in October 2002 revealed that positive attitudes towards Bulgaria's social assistance system prevail as a result of the completed and steadily operating legal and institutional basis of social assistance. The social assessment reveals clear attitudes of approval of the new social policy model based on active approach, differentiated assistance, fiscal decentralization and policies coordination. Results show

that the society has positive attitude towards social activities demonopolization, which implies future involvement of companies and non-government organizations in the performance of social activities.

In summary, **basic recommendations to Bulgaria's social assistance policy** include:

- There is a need **to clearly outline government and municipal rights and obligations in the financing and management of institutions delivering social services.** Enhancing the decentralization in the financing and management of the social services system is a guarantee for efficient utilization of allocated resources and ensuring higher quality of Bulgarian social services.
- The focus should be on **improving the administrative capacity of the social assistance system and promoting the coordination of various structures at national, regional and municipal level by building an integrated information system**, with a view to guarantee efficient operation of the social assistance system.
- There is a need to **develop a Chart of the Rights and Obligations of Socially Assisted Persons and Social Worker's Code of Ethics.**
- There is a need of **regular monitoring of the social assistance system** with a view to identify problems and take timely decisions to overcome them.
- There is a need of higher **coordination of the income, the social assistance, and the labor market policy.**
- The coordination of the work of social institutions can be improved by introduction of **an integrated information system** to facilitate the coordination of the social assistance and the employment promotion policy.

### 3.1.3. Social Dialogue

The **Employment Promotion Act** of 1 January 2002 regulates social dialogue promotion and higher opportunities for social partners to influence the employment policy. The set up of interim Employment Commissions at the Regional Councils for Regional

Development with the participation of social partners and the non-government sector, the set up of Councils for Cooperation at the Employment Agency units on a tripartite principle for control of the implemented active labor market policy, and the set up of a National Employment Promotion council as a standing cooperation and consultative body for employment policy development operating on a tripartite principle guarantee legal involvement of social partners in employment policy development.

On 15 February 2002 the Government signed a **Chart for Social Cooperation with Bulgarian Workers, Employees and Employers Organizations.** The Chart contains the will of the parties to adhere to the principles of social cooperation: partnership by way of the tripartite principle, guaranteed social peace, continuity and coordination, transparency and mutual notification. On national level **the Council of Ministers of the Republic of Bulgaria and the representative organizations of workers and employees and of employers signed a Cooperation Agreement**, which formed the basis of future active social dialogue and cooperation between employers, trade unions and the state.

Branch councils for tripartite cooperation already operate at the Ministry of the Economy, the Ministry of the Interior, the Ministry of Regional Development and Public Works, the Ministry of Transport and Communications, and the Ministry of Healthcare. **There is a need to encourage the set up of such branch councils for tripartite cooperation in other ministries with a view to promote the involvement of social partners in European integration activities.**

On company level, **pilot workers councils** were set up as an experiment **in Bulgarian private companies.** These are an attempt to implement the German model for coordination of the interests of hired labor and owners through dialogue and direct negotiations between workers and employers.

Overall, 2002 can be characterized as a year of absence of serious industrial conflicts and moderate social tension.

### 3.2. Challenges of EU Accession Regarding Social Policy (Social Insurance, Social Assistance and Social Dialogue)

Social security issues are discussed in Chapter 2: Free Movement of People, of the European legislation, which covers four major areas: mutual recognition of professional qualifications, civil rights, free movement of workers and **coordination of social security systems**. Coordination of the social security systems of EU Member States aims at providing permanent social security to people looking for jobs on labor markets in other EU Member States. The European Community requires coordination of the measures laid down in the national legislations rather than harmonization of the social security legislation of current EU Member States and candidate countries. Measures in the area of social security systems coordination cover all EU Member States and EFTA (Norway, Liechtenstein, and Iceland). EU candidate countries have experience in the signing of bilateral agreements with EU Member States. Recommendations are to promote this process with a view to provide guarantees that the persons who will exercise in the future their right to free movement within the Community, will not be sanctioned on this basis in the social security area.

Bilateral social security agreements regulate the provision social security and the grant of short-time compensations and pensions from the obligatory social security funds, where a person worked and was insured in both countries to the agreement simultaneously or in succession. **Eleven social security arrangements, conventions and agreements between Bulgaria and other countries are currently effective**. Negotiations for new agreements with Macedonia, Cyprus, Croatia, Switzerland and Hungary are in progress. The basic principles adhered to in the implementation of social security agreements include:

- The principle of application of one national legislation for the provision of social security.
- The principle of equal treatment as an instrument to overcome direct and indirect discrimination on account of nationality.
- The principle of preserving acquired and pending social security rights.

Social protection and social dialogue issues are also discussed in Chapter 13: Social Policy and Employment. **Social protection** systems are financed and organized on national level by the different EU Member States, but the Community requires from applicant countries to have sustainable systems to enable their coordination with the those operating within the EU, which develop at a high pace.

Promoting **social dialogue** and delegating additional powers to social partners are important focus points of European employment and social policy legislation. EU candidate countries must prove that they attach due importance to social dialogue and that social partners are sufficiently powerful to be able to implement their responsibilities on national and on European level and get actively involved in the consultation process of carrying through employment and social policy bills. Social partners must take part in employment policy development and implementation on national and on European level. It is important for candidate countries to develop tripartite structures (government, trade unions, employers' organizations) as well as independent representative bilateral social dialogue, with a view to guarantee effective involvement of the social partners in candidate countries in the social dialogue on European and on national level.

## 4. Labor Migration Policy

### 4.1. Push and Pull Factors

Major factors having effect on labor migration and requiring special government attention with a view to promote or restrict potential migration from Bulgaria to the EU include:

#### 4.1.1. Demographic Processes

Bulgarian demographic processes involving increasingly lower birth rate and aging population have unfavorable effect on the active people/pensioners ratio, which results in an inefficient social security system discouraging young people from participation as it continues to function of the cost-coverage principle and encourages labor emigration. There is a need of measures to encourage births, lower the social security burden for the employed population

and create incentives for realization of young people on the national labor market.

#### 4.1.2. Labor Market Situation

According to Labor Force Survey data Bulgaria's 2002 unemployment level is lower compared to the previous year, but unemployment remains too high compared to the average unemployment level in the European Union. According to Eurostat data, in January 2003 EU unemployed account for 7.9 percent of the Union's population, with Luxembourg (2.7 percent), Holland (3.1 percent) and Austria (4.1 percent) registering the lowest unemployment levels. Austria's low unemployment rate as well its geographic proximity to CEE countries - candidates for EU membership make the country a major destination of potential migration processes in future EU Member States.

The so-called "brain-drain" from Bulgaria to developed EU Member States is particularly intensive in recent years. The fact that investments in human capital made in Bulgaria have no return generates concern. Nearly two thirds of migrants are in the (10-39) age interval. According to the Census taken as of 1 March 2001, the population in the (20-39) age interval is expected to form the basic portion of future emigrants to the EU. Desire to migrate is also most frequent in the 20-29 age group (37 percent).<sup>7</sup>

Bulgarian young people constitute a significant share of the underprivileged people on the labor market. The problems they have in finding a job result in the first place from absence of working experience, of financial resources; insufficient information, consulting and orientation of young people to entrepreneurship; as well as from the absence of effective lending system for young and promising entrepreneurs. These are the basic lines along which the Govern-

**Table 12. Demographic indicators**

	2000	2001	2002
Population, as of 31.12., number	8 149 468 *	7 891 095 **	7 845 499 ***
Average life expectancy, total (in years)	71.7 *	71.8 **	71.8 ***
Average life expectancy, female (in years)	75.3	75.2	75.3
Average life expectancy, male (in years)	68.2	68.5	68.6
Average age of the population (in years)	39.9	40.4	40.6
Population under, at and over working-age, total	100.0	100.0	100.0
Population under working-age - %	16.8	16.3	15.9
Population at working-age - %	58.3	59.2	60.1
Population over working-age - %	24.9	24.5	24
Natality rate (per 1000 persons)	9.0	8.6	8.5
Mortality rate (per 1000 persons)	14.1	14.2	14.3
Natural growth (per 1000 persons)	-5.1	-5.6	-5.8

Note: \*Data regard the period 1998-2000  
 \*\*Data regard the period 1999-2001  
 \*\*\*Data regard the period 2000-2002  
 Source: National Statistical Institute

<sup>7</sup> [http://www.mlsp.government.bg/bg/projects/youths-2/docs/ LAST\\_YOUTH\\_2MODULES\\_NAPE2002.doc](http://www.mlsp.government.bg/bg/projects/youths-2/docs/ LAST_YOUTH_2MODULES_NAPE2002.doc)

ment should take efforts with a view to stop the “brain-drain” and to motivate young people to look for jobs on the Bulgarian labor market.

#### 4.1.3. *Income Gap*

Higher payment rates in EU Member States are the primary factor encouraging labor migration from Bulgaria to the EU. According to Eurostat’s annual labor market survey, Bulgarian labor is the cheapest in Europe. In Bulgaria hourly pay amounts to an average of EUR 1.35, which is the lowest rate compared to the 15 EU Member States and the 12 countries holding EU accession negotiations. Average earnings per hour in candidate countries are five times lower compared to the average EU level of EUR 22.70. The above data reveal that real income growth in the years up to Bulgaria’s accession to EU must be set forth as a fundamental objective of national economic and social policy, with a view to prevent large-scale migration flows from Bulgaria to the EU.

#### 4.1.4. *Qualification of the Labor Force and Demand for Services*

Recognition of diplomas and qualifications is an important factor for the decision to migrate taken by educated Bulgarians. Mutual recognition of diplomas and qualifications is one of the four major areas of the free movement of people in EU Member States. After adoption of the European legislation in this area and following Bulgaria’s future accession to the EU young Bulgarians with university education may get highly interested in looking for jobs on the labor markets of current EU Member States. Everything will depend on the social and economic situation in the country, which constitutes real challenge for Bulgarian rulers if they want to have return on government investments in the education of these young people.

#### 4.1.5 *Geographic Proximity*

According to NSI’s 2001 survey of potential migration from Bulgaria, conducted after the International Organization for Migration method, preferred destinations of Bulgaria’s labor emigration include countries like Germany (25 percent), the USA (15 percent), Greece (11 percent), Spain (9 percent), Great Britain (8 percent) and Italy (5 percent). Transport costs to the desired emigration destination do matter, as they

become in some cases major barrier to the emigration of Bulgarians as a result of their low standard of living. Data about the countries preferred by Bulgarians to emigrate reveal that geographical proximity is an important factor for the emigration from Bulgaria and there is a need to identify measures like bilateral agreements with such countries with a view to avoid serious pressure on their labor markets after Bulgaria’s accession to the EU.

#### 4.1.6. *Traditions and Networks*

Countries traditionally preferred for emigration by Bulgarians are another important factor, which should be taken into account upon implementation of Bulgarian migration policy. Germany is one of the countries with which Bulgaria has signed bilateral employment agreements, and also the country expecting the largest migration wave after the future fifth EU enlargement, which will cover the 10 new CEE countries.<sup>8</sup> Future bilateral labor exchange agreements in this field with countries preferred for migration by Bulgarians will alleviate social tension and the concerns of these countries about Bulgaria’s future EU accession.

#### 4.1.7. *Ethnic and Political Problems*

Ethnic and political problems in a country encourage emigration rather than temporary labor migration. This factor may have effect mainly on ethnic groups like Bulgaria’s Roma population which is underprivileged on the labor market, uneducated and unqualified and generally engages in illegal activities in the country and abroad. Implemented measures to integrate the Roma people are insufficient. There is a need to develop special programs to improve their education level, to provide vocational training in accordance with current labor market demand, and increase their awareness of EU programs targeting social isolation in CEE countries.

<sup>8</sup> In 2001 under bilateral agreements with Germany regarding employment of workers for execution of contracts among companies and for enlargement of professional qualifications total number of 2 139 Bulgarian citizens have left the country. Under agreements with Germany regarding seasonal employment in the field of hotel and restaurant business 1 266 people have received periodic labor contracts. 221 young people have traveled to Germany regarding summer employment, The New Migration Policy of Bulgaria. Bilateral labor force exchange agreements



### 4.1.8. Cultural and Linguistic Barriers

Socio-psychological and cultural factors have important role in the decision to work abroad, particularly where such decision is taken for a longer period of time. In principle the need to study a foreign language is a serious barrier for most people. This is particularly valid for older Bulgarians who have lost their jobs as a result of the restructuring and privatization of Bulgarian economy. Their limited financial resources, socio-psychological attitudes and lower mobility take them out of the group of potential emigrants after Bulgaria's accession to the EU. The situation is quite different for young Bulgarians. They have rather good language training and are ready to move and find jobs in countries offering higher standard of living compared to Bulgaria.

## 4.2. Migration Processes

**Table 13. Migration flows 1992-2001**

Emigration	196 thousand people
Immigration	19 thousand people
Negative natural growth	337 thousand people

Source: National Statistical Institute

### 4.2.1. Emigration

According to data from the census of Bulgarian population taken in 1992 and 2001, foreign migration amounts to 177 thousand people (196 thousand emigrants and 19 thousand immigrants), with an average of 22 thousand emigrants per year. According to the parallel survey of potential emigration carried out by National Statistical Institute in 2001 after the International Organization for Migration method, potential Bulgarian emigrants are divided into three categories: **permanent emigration, temporary emigration, and other.**<sup>9</sup>

Data about potential emigration reveal that around 80 percent of the population between 15 and 60 years do not intend to leave the country, which means that they are not potential emigrants. In recent years Bulgarian emigration was mainly oriented to countries like Germany - 23 percent, the USA - 19 percent, Greece - 8 percent, Spain - 8 percent, Great Britain - 6 percent, Italy - 6 percent, Canada - 5 percent, France - 4 percent, etc. **In terms of migration destinations preferred by the different**

**Table 14. Categories of potential emigration**

#### **“Permanent emigration” - 15 percent of the population.**

Potential emigrants, who state that they will probably go to live, work or study abroad for more than a year (emigrants - 8 percent and labour emigrants - 7 percent).

#### **“Temporary emigration” – 5 percent of the population.**

Potential emigrants who state that they will probably go to work or study abroad for less than a year.

#### **“Others” – 10 percent of the population.**

Persons who state that this year or in the next years they will probably go abroad for a short time as tourists or to visit relatives and friends.

Source: National Statistical Institute

**categories of potential migrants, labor migrants mainly look for jobs on the labor markets of countries like Germany (25 percent), the USA (15 percent), Greece (11 percent), Spain (9 percent), Great Britain (8 percent) and Italy (5 percent).** The basic factors having effect on the destinations preferred by labor migrants include higher labor pay level (the USA, Great Britain, Italy), geographic proximity to Bulgaria (Greece and Germany), bilateral labor exchange agreements signed (with Germany, for example), as well as emigration traditions (Germany, Greece). **There is a need to encourage the signing of more bilateral employment agreements with older EU Member States in the period before accession,** with a view to avoid the expected initial pressure on the labor markets of the above EU Member States by Bulgarian labor migrants.

An estimate of emigration from Bulgaria to the EU has been developed for the period 2002-2007. It is based on the census of the population at 15-60 ages (5 029 thousand people) and on the expected fulfillment of potential migration attitudes, and the expert evaluation of the coefficient according to the International Organization for Migration method is 12-15 percent. **This survey calls for the conclusion that**

<sup>9</sup> National Statistical Institute data

**in the period 2002-2007 one cannot expect strong emigration pressure from Bulgaria to EU**, which could have material effect on the efficient operation of labor markets in EU Member States and generally destabilize these markets.

#### 4.2.2. Immigration

Fears of current EU Member States about massive migration flow from CEE countries result from their expectations that potential labor migrants from these countries will join by migrants from neighbor countries as well as migrants from the Middle East and Africa. That is why, it is important to study the characteristics of the immigration flow to Bulgaria in previous years with a view to estimate the potential immigration inflow after Bulgaria's accession to the EU.

According to Employment Agency's data, a total of 2205 work permits were issued to foreigners in Bulgaria in the period 1994-2001 (1384 new and 821 extended). **The highest number of work permits for Bulgaria was issued to nationals of the USA (332), Turkey (169), Ukraine (165), Russia (152) and Greece (135).** A glance at the qualification of these foreign workers reveals that the top management personnel employed by foreign investors from European countries and the USA registers the highest number. Next come consultants and engineers and technicians; foreign professors in secondary schools and universities are third in number. According to data by the bodies delivering administrative services to foreigners, as of June 2002 4 758 foreigners have got permanent stay permits on account of registration of business activity, 516 people - on the grounds of employment under labor contract, and 2397 people on the grounds of concluded civil marriage with a Bulgarian national or with a foreigner with permanent stay permit. Business activity of foreigners on the territory of the Republic of Bulgaria has positive effect on the national labor market because it generates employment, guarantees social security and health insurance contributions for the State Social Security and improves the competitiveness of Bulgarian economy through the introduction of new machines and technologies in industry. The low cost of labor in Bulgaria, heavy unemployment, the absence of well-directed tax policy in support of small and medium-sized enterprises, and the high share of the shadow economy, which generates

unfair competition between Bulgarian and foreign economic agents on the territory of the country, constitute a very important factor which has restrictive effect on the immigration flow to the country.

Data about the immigration flows to Bulgaria reveal lack of concern about higher immigration to the country in the next years. **There is a need to encourage immigration measures taken by through the signed bilateral labor force exchange agreements**, with a view to curb illegal migration in the country and lower the concerns of current EU Member States that Bulgaria could become a point of entry of illegal migrants on EU territory.

### 4.3. Policies Regulating Labor Migration

There are **several major objectives of Bulgarian migration policy in the area of labor migration**<sup>10</sup>:

- To develop regulated forms of temporary labor emigration.
- Effective labor market protection.
- To create favorable conditions for integration of the labor force in the country.
- To implement bilateral and multilateral agreements in the field of labor migration and the return of labor migrants to Bulgaria.

#### 4.3.1. Measures Regarding the Regulation of Labor Emigration

**Labor emigration measures** target development of temporary regulated labor migration by way of:

- Creating legal opportunities and control of the implementation of various forms of temporary regulated labor migration through the Employment Promotion Act, the Ordinance on the Terms and Procedure of Carrying Out Mediation Activity for Notification and Employment and through Bilateral Agreements for Labor Force Dispatch and Exchange.

<sup>10</sup> Roundtable: Free movement of workers and access to labor markets of EU member states, Ministry of Labor and Social Policy and European Integration and International Affairs Department, Vladimir Kalchev, The New Migration Policy of the Republic of Bulgaria, 10 December, 2002, Sofia

- Continuous control of the implementation of effective bilateral agreements for labor force dispatch and exchange.
- Intensification of the mediation activity for notification and employment of Bulgarian nationals in other countries on the basis of effective agreements.
- Expanding the bilateral cooperation in the field of employment and implementing active policy with a view to sign more bilateral agreements for labor force exchange or dispatch to other countries.

According to the Ministry of Labor and Social Policy's data, **60 agencies for employment abroad in 20 countries have been issued agency licenses**. These private labor agents are expected to develop in the next years as an alternative of the Employment Agency in the delivery of agency services for employment in the country and abroad. The basic objective is to improve the quality and scope of their services in accordance with actual labor market needs.

The different types of bilateral agreements for labor force exchange are the basic Bulgarian regulatory measures for temporary labor migration. These include the so-called **Employment Agreements**. The labor force exchange principle (**two-way labor migration**) is applied for agreements with EU Member States, and the labor force dispatch principle is (**one-way labor migration**) is applied for agreements with other countries as a measure to curb illegal labor migration in Bulgaria and as a guarantee for the successful integration of the Bulgarian labor market in the EU one. It is recommended to have labor force exchange agreements signed between Bulgaria and EU Member States on national level, as well as on regional and local level, with a view to promote the free movement of labor force within the mobility context, and to solve employment problems at local level. This is a successful measure to cover temporary shortages of labor force in Bulgaria and current EU Member States in accordance with the short-term economic and social situation on local level avoiding market pressure on national level. An inter-ministerial Employment Agreements Work Group was set up at MLSP in 2001. Its tasks involve: analysis of effective employment agreements, developing drafts of new labor force exchange agree-

ments with other EU Member States and with third countries, making proposals for amendments to the national migration legislation.

To date, **Bulgaria has signed bilateral employment agreements with the Federal Republic of Germany** for employment of workers from Bulgarian companies under work contracts in FRG and on employment of workers to improve their professional and language skills; with the **Republic of Portugal** for mutual employment of nationals of the two countries (signed on 26 September 2002), with the Government of the **Grand Duchy of Luxembourg** for exchange of trainees (signed on 06 December 2002), and with the **Czech Republic** for mutual employment of Bulgarian and Czech Republic nationals. Out of the countries, which are not EU members, Bulgaria has signed an agreement for exchange of trainees with **Switzerland**. Drafts of bilateral employment agreements with the Kingdom of Spain, the Republic of Greece, the French Republic, the Republic of Austria, the United Kingdom of Great Britain and Northern Ireland are at different coordination phases.

**A tendency to simultaneously sign employment agreements and readmission and social security agreements has been observed in recent years.** The aim is to better protect the interests of migrants, of the host country and of the dispatching country, and to improve the fight against illegal migration. **Bulgaria has signed readmission agreements with all EU Member States except Great Britain and Ireland with which negotiations are in progress.** This proves Bulgaria's intentions to join in EU efforts to fight illegal migration, which exerts strong pressure on labor markets in the countries concerned.

Concerning the cooperation in the fight against illegal migration and crime on transnational and trans-regional level, **there are 21 effective intergovernmental and inter-ministerial cooperation agreements with European countries**, which reveals Bulgaria's efforts to get successfully integrated in the European structures for fight against illegal migration and crime that impede in principle the security and the effective operation of European labor market.

### 4.3.2. Measures Regarding the Regulation of Labor Immigration

**Labor immigration measures** target in the first place labor market protection and development, control of the employment of foreigners in Bulgaria and equal treatment of legally employed foreign workers.

- Legal guarantees for full control of the observation of employment regulations have been issued.
- Legislative amendments concerning the admission of foreigners as employees have been made (a new Ordinance on the Terms and Procedure of Issuance, Non-issuance and Withdrawal of Work Permits of Foreigners in the Republic of Bulgaria was passed in April 2002. It envisages admission of members of the families of workers from EU Member States to the labor market without a 24-month waiting period).
- Ordinance on the Terms and Procedure of Issuing Permits to Carry out Free-lance Activities in the Republic of Bulgaria to Foreigners was passed in September 2002. It envisages exclusion of EU Member States nationals from the licensing arrangements for carrying out free-lance activities in the country.
- European and international standards concerning the equal treatment of Bulgarian nationals and migrant workers from other countries admitted to the labor market have been reached.
- The Employment Promotion Act contains texts allowing direct implementation of Regulation 1612/68 concerning the elimination of the licensing regime and the acquisition of equal rights in applying for a job and getting employed upon Bulgaria's accession to EU.

**The work permit is the basic instrument of labor migration control both in EU Member States and in Bulgaria.** It guarantees equal conditions of work, pay, paid leave, etc. with those for host country workers. In EU such permit is issued following assessment of the labor market situation in the host country, and the principle is to employ nationals of non-EU countries only where there are no candidates for the job from the corresponding EU Member State or other EU Member States. **There**

**are two basic types of stay permits (for temporary and permanent stay) and two types of work permits (short-term and long-term).**

The basic rule is that the validity of the work permit shall not exceed the validity of the permit to stay. Where foreigners fail to observe the validity, they are prohibited to enter the corresponding country as well as the whole Schengen area, because the violator is put on the general list of persons unacceptable in EU Member States.

## 4.4. Challenges of EU Accession Regarding Free Movement of Workers

Major concerns of current EU Member States about the expected EU enlargement include in the first place a fear that lower wages and social protection levels in future EU Member States could result in intensive redistribution of investments and employment and large migration inflows. The concern about possible **“social dumping”** generated wide debates, which resulted in EC's proposing to future EU Member States a transitional period before full liberalization of the free movement of workers within the EU.

International migration trends are among the reasons for the concerns of current EU Member States about a strong immigration pressure from CEE countries after EU enlargement. The latest publication of the Organization for Economic Cooperation and Development (**OECD**), **International Migration Trends**, reveals increasingly high immigration flows in OECD countries, notwithstanding the slowdown of global economic growth and the strict border control in connection with antiterrorism. An upward trend is observed in all migrant categories - refugees, asylum-seeking migrants, members of the families of workers in OECD countries, or labor migrants. Surveys reveal that Great Britain, Germany and the USA have admitted the highest number of asylum-seeking migrants. But the number of admitted asylum-seeking migrants registers highest growth in CEE countries, which generates concerns in current EU Member States that after the accession of the ten CEE countries in 2004, as well as after the accession of Bulgaria and Romania in 2007 this process will intensify and will exert strong pressure on the labor mar-

kets of EU Member States and on the standard of living of their people. The report states that in the last two years OECD countries have implemented various immigration policies with a view to curb immigration flows to them. Some countries have adopted more restrictive rules on the entry and length of stay of foreigners on their territory. Austria, Denmark and Holland have put barriers for relatives and families joining foreigners working on their labor markets. Australia, Canada, the USA, Great Britain and Norway have implemented a policy of labor migrants selection, focusing their preferences on highly skilled workers. The planned EU enlargement by 10 new countries intensifies the fears of a heavy wave of labor migrants from Eastern Europe. Major concerns are that immigrants from third countries may enter the labor markets of EU Member States exactly through the territories of EU candidate countries.

The free movement of people is one of the four fundamental freedoms, which along with the free movement of goods, capital and services is an integral part of the internal market of the European Union. The Acquis in this area involve mutual recognition of professional qualifications, civil rights, free movement of workers and coordination of social security systems. The free movement of workers within the EU is a particularly sensitive subject at EU level, given the labor market problems most EU Member States have today.

Concerns about a wave of immigration from new Member States that could exert serious pressure on the labor markets of the current 15 EU Member States and on their social security systems are the reason for EC's proposing to candidate countries a transitional period in the free movement of workers area. Thus the maximum transitional period when new EU Member States will not have access to the labor market of the Union is seven years. The applied scheme is 2+3+2, which means that after the first two years restrictions may be eliminated provided that the corresponding country does not constitute migration threat, but the transitional period can be extended up to 7 years where the new EU Member State commits serious violations of the labor market of the Union. EU did not request a transitional period only for Malta and Cyprus. It applied a common approach to all other countries. The fact that countries like Sweden, Holland and Portugal have declared that they will not introduce transitional periods for candi-

date countries after the latter's accession to the EU reveals that they do not expect serious immigration flow to their countries which could exert pressure on their labor markets. The transitional agreement also includes other important aspects such as an immobility clause, according to which the labor markets of current EU Member States cannot be more closed than upon the accession of the new Member States. What is more, current EU Member States must employ with priority nationals of candidate countries over nationals of third countries. Only Austria and Germany where the highest immigration pressure is expected have the right to apply protective measures with a view to eliminate or prevent serious disturbances in certain sensitive areas of the service sector, which might result from the trans-frontier service supply.

### **In June 2002 Bulgaria temporarily closed Chapter 2: Free Movement of People**

, which means that our country accepts the negotiated transitional period. Given the majority of European and national surveys, which conclude that Bulgaria will not be a serious migration threat to the labor markets of current EU Member States, elimination of the transitional period after the first two years following Bulgaria's accession to the EU is expected. Our country has taken the necessary steps to regulate labor force movement on the basis of bilateral agreements with current EU Member States and candidate countries, but there are recommendations to promote this process with a view to the intensified liberalization of the labor market of the Union.

### **Challenges for Bulgaria related to the free movement of workers**

include in the first place signing of labor force exchange agreements with all EU Member States and with the candidate countries; promotion of police and customs cooperation through intensified data exchange; analysis and coordination of joint Bulgaria-EU surveys of the current movement of migration flows during the period till Bulgaria's accession to the EU as well as during the transitional period; better management of Bulgaria's external borders to improve the efficiency of the fight against illegal migration. Regular monitoring of the implementation of European migration and security legislation by Bulgaria would relieve concerns of current EU Member States about heavy immigration wave which would exert strong pressure on their labor markets. It is very important to pay special attention to the factors which would encourage labor mi-

gration from Bulgaria to the EU, and to take due measures and implement the necessary policies in this area with a view to create favorable economic and social environment for the realization of young people in Bulgaria instead of encouraging the “brain-drain” process.

The advantages new migrants will generate for current EU Member States should not be neglected. The shortage of unskilled and highly skilled labor force on the labor markets of these countries will be overcome; the old people needing more health and social services/people of active age ratio will be improved. One should admit that the future EU enlargement may well prove a successful formula of solving important social and demographic problems in the European Union.

Effective and open labor markets are as important to the EU as the effective and open markets of goods and services<sup>11</sup>. Lisbon set the ambitious task to achieve by 2010 a general employment rate of 70 percent and to increase female employment to 60 percent in the EU, which requires coordination of active labor market policies throughout Europe. This is the way to make Europe the most dynamic and competitive knowledge-based economy.

<sup>11</sup> Center for Economic Development (2003): Lisbon Agenda for Economic Reform

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# APPENDICES

**Table A1. Main macroeconomic indicators**

Indicators	1997	1998	1999	2000	2001	2002
GDP, cup, million USD	10 198	12 735	12 946	12 597	13 557	15 500*
Real GDP per capita (PPP), EU-15=100, %	27,63	28,19	28,34	25,76	24,57	31,37*
Inflation (CPI-100), y, py=100, %	1 058,4	18,7	2,6	10,3	7,4	5,8
Current account balance, (as % of GDP)	10,3	-0,5	-5	-5,6	-6,5	-4,4
Foreign direct investments (as % of GDP)	4,9	4,2	6,3	7,9	5,1	3
Exchange rate BGN/USD, avp, BGN	1,68187	1,76036	1,8364	2,12334	2,18472	2,07697
Exchange rate BGN/USD, eop, BGN	1,7765	1,6751	1,94687	2,10191	2,21926	1,88496
Gross external debt, million USD	10 408,5	10 891,9	10 913,9	11 201,8	10 618,7	10 932,9
Gross external debt, as % of GDP	100,4	85,5	84,2	88,9	78,3	70,5
Domestic government and government guaranteed debt, million BGN	2 780,5	3 101,7	2 963,3	1 767,2	1 860,5	2 111,7
Domestic government and government guaranteed debt, as % of GDP	15,95	13,83	12,46	6,9	6,6	6,5
BNB International Currency Reserve, million USD	2474,1	3051,1	3221,6	3460,3	3580,3	4746,8
Base interest rate, nominal, December, %	6,79	5,03	4,46	4,62	4,67	3,35
Base interest rate, effective annual, December, %	6,97	5,13	4,54	4,7	4,75	3,39

\* Preliminary data

**Table A2. Socio-demographic data**

Indicators	1997	1998	1999	2000	2001	2002
Population, as of 31.12, number	8 283 200	8 230 400	8 190 876	8 149 468	7 891 095	7 845 499
Population, annual average, number	8 312 100	8 256 800	8 210 600	8 170 172	8 020 282	.
Working-age population (age 15-64), as of 31.12, number	4749476	4750328	4752804	4748150	4732445	.
Life expectancy, total	70,48	-	71,01	71,7	71,9	71,8
Life expectancy, male	67,07	-	67,6	68,15	68,6	68,6
Life expectancy, female	74,31	-	74,64	75,34	75,3	75,3
Annual total income of households, average per capita, nominal, USD	573	813	818	741	727	
Annual total expenditure of households, average per capita, nominal, USD	469	686	708	651	650	
Annual monetary income of households, average per capita, nominal, USD		610	650	600	608	
Annual monetary expenditure of households, average per capita, nominal, USD	596	631	584	590		

**Table A3. Structure of household expenditures.**

Indicators	1997	1998	1999	2000	2001	2002
Total household expenditure	100	100	100	100	100	.
Total consumer expenditure	85,8	84,4	85,5	84,9	86,1	.
Food and non-alcoholic beverages	54,3	47,8	44	44,1	44,9	.
Alcoholic beverages, tobacco	3,3	3,4	4,1	3,8	3,7	.
Clothing and footwear	5,4	5,8	5,2	4	3,6	.
Housing, water, electricity, gas and other fuels	8,8	10,2	11,9	12,2	12,1	.
Furnishing and maintenance of the house	2,7	3,2	3,3	2,8	2,9	.
Health	2	2,4	2,8	3,6	3,9	.
Transport	4,4	5,1	5,7	5,2	5,3	.
Communications	1	1,3	2,1	2,5	3,3	.
Recreation, culture and education	1,8	2,6	3,3	3,3	3,2	.
Miscellaneous goods and services	2,1	2,6	3	3,3	3,2	.
Taxes	5,1	5,2	4,3	3,7	3,1	.
Household plot	3,8	3,9	3,1	3	3,1	.
Other expenditure	5,3	6,6	7,1	8,5	7,7	.

**Table A4. Key labor market indicators**

Indicators	1997	1998	1999	2000	2001	2002
Economic activity rate (LFS), %	51,6	50,4	49,2	47,5	48,1	48,4
Employment rate (LFS), %	43,9	42,4	40,8	39,7	38,7	40,3
% of total employment (LFS) in						
a. Agriculture					8,6	8,5
b. Industry					32,7	32,8
c. Services					58,4	58,6
d. Unknown					0,4	0,1
% of total employment (LFS) in						
a. Private sector					60,3	62,6
b. Public sector					39,5	37,2
c. Unknown					0,2	0,2
Employees (LFS), thousands	2606,1	2530,6	2437,2	2364,4	2263,2	
a. Private sector	747,4	889,2	990,7	1087,4	1225,8	1333,5
b. Public sector	1858,7	1641,4	1446,5	1277	1037,4	
Employees (LFS), %	100,0	100,0	100,0	100,0	100,0	
a. Private sector	28,7	35,1	40,6	46,0	54,2	1333,5
b. Public sector	71,3	64,9	59,4	54,0	45,8	
Self-employed and Unpaid family workers (% of total employment (LFS))	11,6	10,8	10,4	10,6	10,2	13,3
Self-employed (% of total employment (LFS))	9,7	9,4	9,2	9,5	8,8	.
Unpaid family workers (% of total employment (LFS))	1,9	1,4	1,2	1,1	1,4	.
Employed persons, average annual number	3 157 435	3 152 554	3 087 830	2 980 108	2 940 285	.
a. Agriculture	800353	825185	795589	781566	774080	.
b. Industry	1010431	965527	891164	843 640	812 956	.
c. Services	1346651	1361842	1401077	1354902	1353249	.
a. Private sector	1 745 341	1 922 184	2 002 668	2 110 402	2 157 760	.
b. Public sector	1 412 094	1 230 370	1 085 162	869 706	782 525	.
% of total employment (Employed persons, average annual number)	100,0	100,0	100,0	100,0	100,0	.
a. Agriculture	25,3	26,2	25,8	26,2	26,3	.
b. Industry	32,0	30,6	28,9	28,3	27,6	.
c. Services	42,7	43,2	45,4	45,5	46,0	.
a. Private sector	55,3	61,0	64,9	70,8	73,4	.
b. Public sector	44,7	39,0	35,1	29,2	26,6	.
Unemployment rate (Employment Agency, economically active population 2001), %	-	-	-	-	17,88	16,27
Unemployment rate (Employment Agency, economically active population 1992), %	13,69	12,17	15,97	18	17,32	-
Unemployment rate (Labor force survey), %	15,0	16,0	17,0	16,4	19,5	16,8
Youth unemployment (age group 15-24), registered at EA, end-year, number	108 143	78 465	105 476	105 610	95 682	95 325
Youth unemployment (age group 15-24), as of end-year LFS, thousands	139,4	141,5	137,0	113,5	132,2	.
Youth unemployment (age group 15-24) as % of total unemployment	20,7	16,9	17,3	15,5	14,4	15,8
Long-term unemployment (% of unemployed for 12 months or more in total unemployment (LFS))	56,5	53,3	52,5	58,6	63,2	65,8
Shadow economy labor force in % of working age population (age group 16-65)*		30,4	30,4			

\* Schneider, F.: The Size and Development of the Shadows Economies and Shadow Economy Labor Force of 22 Transition and 21 OECD Countries: What do we really know?, Invited paper prepared for the Roundtable Conference: "On the Informal Economy", Sofia, Bulgaria, April 18-20, 2002, <http://www.csd.bg/news/bert/presentations.html>

**Table A5. Educational level of employed, %. Educational level of unemployed, %**

<b>Educational level of employed, %</b>	<b>1997</b>	<b>1998</b>	<b>1999</b>	<b>2000</b>	<b>2001</b>	<b>2002</b>
Employed, total	100,0	100,0	100,0	100,0	100,0	
Higher total	21,5	22,3	22,9	23,6	27,0	
Higher (Bachelor, Master, Doctor)	15,6	16,4	16,8	15,9	19,2	
Higher (Specialist)	5,9	5,9	6,0	7,7	7,8	
Upper secondary	54,0	56,1	57,3	58,1	55,8	
Lower secondary, primary and primary unfinished	24,5	21,7	19,8	18,3	17,2	
<b>Educational level of unemployed, %</b>	<b>1997</b>	<b>1998</b>	<b>1999</b>	<b>2000</b>	<b>2001</b>	<b>2002</b>
Unemployed, total	100,0	100,0	100,0	100,0	100,0	100,0
Higher total	8,4	8,5	8,0	8,9	11,2	11,9
Higher (Bachelor, Master, Doctor)	5,7	6,2	6,2	5,5	8,0	
Higher (Specialist)	2,6	2,3	1,9	3,4	3,2	
Upper secondary	50,7	50,7	52,5	53,1	54,6	53,3
Lower secondary, primary and primary unfinished	40,9	40,8	39,5	38,0	34,3	34,8

**Table A6. Labor productivity, labor costs and wages**

<b>Indicators</b>	<b>1997</b>	<b>1998</b>	<b>1999</b>	<b>2000</b>	<b>2001</b>	<b>2002</b>
Labor productivity (GDP per employee, cup, USD)	4732	6104	6492	6627	7274	8132
Average unit labour costs:						
Labor costs, total				100,00	100,00	
Wages & salaries				67,20	66,88	
Severance pay & compensation in lieu of notice				2,41	2,86	
Employers' social contributions				25,24	24,59	
Other employers' social expenditure				4,26	4,73	
Taxes relating to employment regarded as labor costs				0,89	0,94	
Average monthly gross wages of the employees under labor contract, total, USD	76,05	104,10	109,45	105,97	109,85	
Average monthly gross wages of the employees under labor contract, total, BGN	127,909	183,25	201	225	240	272
By economic activity groupings (NACE, A17):						
Agriculture, hunting, forestry and fishing						196
Mining and quarrying						416
Manufacturing						244
Electricity, gas and water supply						455
Construction						208
Trade; repairing activities						240
Hotels and restaurants						164
Transport and communications						320
Financial intermediation						586
Real estate, renting and business activities						292
Public administration; compulsory social security						391
Education						269
Health and social work						259
Other activities						237
Average pay (Average monthly gross wages of the employees under labor contract, total) increase (nominal and adjusted to inflation)						
Nominal growth in %		43,3	9,7	11,9	6,7	13,3
Adjusted to inflation growth in %		20,7	6,9	1,5	-0,7	7,1

**Table A7. Expenditures on main labor market policies (active and passive measures as % of GDP)**

<b>Indicators</b>	<b>1997</b>	<b>1998</b>	<b>1999</b>	<b>2000</b>	<b>2001</b>	<b>2002</b>
Expenditures on main labor market policies (active, other and passive measures) as % of GDP		0,63	1,01	1,10	1,01	
Expenditures on main labor market policies (active and other measures) as % of GDP		0,27	0,42	0,24	0,25	
Expenditures on main labor market policies (passive measures) as % of GDP		0,36	0,59	0,86	0,76	

**Table A8. Social security and social policy**

Indicators	1997	1998	1999	2000	2001	2002
Social security burden on employers and employees (calculated as % of payroll) at the end of the year, for III labor category, total:	39	39	35,7	35,7	32,7	36,7
Employers social security burden (calculated as % of payroll)	37	37	34,7	28,6	26,3	27,5
Employees social security burden (calculated as % of payroll)	2	2	1	7,1	6,4	9,2
Replacement rate of unemployment allowance/unemployment insurance (as % to average gross wage)	23,6	29,5	31,4	32,8		
Average monthly unemployment allowance in BGN	30,136	54,03	63,18	73,9		
Replacement rate of average old-age pension (as % to average gross wage)	28,6	33,3	32,7	38,8	38,9	
Average monthly old-age pension in BGN	36,63	61,02	65,77	87,33	93,4	

Sources: BNB, EA, MF, NSI, NSSI; Eurostat

**Table A9. Characterization of potential labor emigration from Bulgaria**

Preferred countries for emigration from Bulgaria for the period 1992-2001	Preferred countries by the Bulgarian potential labor emigrants	Share of the individual age groups among potential labor emigrants	Distribution of potential labor emigrants by sex	Educational status of potential labor emigrants	Ethnic status of potential labor emigrants
Germany (23%) USA (19%) Greece (8%) Spain (8%) Great Britain (6%) Italy (6%) Canada (5%) France (4%)	Germany (25%) USA (15%) Greece (11%) Spain (9%) Great Britain (8%) Italy (5%)	20-29 г. (35%) 40-49 г. (19-22%) over 50 г. (8-10%)	men (65%) women (35%)	higher educated (14%) secondary educated (55%) lower secondary educated (28%)	Bulgarians (77%) Turks (12%) Roms (8%)

Source: National Statistical Institute

**Tale A10. Characterization of the immigration process in Bulgaria**

Distribution of the issued work permits by countries (1994-2001)	Distribution of the work permits by qualification of the workers	Structure of the immigration flow regarding the reason for staying towards 2002
USA (332) Turkey (169) Ukraine (165) Russia (152) Greece (135) Former Yugoslavia (125)  Roumania (123) England (112) Germany (102) FYR Macedonia (101) Italy (90)  France (88)	1-st place: high leading staff, hired by foreign investors from EU and USA  2-nd place: consultants and technical engineer staff  3-rd place: foreign teachers in Bulgarian secondary and higher schools	Registration by trade activity (62%)  Registration by labor contracts (6,7%)  By marriage with Bulgarian citizens or constantly staying persons (31,3%)

Source: Employment Agency



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CENTER FOR ECONOMIC DEVELOPMENT, SLOVAKIA

**EU Enlargement and Its Impact  
on the Social Policy and Labor  
Market of Slovakia**

*Bratislava, 2003*





# 1. Macroeconomic Picture and Stage of EU Accession

## 1.1. Macroeconomic Background

Since the political events of 1989-1990, Slovakia, similarly as other countries of Central and Eastern Europe, has been undergoing a unique change. The country and its economy is affected by at least three overlapping and, in many cases, intertwining developments: socio-economic transition, catching up and adjusting to the European Union, and the challenges of globalization. As a result, in most cases, it is rather difficult or impossible to separate the effects of EU integration from other components of the process. Most of the effects of preparing for EU membership can be attributed to those of transformation or globalization. They would have appeared, even if accession to the EU were not a priority task.

In the early 1990s, economic reform in Slovakia was launched rather aggressively, which enabled completion of its key components within several years. Macroeconomic results reached in the mid 1990s ranked Slovakia among the best performing transition economies. Unemployment oscillated around 11-13 percent. However, the impressive performance (GDP growth of 6.9 percent in 1995, inflation rate of 7.2 percent, and an active trade balance) could not be sustained over a longer period. Due to a variety of reasons, including political, the economic and social reforms were slowed down or even brought to a halt. Delays in the restructuring of the economy, postponement of bankruptcies, restrictions to competitiveness, increasing non-transparency and corruption in the privatization process, low inflow of foreign investment – all these aspects began to reflect in 1996 in the growing imbalance of the Slovak economy.

The end of the decade was therefore marked by attempts to stabilize the economy, to complete the principal reforms, and to start new, more demanding reforms (education, health care, pensions). In 1998,

the exchange regime of the Slovak currency was changed from fixed to floating, which prevented further depletion of foreign exchange reserves. Price deregulation (mainly of energy, water, rent), tax increase, and the introduction of the import surcharge were the main components of the so-called “package of measures” adopted in 1999. After several years of real wages growth, the “package” caused a lowering of purchasing power in 1999. GDP growth remained moderate at around 2 percent and increased to 3.3 percent in 2001. The level of inflation measured by the consumer price index reflected the gradually adopted administrative and economic measures, mainly deregulation of prices and tax range changes (VAT and excise taxes) and increased to an average of 10.6 percent and 12 percent in 1999 and 2000, respectively. Inflation fell significantly to 7.3 percent in 2001 and 3.3 percent in 2002.

The aforementioned measures have helped to reduce the trade balance deficit. Increased inflow of FDI, particularly due to privatization of important utilities and banks to foreign partners, have reduced the balance of payments deficit to less than 4 percent of GDP in 2000. However, the year 2001 was marked by a repeated sharp increase in the trade balance deficit (10.7 percent of GDP). The dynamics of reforms were gradually slowed down by the growing political strains between the government coalition parties as well as by the growing problems associated with the implementation of reforms. The launching of important reforms in the social sector was delayed and caused further growth of the internal debt of these sectors. Labor market distortions, above all high unemployment rates, became the most pressing socio-economics problem.

The Slovak economy grew at a promising rate of 3.1 percent and 4.4 percent during 2001 and 2002, respectively. Unemployment remained high at 18.5

percent in 2002 (19.2 percent in 2001). The current account deficit reached 8.2 percent of GDP in 2002. The high inflow of FDI (16.9 percent of GDP) had an important impact on the balance of payments. It was the privatization of a 49 percent stock of state owned Slovak Gas Company, which boosted the FDI statistics.

The State Budget closed the year 2002 with a deficit of 4.8 percent of GDP. Inflation was kept at a relatively low level of 3.3 percent mainly due to the postponed liberalization of energy prices; the postponement resulting from the upcoming September 2002 parliamentary elections. Inflation is hence expected to grow in 2003. Forecasts of key indicators for 2003 include: 3.5 percent GDP growth, inflation at 8.4 percent, unemployment rate 17.5 percent and current account deficit 7.4 percent as a share on GDP.<sup>12</sup>

## 1.2. Stage of EU Accession

The Slovak Republic started negotiations with the EU on February 15, 2000, i.e. two years later than its neighboring countries from the so-called Luxembourg group of 1st tier accession countries. In the course of the negotiation process, however, the Luxembourg and the Helsinki groups of accession countries tended to merge into the so-called Laeken group of accession countries. Along with other 10 candidate countries, the SR concluded accession negotiations at the European Council in Copenhagen (December 2002). Slovakia thereby made full use of the "catch-up" principle, and confirmed the country's readiness to join the EU in May 2004.

Accession negotiations were taking place in three phases – screening, negotiation process, and ratification process. Table 1 shows an overview of the negotiation process of the SR and the EU.

The negotiated position of Slovakia in chapters 2 and 13 (Free Movement of Persons, Social Policy and Employment) and the implications for the social system, labor markets and mobility, will be discussed more detailed in the following sections of this study.

**Table 1. The negotiation position of the Slovak Republic**

Year	EU presidency	Opened chapters	Closed chapters
2000	Portugal	6. Competition policy 12. Statistics 16. Small and medium-sized entrepreneurship 17. Science and research 18. Education, vocational training and youth 20. Culture and audiovisual policy 26. External relations 27. Common foreign and security policy	12. Statistics 16. Small and medium-sized entrepreneurship 17. Science and research 18. Education, vocational training and youth  26. External relations 27. Common foreign and security policy
	France	3. Freedom to provide services 4. Free movement of capital 8. Fisheries 9. Transport policy 15. Industrial policy 19. Telecommunications and information technologies 23. Consumers and health protection 25. Customs union	8. Fisheries  15. Industrial policy 20. Culture and audiovisual policy 23. Consumers and health protection
2001	Sweden	1. Free movement of goods 2. Free movement of persons 5. Company law 7. Agriculture 10. Taxation 11. Economic and monetary union 13. Social policy and employment 14. Energy 21. Regional policy and coordination 22. Environment 24. Cooperation in the area of justice and home affairs 28. Financial control 29. Financial and budgetary provisions	1. Free movement of goods 2. Free movement of persons 3. Freedom to provide services 4. Free movement of capital 5. Company law  11. Economic and monetary union 13. Social policy and employment  19. Telecommunications and information technologies 25. Customs union
	Belgium		14. Energy 22. Environment 28. Financial
2002	Spain	30. Institutions	7. Agriculture/1st part 9. Transport policy 10. Taxation 24. Cooperation in the area of justice and home affairs 30. Institutions
	Denmark	31. Diverse	6. Competition policy 7. Agriculture/2nd part 21. Regional policy and coordination 29. Financial and budgetary provisions 31. Diverse
2003	Greece	Accession Treaty (April 16, 2003) Ratification process in EU Member States Referendum on EU accession in the SR (May 16-17, 2003)	
	Italy	Ratification process in EU Member States	
2004	Ireland	Expected entry (May 1, 2004)	

Source: Ministry of Foreign Affairs of the SR.

<sup>12</sup> Forecasts of the Ministry of Finance of the SR

## 2. Labor Market

### 2.1. Current State: Factors and Problems

In recent years, the Slovak labor market has been dominated by relatively pronounced trends: growing numbers of economically active population, stagnating employment, and high and regionally differing unemployment rates. Table 2 illustrates the development of the main labor market parameters during the last five years.

Unemployment emerged as a new phenomenon in the beginning of the 1990s. Within a one-year span (1991), unemployment grew from virtually 0 percent to roughly 12 percent due to massive layoffs in companies. Although there had been some signs of unemployment prior to 1990, the Slovak labor market was not prepared for the changes after 1990. New labor institutions had to be established and legislation had to be drafted. The growing fiscal burden associated with provision of unemployment benefits resulted in several restrictive amendments to eligibility criteria. However, the generosity of the unemployment benefit scheme and of the social welfare net remained among the main causes of the negative developments in the Slovak labor market.

Policy responses to the unemployment issue did not show in any substantial changes that would bring the negative development to a halt or even reduce high unemployment rates. Unemployment became the most vulnerable point in the socio-economic development and the most pressing societal problem (as evidenced by numerous sociological surveys, see for instance Table 3). Unemployment rates surprisingly showed a long-term growth despite the slow, but still existing GDP growth. Unemployment grew steadily from 12.7 percent in 1996 to 18.8 percent in 2001. The number of registered unemployed – ap-

**Table 2. Development of labor market parameters, by regions (numbers in 1000 persons, rates in percent)**

Region	Indicator	Year				
		1997	1998	1999	2000	2001
Bratislavsky	Economically active population of which	325.1	331.1	335.8	337.2	337.4
	Employed/self-employed	304.1	308.6	309.2	310.8	308.3
	Unemployed	18.5	20.0	24.6	24.4	28.2
	Economic activity rate	64.7	65.2	65.6	65.4	64.8
	Employment rate	60.5	60.8	60.4	60.3	59.2
	<b>Unemployment rate</b>	<b>5.7</b>	<b>6.0</b>	<b>7.4</b>	<b>7.2</b>	<b>8.3</b>
Trnavsky	Economically active population of which	260.1	260.2	266.5	273.0	286.0
	Employed/self-employed	230.0	226.3	229.8	225.0	232.4
	Unemployed	28.8	30.7	32.8	44.7	51.5
	Economic activity rate	59.7	59.1	59.9	60.9	63.2
	Employment rate	52.8	51.4	51.7	50.2	51.4
	<b>Unemployment rate</b>	<b>11.1</b>	<b>11.8</b>	<b>12.3</b>	<b>16.4</b>	<b>18.0</b>
Trenciansky	Economically active population of which	285.9	297.9	288.4	294.1	296.7
	Employed/self-employed	259.6	270.7	252.4	247.8	254.0
	Unemployed	25.4	23.0	32.9	44.2	39.8
	Economic activity rate	59.4	61.3	58.9	59.6	59.6
	Employment rate	53.9	55.7	51.5	50.2	51.0
	<b>Unemployment rate</b>	<b>8.9</b>	<b>7.7</b>	<b>11.4</b>	<b>15.0</b>	<b>13.4</b>
Nitriansky	Economically active population of which	332.7	329.3	328.2	335.3	343.1
	Employed/self-employed	279.4	285.2	266.9	263.3	261.7
	Unemployed	50.6	39.9	58.3	69.8	79.4
	Economic activity rate	57.9	56.9	56.4	57.2	58.2
	Employment rate	48.6	49.3	45.8	44.9	44.4
	<b>Unemployment rate</b>	<b>15.2</b>	<b>12.1</b>	<b>17.8</b>	<b>20.8</b>	<b>23.1</b>
Zilinsky	Economically active population of which	326.2	332.5	332.3	332.1	334.9
	Employed/self-employed	294.7	292.9	275.1	266.7	267.6
	Unemployed	27.5	34.8	52.6	61.4	63.3
	Economic activity rate	61.6	62.1	61.5	60.9	60.8
	Employment rate	55.6	54.7	50.9	48.9	48.6
	<b>Unemployment rate</b>	<b>8.4</b>	<b>10.5</b>	<b>15.9</b>	<b>18.5</b>	<b>18.9</b>
Banskobystricky	Economically active population of which	307.7	308.3	313.8	317.4	327.6
	Employed/self-employed	262.7	257.4	246.2	245.7	251.2
	Unemployed	42.8	48.2	66.3	69.6	73.4
	Economic activity rate	58.5	58.2	58.9	59.2	60.7
	Employment rate	49.9	48.6	46.2	45.8	46.5
	<b>Unemployment rate</b>	<b>13.9</b>	<b>15.6</b>	<b>21.1</b>	<b>21.9</b>	<b>22.4</b>
Presovsky	Economically active population of which	338.5	342.5	357.7	362.4	366.2
	Employed/self-employed	284.6	282.4	285.9	278.4	279.7
	Unemployed	51.0	56.2	68.3	80.1	83.1
	Economic activity rate	58.7	58.6	60.5	60.5	60.4
	Employment rate	49.4	48.3	48.4	46.5	46.1
	<b>Unemployment rate</b>	<b>15.1</b>	<b>16.4</b>	<b>19.1</b>	<b>22.1</b>	<b>22.7</b>
Kosicky	Economically active population of which	346.0	343.1	350.5	356.7	360.6
	Employed/self-employed	291.0	275.2	266.9	264.1	268.8
	Unemployed	53.0	64.3	81.0	91.2	89.3
	Economic activity rate	59.0	58.0	58.7	59.2	59.2
	Employment rate	49.7	46.5	44.6	43.8	44.1
	<b>Unemployment rate</b>	<b>15.3</b>	<b>18.7</b>	<b>23.1</b>	<b>25.6</b>	<b>24.8</b>

Source: Labor Force Survey, Statistical Office of the SR

plicants for jobs registered with labor offices – reached an average of 520,642 individuals in 2001, as compared to 349,821 persons in 1995. The share of unemployed women varied slightly during the respective period, from 52.5 percent in 1996 to 45.3 percent in 2001. The comparison of male and female unemployment rates shows no significant gender-related deviations, however, the proportion of men among unemployed is moderately increasing. Women, on the other hand, prevail among the long-term unemployed.

**Table 3. Most pressing problems to be solved from the viewpoint of citizens (% of positive answers)**

Problem areas	1997	1998	2001
Unemployment	60	65	82
Health care	48	50	69
Standard of living	65	65	64
Crime and personal safety	62	66	46
Housing	29	29	26
Ethics, quality of interpersonal relations	43	36	24
EU and NATO integration	11	18	12
Environment	18	14	9
Ethnic and minority problems	6	7	5

Source: Public Opinion Research Institute of the Statistical Office of the Slovak Republic.

Young people are among the most affected by unemployment. Youth unemployment rate for those aged 15-24 was almost double the average rate for all age groups at 37.3 percent in 2001. A growing concern is the increasing number of long-term unemployed: the share of unemployed for more than 12 months reached 57.8 percent of all unemployed in December 2001, which is an increase by 5 percent as compared to 2000.<sup>13</sup> A temporary decrease of the number of long-term unemployed was evidenced in the 2nd half of 2000 as a result of the introduction of 65,000 public works.

The Slovak labor market is marked by strong regional disparities which are most vivid in unemployment rates. The gaps between the levels of registered unemployment between individual districts grow steadily and ranged as much as 30 percent in throughout 2001, as compared to 25 percent in January 1997. Traditionally, unemployment rate is lowest in the districts of the capital city Bratislava (3.7 percent-6.2 percent as of December 2001), while it is the highest in the district of Rimavsk6 Sobota (35.5 percent). Regions with higher proportion of educated

labor force usually report lower unemployment rates.

Regional distribution of unemployment underlines the correlation between insufficient education and isolation from the labor market. Regions with higher proportions of labor force with completed elementary education only usually report higher numbers of unemployed registered with labor offices. Statistical figures suggest an ambivalent development in education: along with the growing tertiary enrolment ratio, also the number of primary schools leavers who do not continue in education is on the rise. Experts agree that there is a “hard core” of unemployed who are in fact unemployable with respect to their work-related skills and attitudes. Particularly in regions with low average wages, unemployment benefits and social assistance benefits tend to have disincentive effects on active job search of their recipients, particularly those with potentially low income. As a result, the benefit scheme is indirectly supporting the participation of the unemployed in the shadow economy. Disincentive effects in large families with low income are increased by child and parental allowances, since these cause the total income to climb up close to or even above the potential income from work.<sup>14</sup>

Due to the aforementioned handicaps, cumulated with other factors such as isolation and segregation, long-term and permanent unemployment is rather widespread among the Roma population. Although statistics do not record poverty indicators by ethnic division, it is assumed that particularly Roma in isolated colonies are among the groups with highest risk of poverty. Table 4 illustrates the high unemployment rates of the Roma compared to the other ethnic groups in Slovakia.

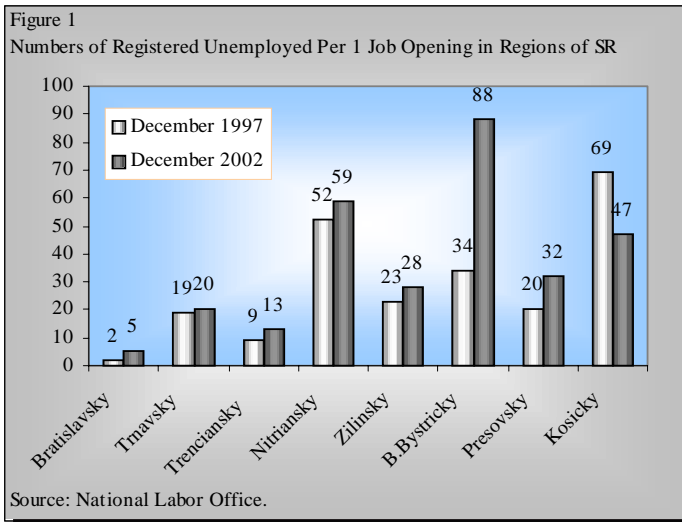
**Table 4. Unemployment rate by ethnic groups (age group 15-64 years, in percent)**

Indicators	1998	1999	2000	2001
Total	12.5	16.2	18.6	19.2
Slovak	10.9	14.9	17.5	17.9
Czech	7.6	11.5	13.3	23.9
Hungarian	18.1	22.4	25.5	27.1
German	11.4	-	-	-
Polish	2.0	5.5	23.9	19.9
Russian, Ukrainian, Ruthenian	15.1	21.6	22.0	17.6
Roma	83.2	77.5	73.5	72.6
Moravian	11.6	20.0	-	-
Other	8.1	17.5	2.4	16.5

Source: Labor Force Survey. Statistical Office of the SR

<sup>13</sup> Labor force surveys

<sup>14</sup> The new cabinet introduced a more stringent regulation of social benefits, including lowering the levels of social assistance benefits (effective since January 1, 2003).



Statistical figures suggest that there is a shortage of official jobs in Slovakia (see Figure 1). In an economy with low generation of job opportunities, the demographic growth of the productive population component will show as growth of unemployment. The demographic development itself, however, cannot be considered the reason for high unemployment. Similar demographic trends namely prevail in a majority of developed countries whose economies, however, are able to cope with this development in the labor market. Unemployment (and thus also shortage of jobs) is a consequence of a whole complex of problems. Most experts agree that the major reasons include:

- inefficient social protection system (relatively generous and not overly motivating, with significant redistribution of sources and solidarity, with prevalingly passive measures);
- insufficient education of a portion of the labor force and weak linkage between education and labor market;
- barriers on the part of the business environment (rigid labor law, instable legislation, low law enforcement, high tax and mainly payroll burden);
- low mobility of labor and inflexible housing market;
- other (e.g., passivity, tolerance of shadow activities).

As large portion of the labor force shifted towards unemployment, the number of employed decreased by 4.6 percent in the period 1996-2001. Women accounted for 44.5 percent on total employment in

1996, while their share increased by 1.5 points to 46.0 percent in 2001. Employment gradually decreased in the public sector (by 23.6 percent); the private sector recorded an increase by 12.6 percent during the surveyed period.

The sectoral structure of employment is undergoing changes, of which the reduction of employed in agriculture and manufacturing industry and the growth of employment in the service sector are among the most significant.

The numbers of economically active individuals kept growing in Slovakia due to the growing proportion of productive age population. Economic activity rates of the population have stabilized at 60 percent.<sup>15</sup> For all Slovak citizens aged 15 and above, 6 in 10 are economically active. Male economic activity rate is approximately 16 percent higher than the rate of the female population.

Unemployment remains evidently the weakest point of the socio-economic development in Slovakia and the most sensitive social problem.

Except for rather occasional cases connected with bankruptcies of enterprises and massive layoffs of employees, high unemployment rates are however no reason for serious social unrest to develop in the country. It may be assumed that high incidence of shadow labor is one of the reasons.<sup>16</sup> Domestic esti-

**Table 5. The size of shadow economy in transition countries**

Country	Size of shadow economy (% of GDP), DYMIC method		Shadow economy labor force (% of working age population, 1998/1999) <sup>a</sup>
	Average for 1990-1993	Average for 2000-2001	
<b>Bulgaria</b>	<b>27.1</b>	<b>36.4</b>	<b>30.4</b>
Czech Republic	13.1	18.4	12.6
<b>Estonia</b>	<b>34.3</b>	<b>39.1</b>	<b>33.4</b>
Hungary	22.3	24.4	20.9
Latvia	25.7	39.6	29.6
Lithuania	26.0	29.4	20.3
Poland	22.3	27.4	20.9
Romania	27.3	33.4	24.3
<b>Slovakia</b>	<b>15.1</b>	<b>18.3</b>	<b>16.3</b>
Slovenia	22.9	26.7	21.6

Note: a. Working age population means population between the age of 16 and 65.

Source: Schneider, F.: The size and development of the shadow economies of the 22 Transition and 21 OECD countries. Bonn: IZA, (2002) in: Study on the Social Protection Systems in the 13 Applicant Countries. Synthesis report, Second draft. GVG, Köln (2002).

<sup>15</sup> Economic activity rate represents the share of economically active population (employed including women on maternity leave, and registered unemployed) on total population in productive and post-productive age.

<sup>16</sup> Shadow labor also distorts data on the numbers of the population living in poverty or being at risk of poverty. It substitutes official earnings from employment, however to the detriment of all who work and pay taxes and social security contributions.

mates of the extent of shadow labor rather differ (ranging from one-tenth up to one-third of the registered unemployed); a foreign source may offer a detached view. Rather surprisingly, Table 5 suggests that the size of shadow (gray) labor and economy in Slovakia is among the lowest ones in Central and Eastern European countries.

## 2.2. Policies in the Field of Labor Market

The main strategic policy document on employment is the National Employment Plan (approved in November 1999, actualized regularly). It follows the four-pillar structure of the European Employment Strategy, while taking account of the specific conditions of the Slovak labor market<sup>17</sup>. The four pillars include concrete measures aimed at improvement of employability mainly through education and training, development of small and medium entrepreneurship in co-operation with local authorities, support of flexibility of enterprises and promotion of equal opportunities between men and women.

The government of the Slovak Republic has prepared in co-operation with the European Commission a Joint Assessment of Employment Priorities in the Slovak Republic. This document presents a set of employment and labor market measures necessary to advance the labor market transformation, to make progress in adapting the employment system so as to be able to implement the Employment Strategy and to prepare it for EU accession.

### 2.2.1. Active Labor Market Policies

The labor market policies in Slovakia traditionally include the passive component (payments of unemployment benefits and social insurance contributions) and the programs of active labor market policy (ALMP). As the result of the increasing numbers of unemployed and a generous provision of unemployment benefits, ALMP programs were reduced dramatically towards the end of the 1990s. Table 6 shows that since 2000 a redirection of measures in favor of active programs (mainly public works and retraining) and a tightening of benefit schemes occurred.

Counselling services are the prevailing form of preventive approach of public employment services

**Table 6. Proportion of GDP spending on labor market policies (in SKK billion at current prices)**

Year	GDP	Labor market	% of GDP policies	PLMP	% of GDP	ALMP	% of GDP
1997	686.10	7.089	1.03	3.990	0.58	3.099	0.45
1998	750.80	7.774	1.04	5.485	0.73	2.289	0.31
1999	815.30	7.776	0.95	7.292	0.90	0.474	0.06
2000	887.20	7.753	0.88	6.182	0.70	1.571	0.18
2001	964.60	7.024	0.73	4.789	0.50	2.235	0.23

Note: PLMP – Passive labor market policy. ALMP – Active labor market policy. Source: National Labor Office, in: Report on the Implementation of conclusions and priorities of the document of the Joint Assessment of Employment Priorities in the SR for 2001, Ministry of Labor, Social Affairs and Family of the SR

(PES) to the unemployed. Counselling services have been delivered mainly to individuals aged up to 29, though not limited to them, mainly through professional career advice, individual consultancy, and counselling programs. Although several steps have been implemented to increase the quality of services at labor offices (e.g., prolonged opening hours), the high ratio of unemployed per competent PES staff negatively affected the rate of availability of employment services for unemployed. There were 103 registered unemployed persons per 1 PES staff member in 2001, and an average of 268 registered unemployed were assigned per 1 first-contact staff.

The most accentuated ALMP program aimed at increasing opportunities for unemployed and socially excluded is the creation of public beneficial jobs, i.e. public works. Insufficient job creation, growing long-term unemployment, and existence of the core of unemployed, resistant to applied general ALMP tools and highly dependent social benefits, induced the setting up of a special program financed through the state budget in 2000 – the so-called "Negotiated public beneficial jobs for long-term unemployed". The main objective of the program was to decrease the extent of long-term unemployment, but also to prevent devaluation of working capital represented by unemployed, to test their interest and willingness to work, and to offer them a possibility of finding stable employment through continuity of the job after expiration of employment benefit.

In 2001, 38,446 public works were created for 40,509 registered unemployed (65 percent men and 35 percent women) and 9,854 public works were prolonged from the year 2000. More than three quarters of these jobs have been created in the four re-

<sup>17</sup> Source: Joint Assessment of Employment Priorities in the Slovak Republic (2001)

gions with highest unemployment rates (Kosice, Banska Bystrica, Presov, and Nitra). The rate of return of the program participants to unemployment/employment is not monitored at present. However, the empirical knowledge indicates that the return rate to unemployment in case of public works is very high, achieving 95 percent to 100 percent.

Young people, belonging to the groups most affected by unemployment, can use the "Short-term program supporting the employment of young people" to address their problems in the labor market. The program has focused on improving young people's chances for employment through counselling, reskilling and job brokering activities of public employment services. In 2001, 14,773 registered unemployed aged 15-29 (55 percent males and 45 percent females) had been involved in the program, which represented 6.7 percent of the average number of registered unemployed in the age bracket towards the end of 2001. More than one quarter (26.1 percent) of the total number of participants has found paid jobs after the program completion.

Among other traditional ALMP tools, re-training is the most important and perhaps also the most efficient. A total of 24,558 registered unemployed have entered retraining programs in the year 2001, which is a fivefold increase compared to 2000. 18,504 registered unemployed completed the training, of which 41.4 percent were men and 58.6 percent were women. The programs were aimed primarily at the disadvantaged segment, thus young people in the 15-29 age bracket (52.4 percent), persons with low education (39 percent) and the long-term unemployed (40.2 percent) were prevailing in the structure of re-training participants. The success rate of retraining programs in the year 2001, measured by placement of participants in the labor market within 6 months of participation, was 37.1 percent.

The support for employment of persons with altered work capacity has been implemented primarily through creating and maintaining jobs in sheltered workshops and sheltered workplaces. A total of 1,359 jobs have been created in the year 2001 for persons with disabilities, which is by 569 jobs more than in the previous year.

**Table 7. Overview of labor market policy expenditures**

Labor market policy	1998		1999		2000		2001	
	SKK thous.	%	SKK thous.	%	SKK thous.	%	SKK thous.	%
Total expenditures	7773826	100.0	7766302	100.0	7752873	100.0	7024121	100.0
Passive LMP	5 484 686	70.6	7 292 270	93.9	6 182 429	79.7	4 789 198	68.2
- unempl. benefits	3 927 123	71.6	5 338 155	73.2	4 412 902	71.4	3 450 004	72.0
Active LMP	2 289 140	29.5	474 032	6.1	1 570 444	20.3	2 234 923	31.8
- retraining	166 955	7.3	73 658	15.5	62 059	4.0	196 840	8.8
- support for new jobs	1 996 583	87.2	296 580	62.6	1 356 458	86.4	1 737 386	77.7
- support for long-term unemployed	-	-	-	-	1 201 391	88.6	1 390 473	80.0
- disabled persons	125 602	5.5	103 794	21.9	151 927	9.7	229 913	10.3
Collected contributions	8 030103	-	7 936818	-	8 446088	-	8 965867	-

Source: National Labor Office, in: Report on the Implementation of conclusions and priorities of the document of the Joint Assessment of Employment Priorities in the SR for 2001, Ministry of Labor, Social Affairs and Family of the SR

The Ministry of Labor, Social Affairs and Family is in the process of drafting a new *Strategy of promoting employment through the reform of the social system and the labor market*. The main principles of the strategy will consist of:

- lowering of disincentive effects caused by the tax and payroll burden;
- strengthening the motivation of the individual to find and maintain a job;
- supporting economic and social activity of the individual;
- more flexibility of the labor market;
- more effective state administration and services in areas of labor market and social affairs;
- reducing the misuse of the social system.

### 2.2.2. Passive Labor Market Policies

Passive labor market policies include payments of unemployment benefits and social insurance contributions on behalf of the registered unemployed. Data on the respective policies are listed in tables 6 and 7.

## 2.3. Challenges of EU Accession Regarding Labor Market Flexibility

The effects of EU accession on the social system, similarly as on the country as a whole, are difficult to separate from the effects of transformation and from other components of development. This becomes obvious already in the preparatory stage for EU membership.

EU accession is expected to bring further opening of the Slovak economy towards the members, while it may raise protection against third countries. Domestic markets will become a part of the common market and will thus react to the new supply-demand conditions. Slovak enterprises will be facing tougher competition, including competition from other accession countries, which in turn will require further structural changes. The regional disparities in Slovakia will be addressed by structural support from EU.

Basically, the opportunities for acquiring education and jobs are expected to improve for Slovak citizens. Free movement of labor may cause a certain portion of the population to migrate to the more advanced economies, however, surveys suggest a relatively low number of those who would permanently settle abroad (see item 4).

The Slovak society will be facing another important event in its short history. Integration into the group of developed countries will further shape the stratification of the society. It may be expected that inequality in the population will grow. The social framework will become largely dependent on the common legislation, which will create pressure on further adjustment of institutions and policies. As a part of the global economy, however, the EU will not remain isolated and will have to implement reforms covering also the social sphere.

Employment and/or labor market policies in general, constituted an important part of the negotiation agenda. The *Chapter 13 on Social Policy and Employment* was provisionally closed during the first half of 2001. The EU points out that the employment situation and the employment policies of the Member States are an issue of common concern, as defined in Title VIII of the EC Treaty. The EU attaches great importance to the labor market situation in Slovakia, and public policy in this area, and will moni-

tor further developments in Slovakia. Monitoring will focus, in particular, on progress in implementing the policy priorities identified in the Joint Assessment of Employment Policy Priorities (JAP).

The employment-related acquis, however, does not have a binding character. Among its key objectives, the Slovak Republic has assumed the responsibility for attaining and maintaining high and stable employment, aiming at full employment as its ultimate goal. Article 35 para. 3 of the Constitution of the Slovak Republic lays down the right to work. The State guarantees, within reasonable limits, the material welfare of those who cannot enjoy this right through no fault of their own. The terms thereof are specified under the Act on Employment No. 387/1996 Coll. as amended.

The 2002 EC Regular Report on Slovakia's Progress Towards Accession states "In the field of social policy and employment, Slovakia is advanced in terms of legislative alignment. Administrative structures are mostly in place, but require further strengthening. There is a particular need to co-ordinate the supervision and enforcement of the transposed health and safety acquis. Administrative preparations for the future management of the European Social Fund need to be reinforced."

The Progress Report further appreciates the progress achieved by adopting a new Labor Code in April 2002. However, the Labor Code was subject to criticism by a large part of the domestic expert community. Subject to negative assessment was mainly the rigidity of the law, negatively affecting the flexibility of employment relations, working time regulation, and collective relations. The new government has therefore prepared an amendment to the law, which shall address the shortcomings in line with ILO standards and EC directives.

A progress report on the implementation of the priorities identified in the JAP was submitted to the Commission by Slovakia in June 2002. This report represents an important step in assessing the extent to which Slovakia is progressing towards its objectives of labor market reform and adaptation of its employment system in order to prepare for future participation in the European Employment Strategy after accession.

The main challenges for the Slovak labor market, which apply also to accession, include:



- addressing high unemployment;
- adjusting the overall social protection system to the economic, social and demographic developments;
- fighting shadow labor and illegal employment by addressing its causes rather than consequences;
- creating more effective linkages between labor markets and education system;
- carefully designed decentralization of employment policies;
- improvement of business environment (reduction of payroll burden, tax reform, etc.);
- refining of labor legislation;
- others (addressing employment-related problems of marginalized groups, the “Roma” issue).

## 3. Social Policy

### 3.1. Current State: Factors, Problems and Policies

The Slovak social protection system<sup>18</sup> is based on three pillars:

- Social insurance
- State social benefits
- Social assistance

#### 3.1.1 Social Insurance

Social insurance consist of:

- Sickness insurance, which consists of a system of benefits of short-term nature that are funded continuously from the insurance premium. Individual types of benefits compensate persons for lost income due to sickness, maternity, and partially for increased costs due to the care of dependent children.
- The fundamental condition enabling persons to claim and receive sickness benefits is the participation of the citizen in the sickness insurance system, or maintenance of claims for a specified period of time based on the duration of the protection period, or the receipt of financial benefits supplementing wages, salaries or compensation for work. A special group of recipients includes persons who, although not participating in the sickness insurance system, are qualified to claim sickness benefits directly by law; such qualification primarily applies to registered unemployed and persons on alternate (civil) military service duties.
- Pension security which is composed of a system of benefits of long-term nature funded in the same way as sickness insurance; qualification cri-

teria for awarding any pension security benefits are similar to the sickness insurance criteria.

- Voluntary Supplementary pension insurance tied to pension insurance and regulated by the state; this is funded from contributions remitted to the individual accounts of insured persons by employers and employees.
- Indemnification for work injuries and occupational diseases is based on the employers' obligatory liability insurance. Since 1 April 2002, it has been transferred from the commercial Slovak Insurance Co. Inc., and currently is ensured by the Social Insurance Agency.

#### 3.1.2 Social Assistance

State Social Benefits are direct financial contributions by the state to aid in overcoming an undesirable fall in the population's standards of living due to the occurrence or lasting of certain events in the lives of families (dependent children) and citizens.

The term Social assistance (SA) expresses the approach of the state to the citizen in need, where the role of the state is only to assist the citizen in overcoming his/her crisis situation and it is expected that the citizen will actively seek out his/her own solutions. Hence, the granting of SA is conditioned by the state of material and social distress an individual is incapable of coping with by himself/herself or with the help of his/her family.

The Act on social assistance stipulates the types of benefits. The benefits include: social counselling, legal protection, social services, social assistance benefit, and monetary benefits to offset the social consequences of severe disabilities. These benefits are based on the minimum subsistence level. Eligibility determinations for SA are made at district state ad-

<sup>18</sup> In this chapter, social protection is understood in the narrower sense. Health care, labor market policy, education, and housing are not included

ministration offices but financial support for associated cash benefits and services is provided through the state budget.

Slovak social protection provides a broad scope of cash benefits and support services to many individuals and families through its programs. The largest share of these payments is made by the Social Insurance Agency (SIA), which administers two payroll tax-supported trust funds: the pension fund and the sickness fund. Recently SIA has inherited also the administration of accident insurance. The pension fund makes payments to old age, survivor and invalidity (permanent disability) beneficiaries while the sickness fund provides payments for short-term illnesses and maternity leave. The SIA also administers the state social benefits, but for this purpose receives a special budget from the MOLSAF.

The National Labor Office (NLO), a second self-governing body within MOLSAF, administers labor market programs in Slovakia. Its responsibilities include job matching, payment of unemployment insurance benefits and the oversight of active labor market programs such as training and public works.

District state administration offices (established under the umbrella of Ministry of Interior) administer and decide on awarding of social assistance benefits. These offices also oversee services to the severely handicapped and long-term care for persons residing in institutions and at home. Financial support for associated cash benefits and services is provided through the state budget.

Ministry of Labor, Social Affairs and Family SR acts as an umbrella institution with competencies in the field of employment, labor market and all other social protection programs. The ministry is primarily responsible for policy-making process, however it also carries out controlling, consultative and advisory activities. Ministry representatives are members of the administrative board both of SIA and NLO.

Social insurance programs are financed mainly through payroll taxes; and benefits are linked to the individual's wage history, hence to contributions. The combined payroll tax rate to finance these programs plus health insurance is 50.8 percent, one of the highest in OECD.<sup>19</sup> High payroll tax rate poses a heavy tax on labor and is a serious barrier to growth, particularly employment growth. High contribution rates are a burden placed mainly on employers with di-

rect impact on economic performance and financial solvency, job creation, and payment discipline.

Social welfare programs (state social benefits and social assistance) are financed by general tax revenue. Eligibility and level of benefits are linked to the subsistence minimum and fixed levels set forth by legislation.

The Slovak social protection system is considered as extensive. The scopes of social programs as well as their coverage are broad. Like other safety nets, the role of the Slovak system is twofold. It provides income for those who are not employed and whose income falls below the "poverty" level, and it aims to stimulate these individuals to find a job and obtain their own means of subsistence. The safety net has been effective in achieving the first goal. Poverty in Slovakia would be significantly higher if its social assistance/support and unemployment insurance programs were to disappear. However, such a generous social safety net can also have negative effects. It can reduce incentives of workers and individuals to actively look for a job and pull themselves out of poverty. (World Bank, 2001)

**Table 8. Public expenditure on social protection**

<b>SKK billion</b>	<b>1995</b>	<b>1996</b>	<b>1997</b>	<b>1998</b>	<b>1999</b>	<b>2000</b>	<b>2001</b>
Pensions <sup>a,b</sup>	41.9	47.65	53.28	59.20	64.01	70.33	75.74
Sickness and Maternity <sup>c</sup>	5.7	7.4	8.1	9.0	9.5	9.1	8.9
Unemployment Insurance <sup>a,d</sup>	6.1	7.5	8.2	8.9	9.0	9.1	8.5
Social Welfare <sup>e</sup>	22.7	23.6	25.5	28.9	32.5	34.6	36.2
<b>Total (SKK billion)</b>	<b>76.4</b>	<b>86.1</b>	<b>95.1</b>	<b>106.0</b>	<b>115.0</b>	<b>123.2</b>	<b>129.1</b>
<b>% of GDP</b>							
Pensions <sup>a,b</sup>	7.36	7.58	7.52	7.64	7.66	7.74	7.66
Sickness and Maternity <sup>c</sup>	1.00	1.17	1.15	1.16	1.14	1.01	0.90
Unemployment Insurance <sup>a,d</sup>	1.07	1.19	1.15	1.15	1.07	1.00	0.86
Social Welfare <sup>e</sup>	3.99	3.75	3.60	3.73	3.89	3.81	3.66
<b>Total (percent of GDP)</b>	<b>13.44</b>	<b>13.69</b>	<b>13.42</b>	<b>13.67</b>	<b>13.76</b>	<b>13.55</b>	<b>13.07</b>

Note: a. Includes administrative expenses after 1995. b. Also includes administrative expenses of sickness benefits after 1995. c. Mainly covers sick leave and maternity leave. d. Includes benefits payable by NLO under Unemployment Insurance, including transfers to SIA and Health Insurance Companies. e. Includes Social Assistance, Social Care, and State Social Benefits

Source: SIA, NLO, MOLSAF and MoF. In: World Bank (2002)

The pension system in Slovakia is facing a gradually deepening financial imbalance. The level of collected insurance premium is perceived as high by the con-

<sup>19</sup> The payroll tax rates for the various social insurance programs are: pensions (28 percent), sickness (4.8 percent), unemployment (4 percent), and health (14 percent). The average rate for EU countries is 37 percent of which 23 percent is for pensions. Source: World Bank (2002).

tributors, however, even the high payroll tax burden is not sufficient to fill the fund for old age pensions and related benefits. Moreover, pensions are relatively low and their real value compared to the average wage is decreasing.

The basic pension system is financed through the PAYG scheme and administered by the Social Insurance Agency (SIA) in the form of the Basic Pension Fund. Sources of financing are generated by collected insurance premium (payroll taxes) from employees, employers, self-employed and their co-workers. Employees and employers contribute jointly 28 percent of the gross nominal wage (6.4 percent and 21.6 percent, respectively). Self-employed persons pay the same percentage (28 percent) from the half of their tax base. Economically inactive persons are covered by contributions of the State (university students, soldiers in compulsory military service, women/men on maternity leave, persons taking care of handicapped, etc.) and the National Labor Office (unemployed); contributions on behalf of inactive and unemployed are set annually by the State Budget Act. The flat rate of contributions by the State remains at a significantly lower level than that of the economically active.

The growing deficit of the pension system is caused by several interrelating factors, including:

- insufficient collection of insurance premium;
- high tax and especially payroll burden for employees and employers;
- high unemployment rate;
- demographic trends, mainly aging of the population.

The system of social protection in the Slovak Republic faces several challenges. Collection of social insurance contributions is on the decrease, State fails to fulfil its legal obligations on behalf of a growing number of economically inactive, the number of beneficiaries and pensions grows beyond the economic potential of the economically active. The result is a growing burden on public finances and a collapsing social system.

The solution of the accumulated problems requires a conceptual change. This change lies in a consensus between and within generations. An optimal balance between social (and intergenerational) solidarity and individual participation is the key element of

the reform. Such agreement should lead to more fairness and adequacy of the social system. Strengthening the link between contributions and benefits does not necessarily weaken solidarity. The redistributive element in the scheme shall guarantee assistance to those in real need.

A new approach to social protection is inevitable, especially for the reasons specified below:

- The current system does not respond to demographic, economic and social developments. It is costly, demotivating, and inequitable. Hence, there is a need for a diversified system of multi-source funding. The current system, and especially the pension system, will become insolvent in coming years and incapable of ensuring entitlements enshrined in law.
- The social system is dominated by passive measures. In general, policy responses are more focused on redistribution of sources rather than their generation.
- The current system is discriminatory, because for the same insurance premium different benefits and allowances are granted to different categories of citizens. There is no adequate relation between contributions and benefits, and taxation is mixed with obligatory insurance, which conceals the high tax burden in the Slovak Republic.

### 3.1.3 Social Dialogue

Social dialogue in Slovakia is presented in various institutional forms and levels. The tripartite dialogue is represented by the Confederation of Trade Unions of the Slovak Republic (KOZ SR), the Association of Employer Unions and Syndicates of the Slovak Republic (AZZZ SR), and the governmental Council of Economic and Social Agreement of the Slovak Republic (RHSD). Social dialogue deals mainly with pressing economic, social, labor and wage conditions. Labor legislation (particularly Labor Code), minimum wage adjustment and social situation were the main areas of social dialogue during 1997-2002.

The relationship between employers, employees and the State has undergone changes in the past decade, which were largely determined by the current political environment. Social dialogue was virtually inactive during the 1996-1998 due to general discrepancies between the trade unions and the government.

The period 1999-2002 was characterized by attempts to restore and stabilize the dialogue. Tripartite members were ready to make concessions in light of the necessary reforms of the economy. The setup of the current government and its pro-reform oriented policy increases the activity of trade unions to act as a social counterweight in an environment of a missing constructive left-wing political representation. However, activities of social partners, particularly of trade unions, sometimes lack a rational and systemic approach (e.g., amendment of Labor Code).

It is to be expected that the role of the social dialogue will further developed to a fruitful exchange of views between and among social partners and contribute to the solution of pressing social and economic issues.

### 3.2. Challenges of EU Accession Regarding Social Policy (Social Insurance, Social Assistance and Social Dialogue)

The Slovak social protection system faces challenges, which are of highest priority even if there was no EU accession agenda. However, integration into the structures of the European Union, impacts upon the reform scenario:

- by facilitating labor mobility and hence transferability of social systems;
- by defining the framework of open method of coordination;
- by granting participation in the shaping of common social policies;
- by offering access to structural funds.

Despite the considerable diversity within the European Union, Member States face common challenges with regard to pension systems. They also share common objectives and are committed to a number of principles, amongst which are equity and social cohesion, which characterize the European social model.

The modernization of pension systems in the EU is made urgent mainly by demographic aging and its impact on the old age dependency ratio. Although the reform of pension systems remains the respon-

sibility of the Member States, co-operation at EU level has intensified – in particular through the Social Protection Committee – and has benefited from the work undertaken by the Economic Policy Committee and its analysis of the projected budgetary impact of aging.<sup>20</sup>

The common objectives for sustainable pension systems stress the need to maintain adequate pension provision and solidarity in pension systems, to secure financial sustainability through a high level of employment, sound management of public finances and appropriate pension reforms, and to modernize pension systems to reflect changing needs of society and individuals.

The old age dependency ratio in most developed economies will be substantially higher in the future. In many Member States, funded pension provision will be expected to play a greater role.

The mobility of workers and citizens in general will strongly depend on the portability of the social security and pension schemes. This is an important incentive for the Slovak pension reform. One of the key features of the reforming pension system in Slovakia should be therefore its compatibility with Member States' schemes. Slovakia should further invest in forecasting of future trends, which should improve the predictability of developments in the pension system and assist pension scheme participants in decisions. Slovakia may also face competition from other pension systems: if there are strong financial incentives built into the various retirement income systems, these could induce people to move to other countries.

Development of the administrative structures for management of the European Social Fund (ESF) has been seriously delayed. The relationship between the ESF Management Department at the Ministry of Labor, Social Affairs and Family and the intermediary bodies within the National Labor Office and the Education Ministry and their regional units should be clarified as soon as possible. Further development of training systems in this area also remains of utmost importance. It is also important that the content of future ESF interventions is embedded in the European Employment Strategy and the fight against social exclusion.

A national integrated strategy on promoting social inclusion, taking into account the EU objectives,

<sup>20</sup> The Future Evolution of Social Protection from a Long-Term Point of View: Safe and Sustainable Pensions (2000)

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needs to be developed. As poverty and social exclusion are multi-dimensional by nature, it is important to promote an integrated approach mobilizing various governmental bodies and all relevant stakeholders in the process. It is also crucial to improve and develop social statistics systems on poverty and social exclusion in line with the EU commonly agreed indicators on social inclusion.

## 4. Migration Policy

### 4.1. Push and Pull Factors, Migration Processes and Policies Regulating Labor Migration

Low wage levels in the post-socialist countries is one of the most important factors attracting investment from labor intensive industries thus threatening jobs and wage levels in the West. At a time of high and persistent unemployment in the EU, the economic integration with the CEECs adds to the frictions in the labor market and in the social welfare systems. These frictions are intensified by CEE workers searching for higher paid jobs in some of the EU countries. Labor market consequences (e.g. loss of employment in some sectors/regions) and the corresponding fears in the population have led to restrictive migration and labor market policies in some European countries.

However, as already stressed by an influential OECD report, such policies are short-sighted, because they do not take account of the complex interdependent relationships between employment, trade and foreign direct investment (FDI): 'International co-operation to control flows is only a partial response to the intensification of migration movements. It is for this reason that the idea of sustainable development as a means of eventually reducing the incentive to migrate in countries with high emigration potential is gaining ground among OECD countries.' (OECD, 1995: 52)

Based on available migration statistics, and backed by a synthesis of past empirical studies we aim to provide a background for a labor migration policy debate in Slovakia, following its accession to the European Union.

#### East-West migration and Slovakia

According to the widely cited report by the European Integration Consortium (Boeri and Brücker, 2000),

in the first years after complete freedom of movement was established, around 335,000 Central Europeans are estimated to move west-wards each year. Over the course of a decade some 2.9 million people would move - of whom roughly 65 percent would end up in Germany, 12 percent in Austria. Within 30 years around 2.5 percent of the population of Germany would be of Central European origin. However, according to the same study, after 30 years return migration will be higher than immigration, so that the net migration reaches negative values.

To compare the East-West migration potential in Slovakia, Bulgaria and Estonia, we rely on estimations by Boeri and Brücker (2000),<sup>21</sup> which are tabulated below. For example, according to their baseline projection, the number of Slovak residents in Germany is estimated to be around 41 thousand in 2005, and about 70 thousand in 2010, if free movement of labor is introduced for all ten candidate countries (CEEC10) in 2002. The comparison of the actual (not reported here) and projected figures for the Slovak labor migration to Germany at the end of 2002 - 11,832<sup>22</sup> compared to 16,532 - suggests, first, that there are still important barriers to a genuine freedom of movement at the dawn of the Eastern enlargement of the EU, and, second, the Slovak migration will hardly pose any major challenge to the enlarged EU labor market.

**Table 9. Number of residents from Bulgaria, Estonia and Slovakia in Germany (baseline projection)\***

	Start Value	2002	2003	2005	2010	2015	2020	2030
Bulgaria	38 847	61 659	82 251	117 526	178 472	212 235	228 967	235 022
Estonia	2 509	6 500	10 114	16 339	27 269	33 562	36 933	38 915
Slovakia	6 707	16 532	25 464	40 950	68 672	85 365	95 080	103 050
CEEC10	535899	754329	952131	1292799	1890933	2235498	2420513	2531556

\*adapted from Boeri and Brücker (2001)

<sup>21</sup> see the study for the methodological assumptions for the projections

<sup>22</sup> a total of short-term (seasonal) and contract (more than one year) workers together (based on statistics from the National Labor Office, NUP)

## Factors of international migration

According to one public opinion survey, the Slovak citizens perceive the benefits of the EU accession in terms of an overall improvement of economic development (44 percent), new job creation (24 percent), EU financial transfers (22 percent), and extended opportunities to work in EU countries (20 percent)<sup>23</sup>. On the other hand, rising price levels (25 percent), the selling-off of the domestic companies (25 percent), and increased budgetary costs (24 percent) are among the disadvantages, which are expected by the population.<sup>24</sup>

Based on the migration trends since the 1990s, Slovakia does not need to worry about the massive influx of labor from abroad,<sup>25</sup> with its labor market being attractive mostly to citizens of other CEE countries, the three most represented national groups of legal foreign workers being the Czechs, the Ukrainians and the Polish. Slovakia's cross-border migration flows are fairly limited both in size and frequency (short-term, seasonal workers dominate).

According to the quarterly statistics published by the National Labor Office (NUP), as of 31 December 2002 the number of working citizens of the EU candidate countries in the Slovak Republic was 2,386, of which from: Bulgaria 44, Cyprus 1, the Czech Republic 2,023, Estonia 0, Lithuania 0, Latvia 69, Hungary 87, Poland 119, Romania 32, and Slovenia 11. In the same period, there were 1082 EU citizens working in the Slovak Republic, of which: France 115, Germany 355, Austria 121, Italy 102, the United Kingdom 187, Belgium 26, Denmark 31, Finland 5, Netherlands 41, Portugal 5, Spain 54, Sweden 23, Ireland 14, and Greece 3.

Based on the OECD research cited in Marcincin and Lubyova (2002), in the Czech Republic the share of foreigners on the total population was 2 percent in 1998, followed by Hungary with 1.5 percent. These figures are fairly close to those of some of the EU member states. Slovakia, with 0.5 percentage share, lagged also behind Bulgaria (1 percentage share), but was ahead of Poland (0.1 percent). Similar picture emerged from a comparison of the shares of foreign workers in total national employment: the Czech Republic was taking the lead with 2.4 percent,

well ahead of Hungary (0.6 percent) and Slovakia (0.3 percent). In absolute terms, the Czech Republic reported the highest number of foreign nationals (219 thousand, of which 110 thousand being workers). The lowest number of foreign workers was reported by Slovakia (27 thousand) and Bulgaria (several hundreds). The Czech labor market seems to be the most open to foreign labor migrants. The least open country from this comparative perspective is Bulgaria, with Poland, Hungary and Slovakia taking the intermediate position.<sup>26</sup>

**Table 10. Immigrants to Slovakia (by country of origin)**

	1993	1994	1995	1996	1997	1998	1999	2000	2001
<b>European Union</b>	362	294	304	272	223	199	218	170	243
EFTA countries	61	57	67	48	54	51	30	41	38
<b>EU candidates</b>	7 406	3 371	1 692	1 320	1 075	965	1 048	1 408	1 116
Ukraine & Russia	411	503	499	357	455	359	266	217	156
<b>Continents:</b>									
Africa	30	48	28	31	29	25	37	33	21
Asia	193	149	82	112	133	133	163	70	118
America	227	192	203	173	141	137	127	192	202
Australia & Pacific	49	63	35	45	36	46	18	16	22
Europe	8 453	4 467	2 707	2 115	1 964	1 709	1 716	1 963	1 659
<b>Total</b>	<b>9 106</b>	<b>4 922</b>	<b>3 055</b>	<b>2 477</b>	<b>2 303</b>	<b>2 052</b>	<b>2 072</b>	<b>2 274</b>	<b>2 023</b>

Note: Turkey and Cyprus are included into both Asia and EU candidates  
Source: Slovak Statistical Office

**Table 11. Emigrants from Slovakia (by country of origin)**

	1993	1994	1995	1996	1997	1998	1999	2000	2001
<b>European Union</b>	31	25	47	70	226	245	247	348	397
EFTA countries	1	0	4	9	27	41	26	36	34
<b>EU candidates</b>	7,295	109	130	103	230	287	230	335	422
Ukraine and Russia	3	4	5	7	2	10	8	13	6
<b>Continents:</b>									
Africa	0	0	1	3	6	3	3	6	3
Asia	2	1	3	3	8	18	10	8	12
America	18	13	10	13	51	104	74	75	110
Australia & Pacific	8	3	9	10	30	21	14	17	17
Europe	7,327	137	190	192	477	600	517	705	869
<b>Total</b>	<b>7,355</b>	<b>154</b>	<b>213</b>	<b>222</b>	<b>572</b>	<b>746</b>	<b>618</b>	<b>811</b>	<b>1,011</b>

Note: Turkey and Cyprus are included into both Asia and EU candidates  
Source: Slovak Statistical Office

<sup>23</sup> This can also be illustrated by the spectacular number of Slovak job applications (5,971 compared to only about 10,000 from Poland) received by the European Commission in Brussels January this year, within the job competition for a total of about 1,000 new posts offered to candidates from the accession countries.

<sup>24</sup> Gyarfasova et al. (2001:211) reporting on the survey carried out in February 2000.

<sup>25</sup> Recent public polls suggest that a massive emigration from Slovakia should not be feared, due to various psychological factors, geographical distance, low internal labor mobility, limited language skills, work qualifications, etc.

<sup>26</sup> In the Czech Republic, more than 60 percent of the foreign population is active on the labor market. In the other four CEE countries, this value is lower than 20 percent. There were 2 percent of foreigners living among long-term or permanent population in the Czech Republic in the year 1998, but more than 2.4 percent of foreigners within the labor force. In Poland, these two values were approximately equal (around 0.1 percent). In other mentioned countries, shares of foreigners within individual labor forces were lower than their percentage shares in the respective populations. By far, the biggest inequality was reached by Bulgaria with a 1-per cent share of foreigners living in the population, but only a 0.01 percent share of foreigners within the labor force.



On the other side of the equation, the Slovaks migrate to jobs mostly to the neighbouring Czech Republic, Austria and Germany. Legal migration of Slovak workers to the Czech Republic and Germany is regularly monitored by NUP<sup>27</sup>. In the case of **the Czech Republic** and Slovakia, there is a substantial migration imbalance between the two countries: while more than 2,000 Czech citizens work in Slovakia legally, the number of Slovak workers in the Czech Republic has traditionally counted in tens of thousands, despite the decreasing volumes in recent years.<sup>28</sup>

According to NUP data, a total of 9,065 Slovak citizens worked legally in **Germany** at the end of 2000, of which 8,151 on a short-term basis, and 914 had job contract lasting more than one year. The total number increased to 11,041 and 11,832 at the end of 2001 and 2002, respectively.

Both measuring and controlling migration flows between Slovakia and **Austria** is a much more difficult task, which deserves a special attention here. Since the Slovak capital of Bratislava and its surrounding region is within the commuting distance from the City of Vienna, labor mobility is not confined just to migration. Rather, a much larger amount of Slovak labor in Austria may be daily or weekly commuters who will not show up in the official migration statistics, and will not be deterred by the administrative constraints on labor mobility.

Using the survey method, Fassmann et al. (1993) analyzed the adds of foreigners looking for work in a local newspaper that is typically used for announcing short-term jobs. They found that the share of adds from former Czechoslovakia was high only 1990 and 1991, but declined considerably afterwards. This trend continued also in the following years. A follow-up analysis in 1994 showed that the share of Czechs and Slovaks among all foreigners offering work was just 18.5 percent. For comparison, the share of Poles was 48.3 percent. Maier (1994) reports the results of interviews conducted at the border stations between Vienna and Bratislava. They found that 39 percent of all trips they observed were interactions between the two cities. When one takes into account also the hinter-

land of the two cities, more than 62 percent of the interactions are captured. Of the 812 people interviewed that were going into Austria, only 1/3 reported that work was the purpose of their trip. Other purposes (business, shopping) were almost as important. Calculations based on these survey data show that the number of Slovaks who commute into Austria for work can hardly exceed 2,500. These mid-1990 predictions are well in line with the most recent experts' opinions saying that there are about 8,000 Slovaks (mainly from the region of Western Slovakia) commuting to Lower Austria, of which about 3,000 commute directly from the capital city of Bratislava.

Among the several recent Austrian studies, relying on econometric modeling, Walterskirchen and Dietz (1998) estimated that the total of 150,000 CEE workers would commute to Austria over the period until 2015, 50,000 of them coming from Slovakia. However, some serious questions have been raised about the relevance of assumptions underlying such commuter number estimates. For example, were the geographic distance that relevant, majority of commuters would come from Bratislava, which is only an hour's drive from Vienna. But according to the opinion surveys quoted above, only very few inhabitants of Bratislava actually contemplate such a move (see also discussion below).

In short, it is evident that the inflow of workers from Slovakia into Austria is fairly limited. Labor mobility is surprisingly low despite enormous income differentials. To some extent this can be attributed to Austria's restrictive immigration policy. Another factor is that Austrian industry seems to rely on established channels (through personnel agencies) and recruits new foreign labor from the traditional countries of Ex-Yugoslavia and Turkey.

### Factors of intra-national migration

There are no sociological surveys available which would shed some light on the factors determining cross-border migration behaviour of the Slovaks. However, the possible causes of the relatively low levels of international migration of the Slovaks (reported above) can be extrapolated from the lack of their labor mobility inside their home country, which

<sup>27</sup> However, some of the Slovak labor migration flows (e.g. short-term and illegal) to other countries is difficult to monitor by the Slovak statistical authorities, and may thus not show up in the official migration statistics. Estimations of Slovak workers abroad by receiving countries are therefore much more realistic than any estimations based on data reported in Slovakia, which indicate only a minimal number of legal Slovak workers abroad.

<sup>28</sup> The number increased from about 23,000 in 1993 to about 72,000 persons at the end of the year 1996. In the period 1997-2000 a declining trend was observed, with the figures falling to 61,000 persons (end of September 2000). This trend was matched by a parallel growth of the number of the Czech citizens working in the Slovak Republic from 1,200 to 2,200 persons during the period 1993 - 2000.

is the lowest of all OECD countries.<sup>29</sup> The lack of cross-border mobility can also be documented by the history of the former Czechoslovakia, when there were few, if any, cultural, religious, or linguistic barriers to labor mobility, as well as no legal restrictions on migration across the Czech-Slovak border. This has not changed after the break-up of Czechoslovakia, as the two countries agreed to preserve the common labor market indefinitely. Nevertheless, migration fell both internally, and between the Czech lands and Slovakia, with only 0.01 and 0.06 percent of the Czechs and the Slovaks, respectively, crossing the new border in 1996.<sup>30</sup>

Significant regional income and unemployment differences in Slovakia were identified as one of the main problems of labor market development, in the Joint Assessment of Employment Priorities in the Slovak Republic<sup>31</sup>, prepared by the EU and Slovak Republic. Despite pervasive regional labor market disparities, the mobility of the Slovak population<sup>32</sup> has significantly decreased in the recent two decades: while almost 120,000 people moved inter-regionally in the year 1980, only about 77,000 people reported a migratory move in 2000 (i.e. 14 people per 1000 inhabitants). Short-distance moving dominates long-distance migration, which is a pattern observed in other candidate countries as well.<sup>33</sup>

**Table 12. Intra-national migration in Slovakia**

	1993	1994	1995	1996	1997	1998	1999	2000	2001
Number of migrants ('000)	85.0	82.6	68.3	80.2	82.5	84.8	79.0	76.9	79.9
of which:									
within districts	59.6	58.7	55.8	50.0	43.5	37.6	35.7	35.2	36.8
within regions	22.2	21.9	23.5	50.0	33.4	27.5	25.1	24.3	25.0
across regions	18.2	19.4	20.7	n.a.	23.1	19.7	18.2	17.3	18.1

Source: Statistical Yearbook 2002, Slovak Statistical Office

<sup>29</sup> see also the recent OECD Economic Survey of the Slovak Republic (2002)

<sup>30</sup> On the other hand, as reported by Fidrmuc et al (1999), some 59 thousand Slovak citizens, including commuters, were employed in the Czech Republic in 1995 and about 72 thousand in 1996. This corresponded to 2.3 and 2.8 percent respectively, of the Slovak labor force, and certainly helped mitigate the Slovak unemployment problem, with the Slovak unemployment rate standing at 13.1 and 12.8 percent in the respective years.

<sup>31</sup> Joint Assessment of Employment Priorities in the Slovak Republic (2001)

<sup>32</sup> measured by moving (ie. formal change of permanent address)

Several explanations were suggested to account for this fall in mobility during economic transition years. First, the removal of some restrictions on the housing market resulted in sharp increases in rents and real estate prices. Second, commuting to work has become more common. Third, the formal requirement of reporting one's change of residence address is now more often ignored (see e.g. Fidrmuc et al., 1999, Fidrmuc, 2000<sup>34</sup>, World Bank, 2001, OECD, 2002). Fourth, similar to countries like Italy and Spain, the existence of social networks and the importance of family and friends to finding jobs are thought to be responsible for the reluctance to move away from depressed regions in Slovakia. Fifth, an important barrier to commuting seems to be the relatively high transport costs in Slovakia (see World Bank, 2001:57-58)

This lack of labor mobility may have important policy implications for the timing of accession to the European Monetary Union (EMU), to be decided on in the coming months and years (see below). Fidrmuc et al. (1999) even argue that low labor mobility in the former Czechoslovakia contributed to economic tensions that eventually led to the break-up of Czechoslovakia at the beginning of the 1990s.

## 4.2. Challenges of EU Accession Regarding Free Movement of Workers

In the area of **mutual recognition of professional qualifications**, the Act on Mutual Recognition of Professional Qualifications, adopted by the Parliament in June 2002, aims to establish a general framework for the recognition of foreign professional qualifications in Slovakia and to align with the general systems directives. Under this Act, the Centre for Equivalence for Diplomas has been established

<sup>33</sup> Analysing migration situation in the Czech Republic, Hungary, Slovenia and Slovakia for the period 1990-98, Huber (2001) finds that the migration rates in mid-1990s were not comparable to those of the EU, reporting even further decrease in the late 1990s. Also, Fidrmuc (2001) finds that there is a low effectiveness of migration on reduction of regional differences in transition economies. Differences in unemployment rates apparently do not affect migration flows among regions. However, an interpretation of the results must take account of the fact, that permanent address-based statistics are misrepresenting, because many people work on the long-term basis outside their home regions without changing their permanent address. This might be explained by a complicated housing situation in Slovakia.

<sup>34</sup> Fidrmuc (2000) provides an econometric analysis of the determinants of intra-national labor migration in Slovakia, based on data for the first half of the 1990s. He includes not only the traditional factors like differences in wages and unemployment, but also other economic (size of the private sector, shares of agricultural and industrial employment), social and demographic factors (educational, ethnic, religious and urban/rural structure of the population), which significantly affected the migration process in the respective period.

as an organizational unit of the Ministry of Education. In February 2002, the Parliament adopted the Act on Higher Education, which makes a clear distinction between academic and professional recognition of qualifications. In April 2002, the Parliament adopted laws in the area of health care, accelerating legislative alignment with sectoral directives. Good progress can be reported on *citizens' rights*. With the new Act on Stay of Aliens, effective from April 2002, Slovakia has aligned its legislation with the *acquis* provisions on residence rights. There have also been developments in the area of voting rights. The Amendment to the Act on Elections to Municipal Self-Government Bodies, which came into force as of March 2002, authorizes foreigners with permanent residence in Slovakia to elect and to stand as a candidate for municipal self-government bodies.

Within the domain of **free movement of workers**, the safeguarding of the supplementary pension rights of employed and self-employed persons moving within the Community has been regulated by the latest amendment to the Act on Supplementary Pension Insurance, adopted by the Parliament in May 2002. Preparatory works has continued to facilitate Slovakia's participation in the European Employment Services network (EURES).

Slovakia has so far concluded 11 bilateral agreements on mutual employment of citizens with other countries.<sup>35</sup> Of these international agreements, only the Convention on good neighbourhood and co-operation with the Czech Republic embodies certain above-standard arrangements (numerous exceptions from work permits, mutual recognition of claims for unemployment benefits, etc.) resembling free movement of workers within EU. Agreements with other countries mostly contain quantitative restrictions on the number of workers, which are very low (typically a few hundreds temporary workers, etc.), especially vis-à-vis current EU member countries.<sup>36</sup>

Slovakia has continued to strengthen bilateral relations with a view to the future **coordination of social security** matters and development of institutional capacity has accelerated. The adoption by the Parliament of the Act on Social Insurance in May 2002 and the Act on Health Insurance in August 2002 have been the first steps in the social security reform

in Slovakia. Bilateral agreements covering health insurance and pension benefits were signed in December 2001 with Austria and in May 2002 with Spain. A similar bilateral agreement with the Netherlands entered into force in May 2002.

### Slovak Roma migration

The economic geography of the Eastern Slovak regions is very specific in two different respects. First, their unpleasant image of "backward peripheries of the New Europe"<sup>37</sup> have recently caught much of the migration policy attention in the EU, due to an exodus of Roma population, which is geographically concentrated exactly in these parts of Slovakia. The Slovak government has had to face and address the criticism from many European governments on the "Roma issue", which posed an unexpected short-run challenge to their asylum systems in 2000.

In 1998, based on data from International Migration Organization (IOM), 467 Roma applied for asylum in Germany and the Netherlands, while the figure for the UK was 1,256. In 1999, the number of applications increased up to 4,836, with the target countries including mainly Finland, Belgium and Denmark. Most recently, the main destination of the Roma asylum-seekers have been the countries of Denmark, Belgium and Norway; their national governments responded by introducing visa for all Slovak citizens, a defensive policy which was partially revised later on.

According to a mid-term evaluation of an EU-funded IOM program (IOM, 2000) for the return and counselling of Roma asylum-seekers from the Czech Republic, Slovakia and Romania who had sought asylum in Belgium, Finland and the Netherlands, as many as one third of those who returned to the Czech Republic left again shortly after the return. It appears that the sustainability of returns depends not only on the quality of the assistance provided upon return and the protection of human rights of the returnees, but also, and more importantly, on **the improvement in the socio-economic conditions of everyday life (i.e. sustainable development concept)**.

Second, as the EU external border moves eastwards, the East-Slovak regions will find themselves in a stra-

<sup>35</sup> Belgium (October 16, 1937), the Czech Republic (October 29, 1992), France (May 22, 1930), Finland (February 21, 1998), Luxembourg (May 27, 1998), Germany (March 18, 1996), Poland (June 16, 1992), Russia (February 13, 1995), Switzerland (December 8, 1995), Ukraine (March 6, 1887), and Hungary (February 12, 1999).

<sup>36</sup> A little bit more liberal are the limits imposed by Germany. These are, however, regularly reviewed by the German side with respect to situation on the German labor market.

<sup>37</sup> The CEE region has a very clearly marked *external periphery*, stretching out from the north-eastern corner of Poland through *eastern Slovakia* to the south-eastern part of Hungary, and then through eastern Romania to Montana and Lovech in northern Bulgaria. These peripheral areas are the least developed in the region. They are relatively sparsely populated, rural in character, and have poorly developed urban systems and infrastructure (although the Hungarian regions along the Romanian border are relatively well developed). Their backward position is historic, dating back to long before the transition period (Gorzela, 1998).

tegic gateway position between the EU and the “Wild East” countries of the former Soviet Union. In the EU, the gateway regions and cities, which have traditionally dealt with large numbers of immigrants benefit from being customs administration centers for the Community. However, given the recent developments in the EU’s Justice and Home Affairs regime, these geographical areas have to carry the administrative burden of processing applications from asylum seekers, irrespective of their final destination (the Dublin Convention). They also have to absorb the policing costs of preventing illegal entry and of dealing with associated criminal activities such as drug and human trafficking, illegal exploitation of cheap foreign labor and the black market. In Eastern Slovakia, problems of peripherality and the fact that political boundaries are increasingly limiting its cross-border development potentials, mean that even the biggest East-Slovak city of Kosice currently lacks the adequate infrastructure to function as a major gateway city, should Slovakia become the EU/Schengen member state in the near future.

### Lack of labor mobility

The pattern of labor mobility described above has at least two important medium-term policy implications. **First**, regional differentials in unemployment and wages will not be eliminated by the migration process<sup>38</sup>. An appropriate policy response may be needed to avert the creation of Mezzogiorno-type regions in Slovakia.

**Second**, labor mobility substitutes for the absence of autonomous monetary policy in a monetary union. Unemployed workers migrate from regions hit by an adverse shock to regions with more favorable conditions, thus equilibrating the effects of asymmetric shocks. In a hypothetical union with perfect mobility of production factors, regions would adjust immediately. However, when labor mobility is low and prices and wages are rigid, effects of such asymmetric shocks persist and currency unions have to rely on other mechanisms, such as fiscal transfers<sup>39</sup>, to absorb them.

In this respect, given the low efficacy of migration process in smoothing away inter-regional unemployment and wage differentials, an early membership in the EMU is not necessarily an optimal policy choice for Slovakia and other accession countries. As the

accession countries will likely continue to face different external shocks than the EMU core, at least in the medium term, they may indeed benefit from retaining the option to adjust their exchange rates (Fidrmuc, 2000, Fidrmuc, 2001).

There are three more general comments on the labor migration trends in Slovakia, that we want to add in the context of the present paper. **First**, migration involves taking risks as well as incurring sunk costs. A certain degree of risk aversion will lead to attitudes of “wait and see”, as long as there is no dramatic deterioration that will force you ultimately to take a decision (Straubhaar, 1998). This option value of migration<sup>40</sup> leads to a paradox. It may well be that a complete elimination of legal barriers to the free circulation of workers will actually result in a decrease of cross-border labor movements and a strengthening of “wait and see” attitudes.<sup>41</sup>

The choice of such rational strategy may help explain the relatively low levels of migration to the EU of the better-off population mainly from the Bratislava capital region. Related to this is another positive economic value of immobility: staying at home allows people to use their specifically local know-how for earning an income and for spending that income. This know-how would be lost in the case of migration (thus reducing human capital formation the home region), and would have to be acquired once more at the new place of work/residence.

**Second**, an increasing geographical mobility of labor triggered by the integration of Slovakia into the EU should be viewed in the light of the fundamental interdependencies governing migration (of labor and capital) and trade (trans- and cross-boundary) in today’s global economy. Such a perspective is strongly supported by theoretical arguments<sup>42</sup>, but nevertheless often neglected in favor of a more

<sup>38</sup> Note also that such possibility of using public expenditures as an alternative adjustment mechanism is even further restricted by the tight fiscal convergence criteria à la Maastricht.

<sup>40</sup> for a comprehensive theoretical argument see Burda (1995).

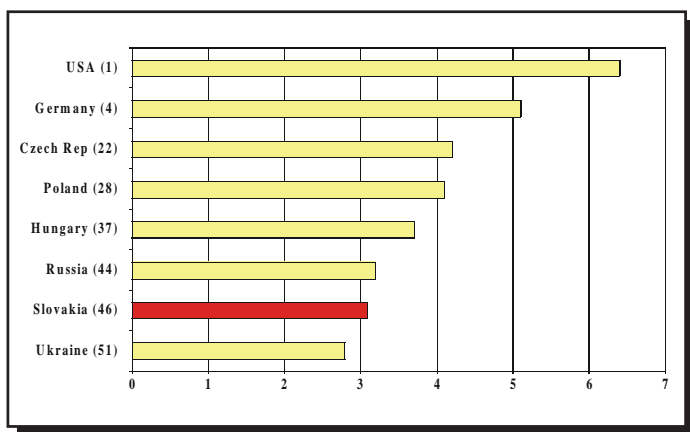
<sup>41</sup> If you are sure you will be able to get in anytime you like, you need not go now.

<sup>42</sup> Economic integration in a single market takes place above all via trade in goods and services and via capital transfers, and not so much via the migration of workers. Trade flows react much more elastically than people to the formation of a single market. To a large extent trade in goods and capital transfers make the migration of labor unnecessary. For economists this is no surprise. It is exactly the result that is predicted by the traditional Heckscher-Ohlin-Samuelson models of international economics: trade and migration are substitutes. The same is true of capital flows. Bringing machinery to labor renders unnecessary the movement of people to the machines (see Straubhaar, 2001, for a more extensive theoretical discussion on the East-West migration potential).

<sup>38</sup> see Fidrmuc and Huber (2001)

sectoral (usually defensive) policy approach. In the EU integration context, in as far as there is a complementary relationship between capital transfers and labor migration flows, FDI and labor mobility are simply necessary in order to exploit the efficiency advantages of an integrated internal market area (see also Akkoyunlu, 2001). In this case, however, it is primarily a question of the migration of highly qualified specialists<sup>43</sup> or much demanded seasonal labor, and not of the mass migration of unskilled workers. What might then cause a real problem, is (too much) CEE emigration rather than (too much) CEE immigration to the EU, as the former may undermine human capital formation in the respective home countries and regions (see Figure 2).

**Figure 2. Brain drain**



Note: The most talented workers remain in the country (1= strongly disagree, 7 = strongly agree)

Source: Harvard University (2002)

**Third**, beside the stressfulness and selectivity of the cross-border migration process, 'it is also *people's social and cultural ties* to their local environment which pose *an important obstacle to labor migration* in Europe and which has been commonly underestimated from the perspective of theoretical economics' (see Straubhaar, 2001). Empirical research and experience show that in the common labor market of the EU, labor has been extremely immobile: the large majority of people prefer to live, work and stay immobile where one has one's own roots. The above-mentioned evidence of the limited intra-national and international labor mobility in Slovakia seems only to correspond to this general EU-wide pattern.

<sup>43</sup> e.g. IT specialists

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# APPENDICES

Note: If not indicated other, data derived from national sources (Statistical Office of the SR, National Bank of Slovakia, National Labor Office, Social Insurance Agency)

**Table A1. Main macroeconomic indicators**

Indicator	1997	1998	1999	2000	2001	2002	Explanatory note
GDP, current prices, million USD	21.080	21.991	20.178	20.134	20.462	23.681	Source: Eurostat
Real GDP per capita (PPP), EU-15=100, %	47.9	48.5	48.3	47.9			
Inflation (CPI-100), yearly, previous year=100, %	6.1	6.7	10.6	12.0	7.3	3.3	
Current account balance (as % of GDP)	-9.9	-10.1	-5.8	-3.7	-8.8	-8.2	
Foreign direct investment (as % of GDP)	0.5	2.1	3.7	10.7	5.8	16.9	
Exchange rate SKK/USD, average for the period, SKK	33.616	35.242	41.417	46.200	48.347	45.335	2002 estimate
Exchange rate SKK/USD, end of period, SKK	34.782	36.913	42.266	47.389	48.467	40.036	
Gross external debt, million USD, million USD	9.896	11.902	10.518	10.804	11.220	13.188	
Gross external debt, as % of GDP	47.8	55.9	53.4	56.7	53.9		
Domestic government and government guaranteed debt, as % of GDP	-2.5	-2.6	-1.8	-3.1	-4.6		
International Currency Reserve at the national Bank, million USD	3.203.9	2.867.1	3.369.9	4.046.2	4.138.0	8.701.6	Since 2002 new methodology of calculation
Base interest rate, nominal, December, %	8.8	8.8	8.8	8.8	8.8	6.5	
Base interest rate, effective annual, December, %	8.8	8.8	8.8	8.8	8.8	6.5	

**Table A2. Socio-economic indicators**

Indicator	1997	1998	1999	2000	2001	Explanatory note
Population, as of 31.12, number	5.387.650	5.393.382	5.398.657	5.402.547	5.378.951	2001 data includes results of population census
Population, annual average, number	5.383.233	5.390.866	5.395.115	5.400.679	5.379.780	2001 data includes results of population census
Working-age population (age 15-64), as of 31.12, %	67.7	68.3	68.8	69.3	68.9	2001 data includes results of population census
Life expectancy, total	72.81	72.66	72.99	73.18	73.40	
Life expectancy, male	68.9	68.6	69.0	69.1	69.5	
Life expectancy, female	76.7	76.7	77.0	77.1	77.6	
Annual total income of households						See table A6



Table A3. Key labor market indicators

Indicator	1997	1998	1999	2000	2001	2002	Explanatory note
Economic activity rate (LFS), %	59.9	59.9	60.0	60.3	60.7		
Employment rate (LFS), %		51.7	49.7	48.6	48.6		
% of total employment (LFS) in:							
agriculture	8.3	8.2	7.3	6.7	6.1		
industry	37.7	36.2	37.0	37.2	37.6		
services	49.7	51.5	52.5	55.9	56.2		
not specified	4.3	4.1	3.2	0.2	0.1		
% of total employment (LFS) in:							
private sector		65.2	66.0	66.8	68.5		
public sector		34.8	34.0	33.2	31.5		
Self-employed (% of total employment (LFS))		6.8	7.7	8.0	8.4		
Unemployment rate, %, National Labor Office	12.94	13.67	17.31	18.24	18.25		
LFS	11.8	12.5	16.2	18.6	19.2		
Youth unemployment (age group 15-24), National Labor Office						17.90	
LFS	21.7	23.6	32.1	35.2	37.3	18.5	
Long-term unemployment (as % of unemployed for 12 months or more in total unemployment), LFS	50.2	50.7	46.9	53.9	55.7		
Informal employment (estimate)				16.3			See also table 5 in the text
Educational level of employed, % of total employed, LFS:							
Basic	29.0	26.7	21.1	19.6			
Trained	31.0	35.3	37.9	40.3			
Secondary	6.9	6.6	5.8	4.7			
Trained with SLE	3.7	4.1	4.1	4.8			
Full secondary compreh.	6.2	6.0	5.5	4.9			
Full secondary vocational	19.9	17.8	22.3	22.4			
University	2.8	2.9	3.0	3.2			
Without education	0.2	0.3	0.2	0.1			
Educational level of unemployed, % of total unemployed, LFS							
Basic	10.8	9.6	7.9	7.0			
Trained	31.3	33.2	35.3	35.1			
Secondary	7.8	7.0	4.9	4.1			
Trained with SLE	4.6	4.8	4.8	4.6			
Full secondary compreh.	4.9	5.8	5.6	5.4			
Full secondary vocational	28.7	27.8	29.5	31.5			
University	10.9	11.1	11.9	12.3			
Without education	0.0	0.0	0.0	0.0			
Labor productivity (GDP per employee, current prices, USD)	9.556.19	10.002.27	9.463.91	9.579.86	9.635.07		See also table A6
Real total labor costs SKK/hour		99.68	101.19	107.08			
Average monthly gross wages of the employees under labor contract, total, USD by economic activity (NACE)	274.5	283.8	259.0	247.4	255.8		
Average pay increase, %:							
nominal	13.1	8.4	7.2	6.5	8.2	298.0	
real	6.6	1.7	-2.8	-3.1	0.8		
Expenditures on main labor market policies (active and passive measures as % of GDP):							
Passive		70.6	93.9	79.7	68.2		
of which:						9.3	
Unemployment benefits		71.6	73.2	71.4	72.0	5.8	
Active		29.5	6.1	20.3	31.8		
of which:							
Retraining		7.3	15.5	4.0	8.8		
Support for new jobs		87.2	62.6	86.4	77.7		

**Table A4.1. Replacement rate of average old-age pension**

Indicator	1997	1998	1999	2000	2001	2002
Replacement rate of average old-age pension (as % to average gross wage)	44.7	44.9	45.5	47.1	46.8	46.5

**Table A4.2. Social Insurance**

Indicator	1998			1999			2000			2001		
	Employer	Employee	Total	Employer	Employee	Total	Employer	Employee	Total	Employer	Employee	Total
Social security burden on employers and employees (as % gross wage)												
Pension fund	21.60	5.90	27.50	21.60	5.90	27.50	21.60	5.90	27.50	21.60	6.40	28.00
Employment fund	3.00	1.00	4.00	3.00	1.00	4.00	2.75*	1.00	3.75*	2.75	1.00	3.75
Guarantee fund	-	-	-	-	-	-	0.25*	-	0.25*	0.25	-	0.25
Health Insurance	10.00	3.70	13.70	10.00	3.70	13.70	10.00	3.70	13.70	10.00	4.0**	14.00
Sickness Insurance	3.40	1.40	4.80	3.40	1.40	4.80	3.40	1.40	4.80	3.40	1.40	4.80
Total	38.00	12.00	50.00	38.00	12.00	50.00	38.00	12.00	50.00	38.00	12.80	50.80

Note: \* Since 1 May 2000

\*\* Since 1 January 2001

Source: Ministry of Labor, Social Affairs and Family of the SR

**Table A5. Labor costs and wages**

Branch of economic activity (NACE)	1999	2000	2001
Economy of the SR	SKK 10 728	SKK 11 430	SKK 12 365 Of which
by branches (as % of average wage)			
Agriculture, hunting and forestry, fishing	78.1	78.9	78.9
Industry total	100.3	102.6	108.2
Construction	92.3	92.2	89.3
Wholesale and retail trade	107.5	110.8	108.3
Hotels and restaurants	75.7	77.0	76.4
Transport, storage and communication	107.8	109.0	110.2
Financial intermediation	186.0	193.8	197.4
Real estate, renting and business activities	122.2	123.3	125.7
Public administration and defence	121.7	120.6	118.6
Education	78.3	78.7	76.4
Health care and social work	84.8	81.5	83.9
Other community and social services	87.8	72.5	71.8

**Table A6. Income. Savings. Expenditures.**

Indicator	1997	1998	1999	2000
Gross money income (USD)	1 954.1	1 988.5	1 786.9	1 717.5
of which in %				
Gross income from employment	65.8	66.5	68.0	69.8
Income from business	3.7	5.6	4.1	3.8
Property income	1.2	1.0	0.8	1.3
Social income	23.0	21.5	21.8	19.5
of which: pensions	17.5	15.8	26.2	14.4
Drawn savings (USD)	248.9	315.3	282.2	291.6
Gross money expenditure (USD)	1,915.1	2,005.6	1,780.3	1,700.8
Of which in %				
Consumption expenditure	79.1	79.2	78.7	79.5
Of which:				
Food and non-alcoholic beverages	25.4	24.3	23.5	22.6
Alcoholic beverages and tobacco	3.1	2.9	2.8	2.7
Clothing and footwear	9.0	8.5	7.3	6.9
Housing, water, energy and fuels	10.9	10.5	12.4	14.1
Furnishing and household equipment	5.0	5.3	4.9	4.8
Health	1.0	1.0	1.2	1.3
Transport	6.9	7.5	6.8	6.8
Communications	1.5	1.7	2.1	2.3
Recreation and culture	6.4	6.9	6.5	6.5
Education	0.4	0.4	0.4	0.5
Hotels and restaurants	3.9	4.1	4.3	4.4
Other expenditure	20.9	20.8	21.3	20.5
Of which: Income tax	6.5	6.9	7.2	5.6
Compulsory personal insurance	7.7	7.6	7.8	8.0
Deposits (USD)	271.6	285.8	279.7	298.2

**Table A7. Migration**

Indicators	1993	1994	1995	1996	1997	1998	1999	2000	2001
International migration:									
Immigration (from):									
EU members	362	294	304	272	223	199	218	170	243
EU candidates	7 406	3 371	1 692	1 320	1 075	965	1 048	1 408	1 116
The Czech Republic	7 232	3 144	1 497	993	867	777	856	1 268	990
EFTA	61	57	67	48	54	51	30	41	38
Ukraine & Russia	411	503	499	357	455	359	266	217	156
Continents:									
Africa	30	48	28	31	29	25	37	33	21
Asia	193	149	82	112	133	133	163	70	118
America	227	192	203	173	141	137	127	192	202
Australia & Pacific	49	63	35	45	36	46	18	16	22
Europe	8 453	4 467	2 707	2 115	1 964	1 709	1 716	1 963	1 659
Total	9 106	4 922	3 055	2 477	2 303	2 052	2 072	2 274	2 023
Emigration (to):									
EU members	31	25	47	70	226	245	247	348	397
EU candidates	7 295	109	130	103	230	287	230	335	422
The Czech Republic	7 276	95	108	89	212	251	208	310	398
EFTA	1	0	4	9	27	41	26	36	34
Ukraine & Russia	3	4	5	7	2	10	8	13	6
Continents:									
Africa	0	0	1	3	6	3	3	6	3
Asia	2	1	3	3	8	18	10	8	12
America	18	13	10	13	51	104	74	75	110
Australia & Pacific	8	3	9	10	30	21	14	17	17
Europe	7 327	137	190	192	477	600	517	705	869
Total	7 355	154	213	222	572	746	618	811	1 011



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PRAXIS CENTER FOR POLICY STUDIES, ESTONIA

**EU Enlargement and Its Impact  
on the Social Policy and Labor  
Market of Estonia**

*Tallinn, 2003*



# 1. Macroeconomic Picture and Stage of EU Accession

## 1.1. Macroeconomic Background

In order to give a systematic overview of the current state of the Estonian macroeconomic framework, some kind of supporting structure would be useful. Estonia is firmly committed to joining the EU and the negotiations on the terms of accession have already been concluded. In September 2003 the Estonian people will give their vote on whether to join or not and this will be the final step of the accession process. Estonia will probably become a member of the EU during 2004.

In light of these events, the accession criteria would be an excellent framework for discussing the development of the Estonian macro economy. The overview starts with the outcomes of existing reforms, which can be viewed as approximating "the Copenhagen Criteria"<sup>44</sup> (specifically, the second criterion, as this seems to be more clearly connected with the current topic) and continues with the Maastricht Criteria<sup>45</sup> that must be met in order to apply for the European Monetary Union.

**The Copenhagen criteria:** The existence of a functioning market economy as well as the capacity to cope with competitive pressure and market forces within the Union.

The Estonian economy is considered one of the most liberal economies in the world. In the index of Economic Freedom, composed by the Wall Street Journal and The Heritage Foundation, Estonia ranked as the fourth most liberal economy in the world. This means that the Estonian market economy is in some aspects more liberal than in several Member States.

The **privatisation** of the economy has been completed, with only a handful of strategic companies left under the governance of the State. The list includes the Narva Power Stations (Estonia's largest oil shale based power stations), the Port of Tallinn (the largest port in Estonia) and holdings (between 40-50 percent of the equity capital) in Estonian Telecom and Estonian Railway. There are some less significant holdings in other companies as well, but the list is relatively short.

Rapid transformation from a planned economy to a market economy is also reflected in the **structure of the Estonian economy**. In 1993 the share of the tertiary sector was 57 percent of GDP, in 2001 this figure has increased to 66 percent. The share of the primary sector has declined from 11 percent to 6 percent (Statistical Office of Estonia). The structure of economy by firm size indicates also a significant shift towards a market economy – in 2001 nearly 96 percent of Estonian companies were micro and small size companies with less than 50 workers. The same group of enterprises gave work to 49 percent of people employed in the entrepreneurial sector (Tax Office of Estonia).

The inflow of **foreign direct investments (FDI)** could be considered as a sign of satisfaction with the Estonian transition process by foreign investors. In 2001 FDI into Estonia reached 597.8 million Euros in total or 438 Euros per capita. If we look at the cumulative FDI inflow during 1989-2000, then, compared with Hungary, Czech Republic, Croatia, Slovenia, Poland and Latvia, Estonia ranked as the third with 1,307 USD per capita (Source: Bank of Estonia). Foreign investments come mainly from the EU countries,

<sup>44</sup> Excerpt from the Copenhagen Presidency Conclusions: "Membership requires a) that the candidate country has achieved stability of institutions guaranteeing democracy, the rule of law, human rights and respect for and, protection of minorities, b) the existence of a functioning market economy as well as the capacity to cope with competitive pressure and market forces within the Union. c) Membership presupposes the candidate's ability to take on the obligations of membership including adherence to the aims of political, economic and monetary union."

<sup>45</sup> The Maastricht Convergence Criteria were established in 1991 for those countries that planned to join the new European single currency arrangements in 1999. They were (are) designed to achieve a greater degree of economic convergence for countries participating in the Euro project. The criteria included targets for inflation, interest rates, government borrowing and the size of government debt.

especially Finland and Sweden.

**The Maastricht criteria:** The growth of the Estonian **Consumer Price Index** (CPI) has dropped from post soviet hyperinflation to 3.6 percent in 2002, almost reaching the price stability criteria set in the Maastricht Treaty. In the near future a slight increase of inflation is expected, mainly due to the convergence process with the EU price levels. However, the rise will not be very high.

The Maastricht Treaty states that the **budget deficit** may not be higher than 3 percent of GDP. In 2001 the Estonian budget was in surplus (0.4 percent of GDP). In previous years the budget has also been in slight deficit, but not significantly above the criterion.

**Government debt**, that must not exceed 60 percent of GDP, is also very low in Estonia – only 1.2 percent of GDP. Both budget deficit and the debt figures can be explained by the monetary policy framework, which Estonia has chosen. Estonia runs a currency board system, according to which the exchange rate is fixed with the Euro (in the beginning of our independence the currency was pegged with the German Mark) at the rate 1 EEK = 15.6 Euro. The precondition for the effectiveness of this system is a sound fiscal policy, as recognized by both government officials and politicians, thus no significant pressure to run budget deficit has emerged.

The last criterion (long term interest rate) is not measurable in Estonia, because there is no analogous government bond on the market that could be used as means of reference. In this respect, the Estonian financial market is not fully developed. On the other hand – this could be explained by the Government's cautious attitude towards taking loans.

The interest rate for long-term bank loans at the end of 2002 was 6.5 percent (Estonian Bank 2003). The Estonian **banking sector** and its services are quite well developed, however, it is mainly controlled by foreign capital. Bank loans are a quite important source of finance. The Estonian **stock market** is not very active and the majority of companies cannot use it as a means of equity finance. Bond finance is also not very popular.

**As a conclusion** it can be said that with 12 years of independence, Estonia has established quite a strong macroeconomic framework. Most of the state actions have been aimed at designing a healthy environment

for businesses and not so much on direct actions (e.g. direct support for businesses, protective tariffs etc). 12 years ago, Estonia did not possess the market economy experience required for a policy of active economic interventions. The resulting liberal and business-focused Estonian economic policy has been productive one. The next decade (post accession) will probably bring about some changes – the state role in the economy is expected to increase, the extent of this, however, is hard to predict.

## 1.2. Stage of EU Accession

Estonia has finished accession negotiations with the EU in Dec 2002. The Accession Treaty will be signed in April 2003. Estonia can become a full member of the EU in 2004, while the current member states, new member states and the European Parliament have ratified the Treaty. The referendum in Estonia will take place in September of 2003.

The negotiations began in 1998. The precondition for negotiations was to accept and implement the principles and *acquis communautaire* of the EU. The *acquis communautaire* was divided into 31 chapters, of which in current project are important Chapter 2 "Free Movement of People" and Chapter 13 "Social Policy and Employment". The ch 13 will be implemented fully and immediately. On the field of free movement of people there will be transition periods for working in another country. The transition period may last up to 7 years. The current EU member states may apply transition period to working both permanently and commuting to work. Estonia may apply similar safeguard clauses to the member state as the member state applies to Estonia. There will be no transition periods in free movement of services, with the exceptions of Germany and Austria.



## 2. Labor Market

### 2.1. Current State: Factors and Problems

The **Estonian population** in 2002 was 1,336,959 of which the working population (15-64 age group) formed 69 percent (916,493). The labor force supply is showing a steady decline. While in 1991 the number of the people aged 15-64 was 1.04 million, in 2001 it had already declined to 0.9 million. The reasons for this apparent trend are twofold: firstly, the outward migration of the working population after gaining independence (mainly in years 1991-1994), secondly, the ageing workforce (see Table 1). While the first reason has no impact on the current and future labor market, the second one needs to be considered in designing employment policies and social security systems (see also item 4.1.1.).

**Table 1. Demographic projections (medium scenario) up to 2020**

Indicator	2005	2010	2015	2020
Population (thousands)	1,316	1,253	1,190	1,127
Percentage of people aged 60 or over	20.6	21.7	23.3	25.0
Median age (years)	38.7	40.0	41.3	42.7
Life expectancy at birth men (years)	65.8	67.3	68.3	69.3
Life expectancy at birth women (years)	76.4	77.2	78.0	78.5

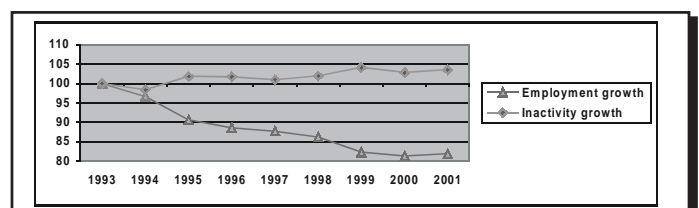
Source: Population Division of the Department of Economic and Social Affairs of the United Nations Secretariat, World Population Prospects: The 2000 Revision, referred through Leppik et al. 2003.

The **labor force participation** rate has also declined and was 70.1 percent in 2001 (15-64 age group)<sup>46</sup>. This decline in labor force participation is caused by the rise in the number of inactive people (see Figure 1). The number of inactive people who are ill or disabled has increased, and in addition, the number of people studying has grown. At the same

time the number of parents who have stayed home to care for children has declined. The substantial rise in discouraged people is one of the main problems in the Estonian labor market. Lately, the number of discouraged people has declined but at the same time the number of students has increased. This indicates that inactive people, instead of labelling themselves discouraged, prefer to be named as caring for family members or studying, even though the reason for it might be that they do not find a job.

The **employment rate** in 2001 was 61.1 percent (15-64 age group). This is higher than in 2000 (60.7 percent), but the overall level is slightly lower than at the end of the 1990s and much worse than the targets set in Lisbon for the EU countries in 2010 (70 percent) (Diamantopoulou, 2000). The employment rate of women was 57.3 percent exceeding the EU target for 2005 but lagging behind the 2010 target of 60 percent by about 3 percent. The employment rate of men was 65.2 percent in 2001.

**Figure 1. The dynamics of employment and inactivity in Estonia 1993-2001 (1993 = 100)**

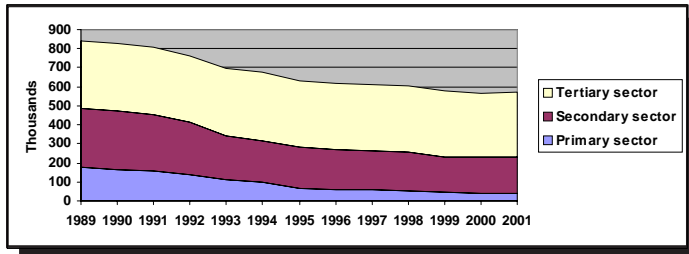


The most rapid decline in employment has occurred in the primary sector. In 2001, only 6.9 percent of the workers were employed in the primary sector compared to 20.4 percent in 1991 (see figure 2). The share of the tertiary sector (i.e. services) is increasing. In 2001, 60.1 percent of all employees worked in the tertiary sector, while in 1991 the figure fell to 43.2 percent. The employment in the secondary sector has declined slightly (33 percent of all employees in

<sup>46</sup> All labour market indicators for Estonia are taken from the Estonian Statistical Office Labour Force Surveys. If some indicator is from another source, it is indicated in the text.

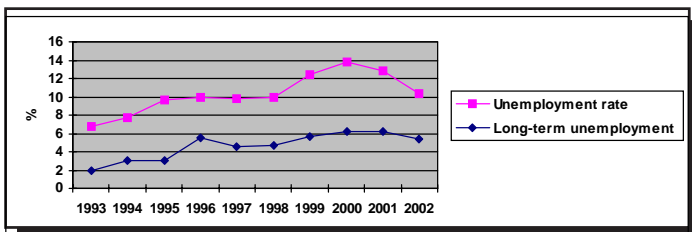
2001 and 43.2 percent in 1991). Rapid decline in primary sector employment has caused many social and economic problems in rural areas, and regional differences in the labor market can be largely attributed to it as well.

**Figure 2. The share of employment in economic sectors in Estonia 1991-2001 (from 1991-1996 the age group 15-69, from 1997 onward the age group 15-74)**



The main problem in the Estonian labor market is the high **unemployment rate**, which in 2002 was 10.3 percent (see Figure 3). The worst year in terms of unemployment was 2000 (when unemployment reached its peak of 13.8 percent), but this trend has reversed in subsequent years. In the last six quarters the unemployment rate decreased and dropped in the 3rd quarter of 2002 to the lowest level since 1995.

**Figure 3. The unemployment rate and the long-term unemployment rate**



The rate of long-term unemployment is almost half that of the total unemployment rate, with the share of long-term unemployment growing (this is partly due to the fact that the overall magnitude of unemployment has decreased). Long-term unemployment is higher among older people and people with less qualifications.

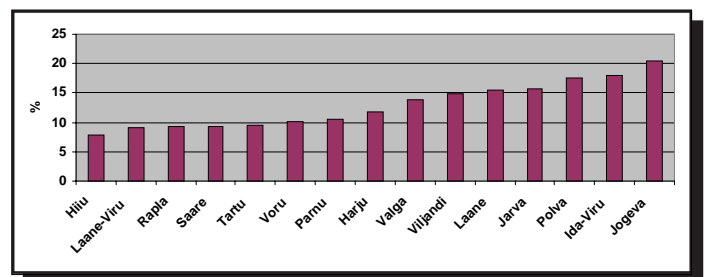
In general, the unemployment level amongst men is higher than that amongst women, contrasting the general trend in the EU countries. At the highest risk of unemployment are young people, especially young women and non-Estonians. Unemployment among the young is 7 percent higher than the overall unemployment rate. The unemployment rate of women aged 15-24 was 22.5 percent in 2002. Here again,

we can see some improvement compared to 2000 when general youth unemployment was at 23.8 percent.

High unemployment rates among non-Estonians (around 6 percent than for Estonians) are attributable to the region in which they predominantly live. Mainly this is the Ida-Viru region, which suffers the highest regional unemployment rate. High unemployment rates amongst non-Estonians are also due to the fact that many of them do not speak Estonian.

In addition to the overall high unemployment rate there are big regional differences in the labor market situation (see Figure 4). The difference between the lowest and highest unemployment rate regions is twofold. Also the income difference between regions is high. It is notable that only the capital region has an average wage higher than that of the Estonian national average.

**Figure 4. The unemployment rate regionally 2001**



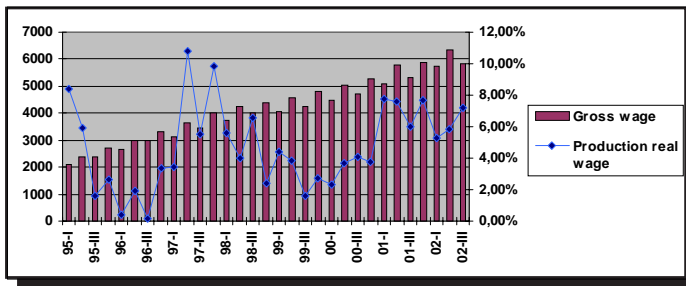
The main reason for a high unemployment rate is the structural nature. The qualifications and skills of the unemployed do not correspond to the labor market's needs. Many of the unemployed are educated below secondary level, making up 15.2 percent of unemployed in the age group 25-64 in 2001 (among the employed it was 8.3 percent). This suggests that Estonia needs an effective training and re-training system, which conforms to labor market needs.

The registered unemployment is half that reflected in labor force surveys unemployment. This is because weak incentives are offered to the unemployed to register. The unemployment allowance has been extremely low and Public Employment Services offer few active labor market measures (see subsection 2.2. for employment policies).

**Wage rates** in Estonia have constantly increased, both in nominal and real terms (see Figure 5). The growth outpaces European average wage growth,

thus in longer term there is expected to be convergence (see Boeri *et al.* 2001a) with the EU wage level.

**Figure 5. Real wage growth and nominal wages (in kroons)**



The wage rates in different economic activities differ significantly. The highest wages are in financial intermediation and in public administration. The lowest wages are in agriculture, hunting, and hotels and catering.

To conclude, the Estonian labor market is characterized by:

- Low and declining labor force participation and low employment rates.
- High unemployment rates, a large share of long-term unemployed among the unemployed, high unemployment of young people and non-Estonians.
- High regional disparities in labor market performance.
- Mismatch of labor demand and supply (structural unemployment).

The main reason for labor market problems has been a rapid structural change, resulting in people's qualification and skills becoming redundant. Therefore there has been an emergence of structural unemployment and regional disparities in labor market performance.

## 2.2. Policies in the Field of Labor Market

### 2.2.1. Active Labor Market Policies

The Employment Service Act specifies seven types of active labor market programs in Estonia:

- Information on the situation in the labor market and the possibilities of employment.

- Employment mediation.
- Vocational training.
- Employment subsidy to start a business (business start-up grant).
- Employment subsidy to employers to employ less competitive unemployed persons (wage subsidy).
- Community placements.
- Vocational guidance (public work).

Community placements have been financed through local budgets since 2001, with no transfers made from the state budget. As no additional resources were allocated at a local level, the interest in organizing placement programs and the number of participants has declined considerably (see Table 2).

**Table 2. Number of participants in active labor market programs (1995-2001)**

Program	1995	1996	1997	1998	1999	2000	2001
Participants in employment training	9,809	9,434	8,241	7,956	7,027	8,150	10,232
Found job after training (%)	52.9	64	75.8	61.9	56.2	57.3	52
Employed with subsidies to employer	121	246	216	136	265	189	356
Received business start-up subsidy	459	456	434	380	433	413	421
Participants in community placement	5,741	4,089	4,661	3,771	3,667	4,177	125
Total number of participants in ALMP-s	16,130	14,228	13,552	12,243	11,366	12,929	11,134

Source: Estonian Labor Market Board

Table 3 shows that total public expenditure on labor market policies measured as a percentage of GDP, has been very low in Estonia, ranging from 0.19 percent to 0.33 percent of GDP. The comparable indicator in the EU countries was 2.6 percent in 2000. The expenditure on active labor market policies in Estonia account for only 0.08 percent of GDP, which is more than ten times less than the amount spent in the EU countries, which have comparable or even lower unemployment rates. In 2001 only 26.8 percent total spending was dedicated to active measures in Estonia.

Out of the active measures **labor market training** is the most important, both in terms of expenditure and in terms of participants. Employment training may take the form of 1) vocational training or 2) more general training aimed at providing information on the labor market situation, and psychological preparation for competing in the labor market. Most of the participants belong to the first group. The local labor offices organize training and the duration of the courses is limited to a maximum of 6 months. In 2001 the average duration of the training course was 25 days. Participants in training receive a retraining allowance equal to 1.5 times unemployment benefit. Actual participation in labor market training decreased steadily between 1995 (9,809 participants) and 1999 (7,000 only). However, since 1999 the number of participants has increased reaching the highest absolute figure since 1995 in 2001 (10,200). Hence, comparing the relative numbers, we see that whereas in 1995 about 28 percent of registered unemployed participated in training, in 2001 the respective number was only 19 percent. This can be explained by the increasing costs of training the participants.

At the same time there is no state-financed system to support adult training (except for the unemployed, civil servants and teachers). This can be considered as a major shortcoming within existing Estonian labor market policy. The skills of the workforce are often obsolete and do not respond to the needs of employers, who cannot find employees with required skills. Supporting in-service training of the workers and providing opportunities for re-training are the key factors in fighting structural unemployment.

The **business-start-up grant** is the second largest measure in terms of public expenditure. However, only a small number of unemployed (between 380 and 460 annually since 1995) have participated in the program. To apply for start-up subsidy the unemployed must be at least 18 years of age and have undergone relevant training or demonstrate "sufficient" experience. The upper ceiling of the subsidy amounts to 10,000 EEK (since the beginning of 1998), which is about 640 Euros only. It must be mentioned that there are also additional business support measures, which are not provided through public employment services but Enterprise Estonia.

Wage subsidy to the employer for recruiting less

competitive persons has been the least important active measure both in terms of expenditure and participants (only between 120 and 350 unemployed annually since 1995). The following persons who are registered as unemployed are considered to be less competitive in the labor market: disabled persons, pregnant women and women who are raising children under six years of age, young people aged 16-24, persons who will be retiring within 5 years and persons who have been released from prison. The level of the wage subsidy is 100 percent of the minimum wage during the first 6 months and 50 percent of the minimum wage during the next 6 months of his/her employment period.

**Table 3. Expenditure on labor market policies in Estonia**

	1993	1994	1995	1996	1997	1998	1999	2000	2001
<b>Expenditure on labor market policies as a % of GDP</b>									
Total on labor market policies	0.19	0.24	0.17	0.17	0.17	0.16	0.34	0.33	0.30
Passive labor market policies	0.17	0.11	0.07	0.07	0.08	0.08	0.26	0.25	0.22
Active labor market policies	0.02	0.13	0.10	0.09	0.09	0.08	0.08	0.08	0.08
Passive labor market policies	88.6	45.8	40.5	44.8	47.3	49.9	75.7	77.0	73.2
<b>Expenditure on active and passive policies as a % of total expenditures</b>									
Active labor market policies	11.4	54.2	59.5	55.2	52.7	50.1	24.3	23.0	26.8
Labor market training	84.3	62.5	55.5	57.9	59.6	55.4	59.3	58.1	63.7
<b>Breakdown of the expenditure on active labor market policies, %</b>									
Community placement	7.8	5.2	2.7	4.6	4.1	3.3	5.2	4.9	0.0
Start-up grants	7.9	4.7	9.1	7.7	7.1	6.4	6.6	6.6	5.3
Subsidy to employer	0.0	0.5	0.9	1.7	1.7	1.9	2.8	3.2	4.1
PES administration	0.0	27.2	31.9	28.2	27.5	33.0	26.1	27.1	26.9

Source: National Labor Market Board, Statistical Office of Estonia

To conclude, the expenditure on labor market policies is very low in Estonia compared to the EU countries, as well as other transition countries in Central and Eastern Europe. This results in low spending on active measures and low participation in active labor market measures. However there are also employment-supporting measures in Estonia carried out through channels other than public employment services. To gain a comprehensive picture on employment policy, these should be taken into account.

There is no evidence to suggest that active measures are effective. In order to develop an appropriate set of active measures the existing policies should be regularly evaluated.

### 2.2.2. *Passive Labor Market Policies*

The main passive labor market policy measure until 2003 in Estonia was a flat rate unemployment assistance benefit, which was launched in 1991 and was financed from the state budget. In January 2002 the Unemployment Insurance Act came into force and the payments out of the Unemployment Insurance Fund started in 2003. The unemployment assistance benefit is now paid only to those who are not eligible for unemployment insurance payments (e.g. students).

#### **Unemployment assistance**

In order to get unemployment assistance the person must be registered as unemployed in the public employment service and have been employed for 6 months during the previous year. Unemployment assistance is paid up to 270 calendar days. The replacement rate of the assistance benefit has been constantly low in Estonia, comprising only 6 percent of the average wage in 2002.

#### **Unemployment Insurance**

The Estonian Unemployment Insurance Fund pays unemployment insurance benefits and administers the unemployment insurance system. The unemployment insurance operates as a compulsory insurance. The rate of the contribution made by the employee is 0.5-2.0 percent of the employee's income and the employer's rate is 0.25-1 percent from the total salary paid out to all employees. The Government establishes the rates for each year. Self-employed persons are not covered by the unemployment insurance scheme.

The right to receive unemployment insurance benefit arises when a person has made contributions for at least 12 months during the previous 24 months. Unemployment insurance benefits are not paid to those who leave their job or service voluntarily or on the initiative of the employer for a breach of duties, loss of confidence or indecent act on the employee's behalf. They are still entitled to unemployment allowance.

The unemployment insurance benefit is paid from 180 days up to 360 days depending on the length of contribution payments. If the period of unemployment insurance benefits is 180 days, a person can apply for unemployment allowance at the end of the period. During the first 100 days of unemployment an insured person is entitled to 50 percent of his/her previous average daily income, afterwards it is 40 percent.

#### **Early retirement**

There is no early retirement system in the framework of labor market policies in Estonia. Although, the State Pension Insurance Act, which came into force in 2000, provides the option of retiring 3 years before statutory retirement age, effective from 2001. If a person chooses the option of early retirement, the pension payments will be reduced by 0.4 percent for each month occurring between the actual date of retirement and statutory retirement date. Since this is a new arrangement no data is available indicating how many people have chosen this opportunity and what the effect has been.

As with the active measures, there is no evidence of the impact of passive measures on work incentives and people income.

## 2.3. Challenges of EU Accession Regarding Labor Market Flexibility

Estonia has completed the accession negotiations with the EU. Estonia is prepared to take over the *acquis* in the field of labor and social policy without exceptions and transition periods. The negotiations concentrated on several issues, which included occupational health and safety, equal opportunities of men and women, public health, promotion of social dialogue, social protection, social security, and labor law. There were several amendments introduced into Estonian legislation and several acts are still in the legislative process (e.g. the law on equal opportunities for men and women). There are also several ongoing projects for introducing and implementing EU principles. For example, there is a project for promoting social dialogue on a sectoral level. The sectoral level social dialogue is the main level in the EU countries and in Estonia it is virtually non-existent.

In general, it is not envisaged that there will be any

obstacles to joining the EU in this area. Since 1999, Estonia has annually prepared National Employment Action Plans, which follow the European Employment Guidelines' principles, objectives and structure. This ensures that Estonian priorities are in line with the EU priorities. However, reaching the EU employment objectives (by 2010 employment rate 70 percent, women employment rate 60 percent and employment rate of older workers 50 percent) is a serious challenge for Estonia.

The precondition of joining the EU is the ability to implement EU policies. In the EU, Estonia will classify as a region for the highest support rate. This will provide an essential increase to the finances available for employment policies. One of the priorities of the National Development Plan, which is the main document for obtaining the funding from the EU Structural Funds, is the development of human resources. The additional funding of 1 billion kroons for the period of 2003-2006 is planned for human resources development. This will raise the annual spending on the active labor market policies by more than double. Such a jump in financing poses the problem of how to effectively use the available finances. Therefore the increase of administrative capacity is one of the priorities, which should be carefully considered. Despite the remarkable increase in financing, it is estimated that the share of ALMPs as a percentage of GDP will remain around 0.18 percent, which is still low compared to the EU average of 1 percent.

Estonia expects to join the EU in 2004. The effect of joining the EU on the labor market is unpredictable. This issue has not been thoroughly researched. Thus, there are several opinions on the future labor market trends, especially concerning the migration flows. On the potential migration movement see Chapter 4. While most of the current EU Member States will not allow free inflow of Estonian workers, they have to allow (with exceptions of Austria and Germany) free movement of services. This might also have an impact on the Estonian labor market by increasing demand for Estonian labor as the wages in Estonia are lower, Estonian companies can offer cheaper services (e.g. construction) and demand for their services will increase.

Another impact of EU accession on the Estonian labor market might come through the inflow of FDI. The essential additional inflow of FDI could increase

job creation and labor demand in Estonia. This would reduce unemployment and even induce the inflow of migration. Besides the main source countries of FDI for Estonia (Sweden and Finland), it is expected that the EU enlargement will create awareness of and confidence in an attractive Estonian economic climate among potential investors from other EU Member States.

Fast or rapid changes in labor market situation, due to the accession to the EU, are not predicted. The Government prognosis does not foresee a jump in employment, unemployment or wages due to joining the EU (see Table 4). If Estonia manages to use efficiently the financial aid available from the EU, it could be expected that the active policy measures help the unemployed to find jobs more easily and there will be a gradual decline in unemployment.

**Table 4. The government prognosis of labor market indicators**

	2002	2003	2004	2005	2006
Growth of employment (%)	1.4	0.2	0.2	0.3	0.3
Unemployment rate (%)	10.3	10.1	10.0	9.8	9.5
Real growth of wages (%)	7.1	6.8	5.3	5.6	5.7
Real growth of GDP (%)	5.6	4.8	5.4	6.0	6.0

Source: Ministry of Financial Affairs 2003

The wage level is expected to converge to the European average wage level, but there is no reason to believe that this should happen faster than the convergence of GDP. According to the research by the European Commission it will take Estonia 19 years to get to the level of 75 percent GDP per capita of the EU average.

No rapid changes are expected due to EU accession. Thus no special policies have been developed. Of course, Estonia adopts the *acquis communautaire* and, therefore some amendments to existing laws and some new legal acts must be adopted. However, the process of adoption of the EU legislation has already begun and is expected to continue smoothly.

**Conclusions:** The Estonian labor market has several problems: low labor force participation and low employment rates, high unemployment rate, a large share of long-term unemployed among the unemployed, high unemployment of young people and high regional disparities in labor market performance.

The causes of these problems are rapid changes in

economic environment, which has caused the destruction of many jobs in agriculture and industry. Adult education, the vocational education system, and active labor market measures are not developed enough to bring people's skills in line with the labor market needs and get the unemployed back to work. In addition, the regional mobility of labor is not enough to reduce labor market differences and bring down unemployment in high-unemployment regions.

EU enlargement will bring to Estonia an essential increase of finance for employment policies. Therefore there has to be a qualitative and quantitative improvement in the implementation of employment policies. The current system could not utilise effectively the extra finances from the EU.

In the context of EU accession no significant changes are expected in general labor market conditions. The EU principles in this field are being adopted gradually in accordance with the NEAP, which has been already prepared since 1999.

## 3. Social Policy

### 3.1. Current State: Factors, Problems and Policies

#### 3.1.1. Social Insurance and Social Assistance

In terms of eligibility, social security and social assistance rights in Estonia are primarily residence-based (for an overview of social benefits and schemes see Tables A.11. and A.12. in the Appendices). Nationality is not a criterion, which means that Estonia's sizeable non-citizen population is also covered. Residence is the only criteria for the receipt of national pensions, family benefits, funeral grants, social benefits for disabled persons and social assistance subsistence benefits, when a contingency occurs, making the coverage of these schemes universal. For old age, work incapacity and survivors' pensions, and unemployment benefits, fulfilment of an additional employment-related qualification period is required, and accordingly, these schemes are designated to cover all economically active persons. The only exception relates to the unemployment insurance scheme, where self-employed persons are excluded from the scope.

Regarding health insurance, individuals are insured firstly on the basis of payment of social tax. However, as a number of large population categories (pensioners, children etc.) are equalised with the insured, the coverage is nearly universal, reaching 94% of the population. Emergency social and medical assistance is available to all persons legally staying in Estonia.

#### The type of benefit

As for cash benefits, flat-rate benefits prevail. National pensions, family benefits, state unemployment allowance, social benefits for disabled persons and funeral grants are all flat rate benefits. Old-age, work-incapacity and survivors' pensions are so far relatively weakly differentiated by former earnings. Sickness and maternity cash benefits and unemployment insurance are currently the only cases of direct earnings-related benefits. However, with recent reforms, the role of earnings-related benefits has increased. From 1999, pension rights are acquired on the bases of social tax paid on earnings. Also, the introduction of the funded pension pillar will emphasise the link between contributions and future pensions. Means-testing is applied only in connection with social assistance subsistence benefits.

The Estonian social protection system includes 3 contributory social security schemes - pension insurance, health insurance and unemployment insurance. The other schemes: family benefits, state unemployment allowances, funeral grants and social benefits for disabled are non-contributory, being financed from general state revenues.

The main financing source for social protection is a social tax – 33 percent of the payroll, which is paid by employers and self-employed persons, and is earmarked to finance pension and health insurance. The direct participation of employees in the financing of social security was introduced only in 2002, and the 1 percent unemployment insurance contribution is currently their only direct share. This is supplemented with the 2 percent contribution for funded second pillar pensions. However, the latter contribution is compulsory only for young persons entering the labor market and optional for all current employees.

**Financing**

Revenues from social tax account form 70 percent of the total social protection expenditure. General state revenues make up about 24 percent and resources of local government the remaining 6 percent of expenditure.



So far, all social security schemes are financed on pay-as-you-go principle. However, all the contributory schemes have developed (or are currently developing) notable cash reserves and/or reserve capitals. As a result of the ongoing pension reform, a fully funded pension scheme was introduced in 2002, which in turn creates a necessity for state subsidies to the first pillar to cover for the partial loss of social tax revenues.

### Administration

Social security schemes are administrated on the national level, either by specialised state agencies (Social Insurance Board, Labor Market Board) or by autonomous public-legal bodies (Health Insurance Fund, Unemployment Insurance Fund). The governing bodies of the public-legal funds include representatives of social partners, but except this supervising function, the role of employers' organisations and trade unions in the social protection administration is relatively modest. The administration of social assistance and social services rests with local municipalities, who may sub-contract the provision of services from NGOs or private bodies.

**In conclusion**, the Estonian social protection system is characterised by the following dominating features (Leppik and Kruuda 2003):

- Universal (or nearly universal) coverage.
- Substantial role of flat-rate benefits (but these provide relatively low replacement rates).
- Relatively few earnings-related benefits (but their role is increasing).
- Public administration of schemes with a relatively modest role for social partners.
- Great reliance on contribution-based financing.

Social protection expenditure in Estonia has accounted for 16-17 percent of GDP. In comparative terms, this places Estonia behind the average level of GDP spending on social protection in the EU, which is about 28 percent. However, it should be kept in mind that at least in the OECD countries the share of social protection expenditure in GDP correlates with the GDP per capita, meaning that more affluent countries spend relatively more on social protection than lower-income countries (see e.g. Scharpf 1997).

### 3.1.2. Social Dialogue

Social partnership is poorly developed in Estonia. This also reflects in the development process and the implementation of employment policies. Social dialogue is better developed on a national level compared to lower levels where it is virtually non-existent. The weak development of social partnership is, partially, a result of poorly developed social partners. This is evident from the institutional and financial shortcomings of social partners' institutions, as well as their low representation.

Social partners in Estonia, as in most other CEE transformation countries, are weakly institutionalised. On the employees' side, trade union membership is around 14 percent of all employees as of the beginning 2002 and membership is declining (almost 100% at the end of the 1980s, 21 percent in 1996). Some industries in Estonia, such as construction and banking, are almost union-free.

There are two national trade union confederations, which are internationally and nationally recognized as social partners: the Association of Estonian Trade Unions (EAKL), and the Estonian Professional Employees' Unions Association (TALO). The EAKL is the largest organization for blue-collar workers, comprising 25 branch unions as of April 2003 and approximately 50,000 members. TALO is recognized as the organization of trade unions of white-collar workers. TALO comprises 11 branch unions, 1 co-operative association and approximately 37,000 members.

There is one federal organization of employers - the Estonian Employers Confederation (ETK). The membership comprises 21 branch associations of employers, 4 associated member associations and 23 commercial undertakings as of 2002. This means that the ETK encompasses 1,442 enterprises with around 45,000 employees (25 percent of all employees). Overall there are 39,794 commercial undertakings (Statistical Office of Estonia).

The regional social dialogue is hindered by the lack of regional organizations. Of the named three organizations only EAKL has regional branches in 5 regions of Estonia. The aim of the regional organizations is the counselling of existing unions and promoting new ones. There is one regional employment pact concluded in the Ida-Viru region, which is aimed at promoting employment and fighting unemployment through measures created in social partnership.

The low level of membership is accompanied by low level of collective bargaining coverage that is roughly equal to trade union membership. This indicates that there is no higher level binding collective bargaining than enterprise level, thus the agreements cannot be extended further and coverage rate is low. The number of valid collective agreements registered in the collective agreements register as of in April 2003, was 102 (Register of Collective Agreements). The total number of agreements is higher because some agreements are not registered, as the register is created only in the last year. The number of agreements in private enterprises is 60, other agreements cover state and municipal entities, such as schools, hospitals etc.

It must be mentioned that there are no other forms of workers representation, such as works councils, present in Estonia. Thus industrial relations are mainly regulated through minimum standards set at state level, partially through social dialogue on a national level, and through individual contracts.

The only level on which social dialogue is held more or less regularly is on a national level. There are contracts concluded almost in every year regarding minimum wage, and some tripartite agreements have also concerned the development of the social security system (e.g. unemployment benefits, subsistence level). It must be mentioned that the range of issues discussed is not wide, but the social dialogue is present and accepted by all social partners as a necessary medium in the labor market. In 2002 a wider context agreement was also concluded on labor market policy development.

At the same time there is the problem that the voice of social partners is only partially taken account on a national level. The Government is still the final decision maker and social dialogue is sometimes just for meeting European demands. At the end of 2002 social dialogue was halted by the trade unions. This was on the grounds that the Government did not fulfil the tripartite contract. Namely, the Government did not increase previously agreed tax-free minimum income and unemployment allowance. Because of this, the trade unions sued the Government and social dialogue will not resume before the case is resolved.

In addition to state level, regular social dialogue social partnership is implemented through regular tripartite bodies. The tripartite bodies are listed in the

Appendices. In general, the tripartite bodies have a consultative role. Participation in various councils and boards undoubtedly increases the importance of partnership and social dialogue in Estonia. It should be mentioned here that public employment services have recently created regional employment councils, which could have a real impact on the future labor market policies on a regional level. At present there is not much information on their effectiveness.

### 3.2. Challenges of EU Accession Regarding Social Policy (Social Insurance, Social Assistance and Social Dialogue)

One of the core areas of binding *acquis communautaire* of the European Union in the field of social protection relates to the co-ordination of social security schemes for migrant workers and members of their family<sup>47</sup>.

The EU's co-ordination rules – Regulations 1408/71 and 574/72 – are based on four key principles:

- **Equal treatment of one's own nationals and nationals of the other Member States**<sup>48, 49</sup>: Intra-Community migrant workers are subject to the same obligations (e.g. with respect to the payment of social contributions) and are entitled to the same benefits as the nationals of that state based on national legislation.
- **Applicability of only one state's legislation for each individual**: This principle protects against both positive and negative conflicts of law, ensuring that persons can't be entitled to the same benefits from 2 countries simultaneously, while guaranteeing that they are always insured somewhere, but do not have to pay social security contributions in more than one state. The main rule here is the principle of **lex loci labouris**, i.e. legislation of the state of employment is applicable.

<sup>47</sup> Social security co-ordination is a mechanism, which links different national social security systems with an aim to secure social protection for persons moving from one country to another.

<sup>48</sup> The regulations apply also to stateless persons and refugees, but currently do not apply to third-country nationals. However, the European Commission has prepared a draft regulation on extending the personal scope of co-ordination also to third country nationals legally residing in any of the Member States. There is a general political agreement in the EU that the draft will be adopted in 2003.

<sup>49</sup> Unless the co-ordination rules are extended to third-country nationals, this may have important implications in relation to the Russian-speaking minority in Estonia. In particular, those Russian-speakers, who have opted for Russian Federation (or Ukraine or other CIS country) citizenship and who number around 100,000 people or 7% of the population, will not have the additional rights arising from co-ordination regulations once Estonia has joined. However, this may also prompt some of these Russian-speakers to give up Russian citizenship and apply for Estonian nationality.

- **Retention of acquired rights:** Persons who have acquired rights for social security benefits in one Member State maintain these rights irrespective of any movement of residence to another Member State. This implies intra-community export of benefits (primarily pensions) for the persons concerned.
- **Aggregation of periods of insurance or residence:** In case the right to benefit is subject to a qualification period or the amount of benefit depends on the period of insurance or residence, periods completed in other Member States are also taken into account. When paying out pensions, a *pro rata* principle is used. Each Member State involved has to pay that share of the total amount, which corresponds to the insurance period completed in that state.

### 3.2.1. The Role of the Association Agreement

In principle, the core legal instrument, which provided for the approximation of legislation and co-operation between the EU and Estonia during the pre-accession period, was the Europe Agreement, which, entering into force in 1995 established an association between the two sides. While the basic objective of the document was 'to provide an appropriate framework for the gradual integration of Estonia into the European Union', it also contained certain provisions on social security. In general, these were presented by the Commission (CEC 1995:72) as a preparatory stage towards implementation of more complex EU social security co-ordination regulations. As a result, the respective provisions of the Europe Agreement were limited to just three questions:

- The export of pensions linked to old age, death, work accident or occupational disease (with the exception of non-contributory benefits).
- The equal treatment of persons with respect to family allowances.
- The aggregation of insurance periods completed in the various Member States for the purpose of pensions and annuities with respect to old age, invalidity and death and for the purpose of medical care for workers and their family members.

These 'partial co-ordination' provisions reflected the EU's general social security co-ordination policy to-

wards third states, which had association or cooperation agreements with the Community<sup>50</sup> (Pizarro 1995). However, the provisions were not fully reciprocal. The first two (export of pensions and granting of family allowances) were symmetrical, while the third was applied only to Estonian nationals. As the Europe Agreement did not establish free movement of workers, there was also no aggregation of insurance periods across the EU border for establishing rights to social security benefits. Only insurance periods completed by Estonians in different Member States could be added up. Furthermore, the application of these provisions is limited to citizens only.

The primary impact of the Europe Agreements' social security provisions on Estonia would arise from the obligation to export pensions, as currently pensions are paid only to persons residing in Estonia. The agreement came into force in 1997. However, even by 2003 the social security provisions had not yet entered into force because of the absence of implementing provisions due to lack of consensus among the current EU Member States. As the matter currently stands, it is likely that the provisions will never be implemented, since from the date of accession in 2004, these will be overruled by the EU Regulations 1408/71 and 574/72.

### 3.2.2. The Future of Bilateral Social Security Agreements

Against the background of failure of the Association Agreement, the main instruments of social security co-ordination in the pre-accession period have been bilateral social security agreements. Estonia has currently 4 bilateral agreements with current Member States or applicant countries of the EU. Agreements with Latvia, Lithuania and Finland (all from 1997) cover all major branches of social security, while an agreement with Sweden (from 1993) covers only medical care for temporary visitors. An agreement with the Netherlands on export of pensions has been recently elaborated and will be signed in 2003.

From the so-called third countries, an agreement with Ukraine is in force from 1997. An agreement with Russia (limited to pensions) was signed in 2002 and an agreement with Canada is currently being negotiated.

<sup>50</sup> For example, the social security clauses in the CEE association agreements and in the earlier Mediterranean Cooperation Agreements were identical. Cremona, M. 'Movement of persons, establishment and services' in Maresceau, M. (ed.) *Enlarging the European Union: Relations Between the EU and Central and Eastern Europe*, London and New York, p. 198.

While the existing agreements with the EU and candidate countries broadly follow the principles of the EU regulations 1408/71 and 574/72, there are nonetheless certain differences.

The bilateral agreements apply to all persons insured under the national legislation, regardless of nationality. Even when the personal scope of the EU Regulations is extended to third-country nationals, there remain some groups (e.g. recipients of national pensions or work incapacity pensions with no prior employment records) who would fall under bilateral agreements, but not under the EU Regulations. This is because the Regulations (as a general rule) apply only to economically active persons and their family members, while existing bilateral agreements apply to all persons who are subject to national social security legislation, including economically non-active persons. There are some differences also in respect of the material scope (types of benefits to be co-ordinated), but most importantly, in respect of the principles of co-ordination.

From the date of accession, the EU Regulations replace the provisions of any bilateral social security agreements, as regards persons and matters covered by the Regulations. However, the agreements remain in force in respect of persons and matters outside the scope of Regulations. Although there is thus no formal obligation to harmonise the existing bilateral agreements with Regulations 1408/71 and 574/72, the differences in principles of co-ordination would cause substantial administrative problems. This is because persons in similar situations could end up with different benefits or could be subject to different procedures depending whether their rights derive from the EU Regulations or from a bilateral agreement.

### *3.2.3. Implications of the EU Social Security Co-ordination Rules*

As the 'migrant worker regulations' deal only with social security co-ordination and not with harmonisation, no formal changes to national legislation were necessarily incumbent on Estonia. Nevertheless, this does not mean that the principle of co-ordination would leave Estonia's social protection system unaffected.

Firstly, the application of co-ordination rules has financial implications. It adds a financial burden to existing

social security schemes, since the regulations give persons moving within the Union new rights. The two largest social protection schemes, i.e. health insurance and pension insurance, will be the most influenced.

The burden arises most notably from the following aspects:

- Export of pensions.
- Extending rights to health care abroad.

With accession, the right to a pension will be extended to the whole territory of the enlarged Union. According to the national legislation, the payment of pensions and other benefits is limited to persons residing in Estonia. Export of benefits is currently possible only under a bilateral social security agreement. From the current EU Member States, Estonia has a relevant bilateral agreement only with Finland. (A relevant agreement has been negotiated also with the Netherlands). From the other applicant countries, Estonia has relevant bilateral agreements with Latvia and Lithuania. The increase of costs for the state pension scheme will still be relatively modest. The Ministry of Social Affairs has estimated that the additional expenditure will not exceed 0.5 percent of the current pension spending, given the relatively small number of Estonian nationals currently residing in the EU Member States and other applicant countries (see Table A9. in the Appendices).

With accession, persons covered by health insurance in Estonia will obtain certain new rights to medical care in the territory of the enlarged Europe. This includes:

- Tourists, other temporary visitors and persons working in international transport (e.g. seamen and lorry drivers) will be entitled to emergency medical care in other Member States at the expense of the Estonian Health Insurance Fund.
- Frontier workers and their members of family will be entitled to medical care both in the country of work and country of residence.

Although in principle, the Regulation 1408/71 prevents medical tourism (travelling abroad to obtain medical treatment) via the requirement of prior authorisation from the competent institution, such authorisation may not be refused where the treatment in question is foreseen under the national legislation, but cannot be given within a reasonable waiting pe-

riod.

Estonian tourists travelling to the EU countries currently have to buy a private travel insurance to cover the risk or potential need for emergency medical care. Under the EU rules this risk will be insured by the public purse, transforming thus from individual to collective responsibility. As higher-income persons tend to travel more often, the obligation to reimburse treatment costs incurred in other EU countries means that higher-income people will absorb in relative terms more resources from the Health Insurance Fund.

In the case of migrant workers from the other Member State, whose dependent family members do not transfer their residence, Estonia would have to refund the medical care (not only emergency, but also regular medical care) delivered in another Member State to those family members.

The burden on health insurance is expected to be more significant as compared to that of pension insurance. In the latter case, exported pensions (or parts thereof) are still paid according to Estonian rates. In the former case, treatment costs will have to be refunded by the Estonian health insurance system on the basis of the actual amounts incurred in EU Member States. Given the predictable flows of tourists (see Table A10 in the Appendices) and existing differences in the prices of medical services between Estonia and the current EU Member States, the additional burden is estimated to amount to 3 percent of the current spending of the Health Insurance Fund on medical services.

It is notable that the effects of reimbursement are disproportionately higher for countries with lower prices of medical services. The Regulations provide a possibility for two or more Member States to conclude so-called 'waiver agreements', whereby the states mutually waive reimbursement of costs of medical services provided to nationals of the other contracting state. The Government could use this possibility and make an effort to conclude waiver agreements at least with some EU Member States in order to ease the administrative burden associated with the implementation of the Regulations.

Although, in theory, the social security co-ordination rules should not discriminate against specific types of schemes, the reality is somewhat different. Some types of schemes are more 'fit' for co-ordination than others. From the state's perspective (and not neces-

sarily from the perspective of concerned individuals), the most problematic are residence-based schemes, which offer universal flat-rate benefits with no qualification period (see also Sakslin 1997). As access to these benefits is relatively easy, co-ordination can increase costs significantly. Finland and Sweden, where universal benefits are widespread, modified some characteristics of their universal schemes before entering the Union. As universal flat-rate benefits have also been the predominant type of cash benefit in Estonia, accession may force a tightening of some of the eligibility criteria.

The regulations implicitly favour schemes designed to protect an economically active population by offering earnings-related benefits, or benefits which relate to either previous earnings, previous insurance contributions, previous periods of insurance coverage or any combination of these factors. In other words, the regulations are built around a typical Bismarckian model of social security. Another favourable option for the states would be targeted means-tested benefits, which escape co-ordination as they are considered social assistance, not social security. Also, in-kind benefits (as opposed to in-cash benefits) are largely non-problematic as they are not exportable.

Solutions to these problems have been suggested (e.g. Pieters 1997), but so far rejected. It is important to recall here that the system of social security co-ordination was developed as a measure of 'market-building', and has been locked into this. Changing the current principles of co-ordination to accommodate better residence-based schemes is regarded by some commentators as a 'spill over' into a 'non-market' area, and has therefore drawn both praise and criticism.

Social security co-ordination rules also have a substantial indirect impact upon future policy-making in the area of social security. They limit the policy options otherwise available. (See also Liebfried and Pierson 1996.) For example, a state may not limit social security benefits only to its nationals. Or, in case there is such a limit, the co-ordination rules would extend these benefits automatically to all nationals (and also stateless persons and refugees) of the Member States. Likewise, a state may not limit the payment of social security benefits to its own territory. Or, again, if this were done, the co-ordination rules would extend the payment of such benefits to

the whole territory of the Union. Nonetheless, it remains the case that such limitations can still be imposed with respect to nationals and territories of third countries.

**Conclusions:** While Estonia's absolute level of social protection expenditure is lower than among the existing EU states, this gap could be linked more to the general differences in wealth, and to a lesser extent to a specific lack of social protection.

Social dialogue is weakly developed in Estonia. At a national level it occurs invariably, but at all other levels it is virtually non-existent. The main reason for a lack of social dialogue is the weakness of social partners, which is evident from a low representation, which in turn causes scarce financial resources. Although social dialogue has existed, it is the Government who has the final decision on the implementation of agreements.

The direct effect of accession upon social protection systems and policies will be rather limited, but there will be important indirect implications. Social security co-ordination extends the rights of Estonian citizens moving across Europe, while also adding a certain degree of financial constraints to its existing schemes of pension and health insurance.

Application of the EU's social security co-ordination rules also requires extending relevant administrative structures both at Ministry level as well as within the implementing bodies. Also, the existing bilateral agreements need revision to avoid extra administrative complications. In this respect, the principles of co-ordination of EU Regulations could be bilaterally extended to all persons who are currently in the personal scope of bilateral agreements. The Government could also make an effort to conclude arrangements on mutual waiving of reimbursement of the costs of medical services with some of the EU Member States, in order to ease administrative burden associated with implementation of the EU Regulations.

## 4. Labor Migration Policy

### 4.1. Push and Pull Factors

Todaro (1969) and Harris and Todaro (1970) related migration decisions to expected earnings adjusted for the probability of employment at destination. Nowadays, migration research identifies a series of push and pull factors that influence labor migration. These factors are often difficult to quantify and they interact in complex ways, rendering any precise forecasting very difficult. In this chapter we discuss different factors that could influence the migration potential of Estonia after the joining European Union.

#### 4.1.1. Demographic Processes and Ageing of the Working Population

In the past few decades Estonia has witnessed some important demographic changes. The population grew at a relatively high rate in the 1970s and 1980s, due to high fertility rates and increasing life expectancy. In the 1990s, the population decreased steadily due to the co-effect of two factors:

- Migration both to the East and West was larger than immigration, which was influenced by the establishment of immigration quota by the state.
- The negative natural increase.

The most important reason of the population change during 1990s has been the decreasing number of arrivals simultaneously with the large number of departures from Estonia. At the beginning of the 1990s there was a remarkable outflow of the Russian speaking population into Russia, Ukraine and Byelorussia. Emigration to Western European countries has been steadily low. The data characterising migration in the 1990s are presented in Table 5, unfortunately the Statistical Office of Estonia does not publish data about migration since 2000. The Immigration Law, which came into force in 1990, and the Law of For-

eigners (1993) played an important role in the decrease of immigrants. By these laws, immigration may not exceed 0.05 percent of the resident population at the beginning of the year.

**Table 5. Estonian migration flows in the 1990s**

Migration flows	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999
Immigration	12,498	8,381	5,203	3,548	2,390	1,575	1,616	1,552	1,585	1,414	1,418
Emigration	12,326	12,403	13,237	37,375	16,169	9,206	9,786	7,235	4,081	2,545	2,034
Net migration	172	-4,022	-8,034	-33,827	-13,779	-7,631	-8,170	-5,683	-2,496	-1,131	-616

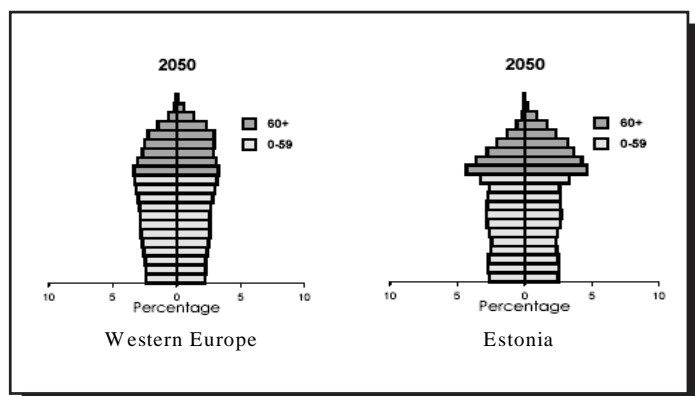
Source: Statistical Office of Estonia

During the last decade, as economic conditions changed, many young families postponed the birth of the first child. Birth rate decreased considerably in the 1990s, but the falling trend has now slowed and some increase is expected in the near future. Adjustment problems and economic instability have also resulted in unstable family relations, with an increasing number of divorces and a falling birth rate. Also the life expectancy of both men and women declined remarkably at the beginning of the 1990s. Since 1996, the life expectancy of women has exceeded the level reached in 1989, showing that the life expectancy of women has become longer during the stable years of independence. The life expectancy levels of men are still some percentage points lower than they were in 1989. Health care statistics reveal that the number of unnatural deaths (alcohol, poisoning, suicides, homicides, traffic accidents) has increased nearly two-fold in the 1990s as compared to the 1980s.

The ageing of the population is a major challenge for the European labor markets. While changes in

the age structure have not had a significant effect so far, they will become more relevant in the decades to come (see Figure 6). The situation of population ageing is particularly worrying in Estonia. If the current population growth trend continues, ageing of the population will be faster than in any of the other countries of the European Union. The age structure of Estonia already causes the need to expand the tax base to avoid a sudden increase in the proportion of dependent people, which could bring about serious social problems.

**Figure 6. Predicted population pyramids in Western-Europe and Estonia in 2050**



Source: World Population Ageing: 1950-2050

Ageing of the population inevitably causes the fast reduction of the working age population, with the number of people 50 years or older continually increasing. This is taking place at a time, when technological changes require constant re-qualification and training, and the younger generation has to spend more time in the educational system. This has two implications: firstly, it introduces the need for lifetime training, which allows the ageing population more opportunities to participate in the labor market, and secondly, it places special needs on Estonian labor, social and migration policies, all of which will require careful attention to secure the necessary future labor supply.

#### 4.1.2. The Labor Market Situation

The differences in the situations of the labor markets of the source and destination countries of migration are generally considered to be important factors for migration decisions. During the last decade there have been some remarkable changes in the Estonian labor market. As described in Subsection 2, em-

ployment has fallen even more rapidly than participation, leading to an increase in unemployment in Estonia. A significant increase in employment in services has been achieved, but it has not yet been sufficient to compensate for the ongoing adjustment and job losses in agriculture and industry. Participation, as well as employment rate in Estonia is below that of the EU and other potential destination countries for Estonian migrants (see Table 6).

**Table 6. Key indicators of the labor market in some EU Member States and Estonia in 2001**

Country	Participation rate	Employment rate (age 15-64)	Employment in primary sector	Employment in secondary sector	Employment in tertiary sector	Unemployment rate	Unemployment rate of youth	Long-term unemployment rate
<b>Estonia</b>	<b>69.9</b>	<b>61.1</b>	<b>7.1</b>	<b>34.2</b>	<b>58.7</b>	<b>12.4</b>	<b>24.5</b>	<b>5.8</b>
<b>EU15</b>	<b>62.2</b>	<b>63.9</b>	<b>4.2</b>	<b>26.4</b>	<b>69.4</b>	<b>7.4</b>	<b>14.9</b>	<b>3.3</b>
Denmark	79.9	76.2	3.3	22.6	74.1	4.3	8.5	0.9
Finland	75.0	68.1	5.8	27.7	66.4	9.1	19.7	2.5
Sweden	75.2	71.7	2.6	23.3	74.1	5.1	11.1	1.2
Germany	71.4	65.8	2.4	28.6	68.9	7.9	9.4	3.9

Source: Employment in Europe 2002.

The Estonian labor market is characterized by a high degree of unemployment, which even increased during the late 1990s. One explanation for this high unemployment, as described in Subsection 2, is mismatch with respect to qualification and region. Unemployment is especially high among young and less educated persons. At the same time, there is also a surplus demand for highly skilled labor, as well as craftsmen and sales personnel.

Comparing the average unemployment rates, we can see that the unemployment rate in Estonia is almost two times higher compared with EU average and it is higher than the unemployment rate in the neighboring EU member countries. Especially big differences are among youth unemployment rates. As migration theory suggests: a high level of unemployment in the country of origin can be a significant push factor of migration. However, as Estonian unemployment is mainly structural (with a large proportion of long term unemployed) and as unemployment is affecting mainly people from different risk groups, this factor is not very influential in determining migration potential, as many will not possess the skills to find a job within other EU countries.



The implementation of structural labor market reforms has paved the way for the recent improvements in the European labor market. Strong employment growth without inflationary pressures suggests that the gains in employment and participation and the decreases in unemployment are sustainable and structural in nature. There is evidence that in the second half of the 1990s, structural unemployment declined overall in the EU and was accompanied by strong employment generation (Employment in Europe 2002). Unfortunately we cannot observe the same tendencies in the Estonian labor market. Due to its smallness and openness, the Estonian economy is influenced by internal and external shocks (for example, financial recession caused by the stock market crash in October 1997 and the crises in the world financial markets; the Russian economic collapse in 1998; etc), also the job destruction process is higher than job creation process and unemployment rate, especially youth unemployment rate, is high. All of these factors increase the migration potential in Estonia.

#### 4.1.3. Income Gap

The wage gap and the speed of approximation of wage levels are key factors of labor migration. As argued by Faini and Venturi (1994), the effect of wages in the region of origin, however, need not be linear. In particular, potential migrants in poor regions (countries) may be unable to bear the cost of migration. As wages rise, emigration from such regions will increase as the liquidity constraint ceases to be binding. On the other hand, rising wages at home reduce incentive for migration. As we can see from Table 7 there exist remarkable differences in wage levels comparing Estonia and the EU countries. Over the time, the differences have diminished and as the wage statistics shows, wage growth has been higher in candidate countries than in the EU Member States. However, the process of convergence is time consuming and is expected to last at least 15-20 years.

While the nominal wages in the EU exceeded that in Estonia many times over, in purchasing power terms, the ratio is more modest (see Table 8). Moreover, the accession countries are reporting higher growth rates, as the positive effects of structural reforms bear fruit, but also because of FDI inflows and financial transfers from the EU (Fridmuc 2001). However, ac-

**Table 7. Wage level in Estonia and some European Union countries in 1995 and 1998**

Country	1995		1998	
	Yearly wage (in USD)	Share from EU15	Hourly wage (in EUR)	Share from EU15
<b>Estonia</b>	<b>2,478</b>	<b>7.1</b>	<b>1.57</b>	<b>14</b>
<b>EU15</b>	<b>34,885</b>	<b>100.0</b>	<b>11.05</b>	<b>100</b>
Denmark	39,079	112.0	17.32	157
Finland	37,992	108.9	11.87	107
Sweden	36,004	103.2	16.00	145
Germany	40,999	117.5	16.71	151

Source: Brücker et al. 2001; Eurostat Yearbook 2002.

According to Boeri and Brücker (2001 a) it will take Estonia around 16-18 years to catch up low income level Member States of the EU.

**Table 8. Income per person in purchasing power parity in 1997-1998**

Country	1997		1998	
	USD	Share EU15	USD	Share EU15
<b>Estonia</b>	<b>5,090</b>	<b>25</b>	<b>5,736</b>	<b>28</b>
<b>EU15</b>	<b>20,710</b>	<b>100</b>	<b>20,176</b>	<b>100</b>
Denmark			23,830	118
Finland			20,270	100
Sweden			19,480	97
Germany			20,810	103

Source: 1997 – Brücker 2001; 1998 – Boeri et al 2001a.

The income difference will remain the main pull factor of migration. According to a survey launched in 2000 by Estonian poll firm SaarPoll, around 90 percent of respondents saw income increase as the main incentive to go to work abroad (Paas *et al.* 2003).

#### 4.1.4. Qualification of the Labor Force and Demand for Services

The average educational level in Estonia is high and comparable with the average level of the EU countries. If recognition of diplomas of the accession countries is agreed on, some increase of highly skilled labor force movement between East and West (both sides) can be predicted and the wages of highly qualified persons will rather quickly create a new wage equilibrium for some occupations in some areas of economic activity.

The subcontracting of services to other businesses is driven by factors of cost (e.g. in construction) or skill (e.g. business services or the IT sector) rather than, for instance, individuals perceiving a wealth gap. A recent example in Europe was Germany, who was looking for IT specialists from East European countries. Another example is the Swedish labor market, where there is a severe shortage of health and social care personnel and it appears likely that this shortage will grow more severe in the future.

At the same time, there has been overproduction of doctors and other health care staff for several years in Estonia and this may be an important push factor for migration. In the Swedish labor market, there is a shortage in the teaching field, in childcare, and also among engineers and IT staff.

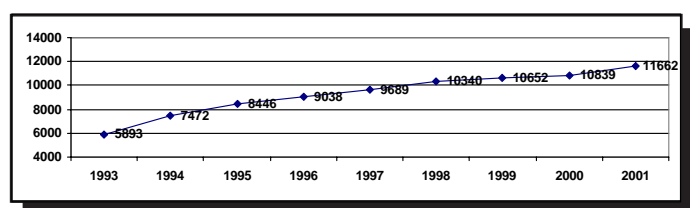
These kind of recruiting activities are an important pulling factor of Estonia's "brain drain". It could also affect the movement of low paid blue-collar workers who could be invited by host countries to seasonal agricultural works.

#### 4.1.5. Proximity

Distance is not a crucial factor for the traditional migrant, but it will be an important factor for those workers, who are looking for temporary work or commuting. A survey by the SaarPoll in 2000 revealed that only 4.0 percent of potential migrants are interested in permanent emigration from Estonia, 7.9 percent of them would choose to work a few years abroad, 17 percent would choose to work a few months and 19.9 percent would prefer commuting, seasonal and casual work. From the destination countries, 33 percent of Estonians would prefer Finland, 19.3 percent would choose Germany and 16 percent Sweden.

As Figure 7 shows, the number of Estonian citizens in Finland has grown constantly. Finland is close to Estonia geographically, culturally, and linguistically, with many Estonians speaking Finnish.

**Figure 7. Number of Estonian citizens in Finland**



Source: Statistics Finland 2001.

According to Eurostat statistics, the highest percentage of Estonians outside of Estonia is in Finland, followed by Germany and Sweden. One reason for that is of course proximity, the second one are the networks and cultural similarities with these countries.

#### 4.1.6. Other Push and Pull Factors

##### Social rights

Alongside the expected higher earnings, higher earnings-related social security benefits in the current EU Member States may contribute to the pull factors, considering the relatively low replacement rates of Estonian benefits (see Table A12 in the Appendices). This is facilitated by the EU social security co-ordination rules, which stipulate coverage of migrant workers with health insurance in the host country and portability of pension rights acquired in the other Member States.

At the same time, social tourism of economically non-active persons is prevented by the relevant EU law. Directive 90/364/EEC on the right of residence has established the existence of an adequate medical insurance and sufficient means of living as pre-conditions for exercising the freedom of movement, in order to avoid becoming a burden on the social assistance system of the host Member State.

##### Tradition and networks

There is empirical evidence that traditions, family, national or ethnic networks are an important factor for migration. However, concentration of Estonian nationals in the EU Member States is insignificant and it is unlikely that they will attract extra inflow of migrants from Estonia. There are some old Estonian communities in existence in Europe (for example, in Sweden), but they consist of mostly elder persons, with the younger generation quite well assimilated with the local communities.

##### Ethnic and political problems

The ethnic and political problems have lesser importance in the determining of migration potential in Estonia. Russians in general tend to migrate more than native people in Estonia. The situation of non-Estonians is somewhat more complicated in the labor market, but the reasons for that are mainly structural changes that took place during the last decade in the Estonian economy. Those who are long-term

unemployed have lower qualifications, they usually do not have language skills, and their ability and desire to move is limited. According to the above-cited survey of SaarPoll, the probability of migration of Russians is twice as high as that of Estonians.

### Cultural and linguistic barriers

It was already explained that the most popular country for Estonians is Finland. If we look at surveys of how many people have done some preliminary investigations about future possibilities to work abroad, then we can see that the number is very small. Only 10 percent have made some preliminary investigations. 64 percent said that they speak only two languages, this is mostly English for the younger generation and Russian for middle age (over 30) and older generation. 73 percent of potential migrants have very poor information about the possibilities of working abroad.

Summarizing the pull and push factors of migration, we can say that the main push factors for Estonians are low income levels and a worse situation in the labor market compared to neighboring EU member countries, especially the high unemployment rate and limited job creation process. The main pull factors are a higher income, a better situation in labor markets and the need for specialist professions (who will easily qualify for work permits). The main factors impairing mobility are the following: language problems, difficulties in assessing foreign qualifications, socio-cultural conditions, availability of accommodation in the destination country, family situation (schooling of children, employment of partner), but also labor and social welfare regulations.

## 4.2. Migration Processes<sup>51</sup>

### 4.2.1. Emigration

The number of Estonian residents in the EU member countries is insignificant, the main reason for which are work and resident's permits - Estonian residents have to apply to immigrate into the EU member countries. According to Eurostat about 16,764 people from Estonia lived in the EU member countries in 2001 (see Table 9). This number is negligible, both in terms of the Estonian population (1 percent in 2001) and even more in terms of the EU Member States population. The highest percentage of Estonians outside

of Estonia is in Finland and the next were Germany and Sweden. According to the statistics from the Estonian Tax Board there were 5,300 people receiving income from abroad in 2001.

**Table 9. Number of Estonian citizens in the EU Member States in January 2001**

Country	Number of people
Finland	10,839
Germany	3,429
Sweden	1,554
Denmark	458
Italy	179
Netherlands	111
Belgium	72
Spain	52
Greece	39
United Kingdom	32
Portugal	1

Source: Council of Europe. Recent Demographic Developments in Europe 2001, UK Department of Social Security

In the negotiation process of joining the EU, Estonia has not requested any transitional arrangements and has agreed to a transitional arrangement with respect to the free movement of workers, put forward by the EU. Restrictions on the movement of workers from Estonia to the EU will apply for a minimum two-year period, as of the date of accession, and may remain in force for a maximum of seven years<sup>52</sup>.

Current Member States will continue to apply national measures as regards the right of Estonian nationals to take up work. In this context, any current Member State may introduce, under national law, greater freedom of movement of workers than at present, including full labor market access. Sweden, Denmark, Netherlands, Ireland and the United Kingdom have announced that they will grant labor market access to the new Member States upon their accession. Current bilateral agreements will continue to apply and may be further developed. The access of Estonian nationals to current Member State labor markets cannot be more restricted than that prevailing at the

<sup>51</sup> This chapter is based on the documents: 2002 Regular Report on Estonia's Progress Towards Accession; Supplement to the Progress Report; NPAA 2002-2003.

<sup>52</sup> Before the end of the second year following Estonia's accession, a review of the functioning of the national measures shall be held on the basis of a report from the Commission to the Council. On completion of the review and no later than at the end of the second year following Estonia's accession, current Member States should notify the Commission on whether they intend to continue applying national measures or whether they intend to apply the *acquis* henceforth. In the absence of such notification, the *acquis* will apply. Five years after Estonia's accession a current Member State maintaining national provisions may, in case of serious disturbances of the labor market or threat thereof, prolong these for a maximum of two years, after notifying the Commission accordingly. In the absence of such notification the *acquis* will apply.

time of the signature of the Accession Treaty. In addition, current Member States will introduce a preference for Estonian national over non-EU labor. The specific case of commuters or frontier workers is also subject to the above arrangements and may be dealt with through national measures during the transitional arrangements.

Any current Member State applying the *acquis* may invoke a safeguard clause until the end of the seventh year following Estonia's accession. As long as safeguard measures can be invoked, Member States may, in urgent and exceptional cases, suspend full application of the *acquis*, followed by a reasoned ex-post notification to the Commission. Member States issuing work permits to Estonian nationals during this period will do so automatically.

Estonian nationals legally residing and employed in a Member State shall enjoy equal treatment to nationals in respect of working conditions, pay, etc, but not regarding access to the labor market of another Member State. In all instances where the *acquis* is suspended during the transitional arrangements, members of the family of a worker already living in a Member State at the time of accession shall have, immediate access to the labor market of that Member State. Estonian migrant workers and their families legally resident and working in another Member State or migrant workers from other Member States and their families legally resident and working in Estonia may not be treated in a more restrictive way than those from a third-country.

#### 4.2.2. Immigration

According to the Estonian law, there exist immigration quotas 0.05 percent of Estonian population per year. Actual immigration is higher because of different exceptions in quotas. The following table illustrates the decisions made by the Citizenship and Migration Board on the issue of different documents and Table 11 describes the distribution of non-permanent habitants by citizenship.

The citizens from EU member countries are not subject to immigration quotas. After joining the EU, Estonia may apply to nationals from a current Member State, national measures equivalent to the measures applied by that Member State with regard to Estonia in the context of the above arrangement on free movement of workers and provision of services. As

**Table 10. Decisions made by the Citizenship and Migration Board on the issue of different documents**

Document	1997	1998	1999	2000	2001
Temporary residence permit	8,237	27,650	11,626	30,653	39
Permanent residence permit	716	12,485	75,031	162,233	66,156
Work permit	6,172	4,495	1,798	2,409	4,791

Source: Citizenship and Migration Board

**Table 11. Distribution of persons with valid residence permits by citizenship**

Citizenship	Persons with non-determined citizenship	Russian	EU nationals	Other states
Share (%)	64	33	1	2

Source: Citizenship and Migration Board

long as a current Member State applies national measures to nationals of a new Member State, Estonia may resort to the safeguard provisions outlined above with regard to the new Member States, with the exception of Cyprus and Malta. Nationals of other Member States legally resident and employed in Estonia shall enjoy treatment equal to Estonian nationals in respect of working conditions, pay, etc.

#### 4.2.3. Measures Regarding the Regulation of Labor Migration

There are several measures undertaken to facilitate free movement of workers. These include, among others, steps towards mutual recognition of diplomas, ensuring residence rights for the EU citizens residing in Estonia, preparations to participate in European Employment Services System (EURES).

Estonia negotiated on recognition of diplomas and qualifications in respect of free movement of workers who completed education during the time when Estonia was part of the Soviet Union (diplomas issued in the Soviet Union) and of persons who began to study a profession listed in the Sectoral Directives (medical doctors, dental practitioners, pharmacists, nurses of general care, midwives, veterinary surgeons) before the harmonization of the Estonian curricula and duration of training with EU requirements.

With respect to professional qualifications obtained before harmonization, Estonia needs to introduce

measures to ensure that all its professionals can, as of accession, meet the requirements laid down by the directives. In the case of the general occupations, the third country qualifications recognized by Estonia will be recognized throughout the EU. In the case of health care and architecture relevant Estonian bodies must confirm the equivalence of the qualifications to Estonia's diplomas. In addition, people with those occupations need to have a certificate to demonstrate that they have been working in the profession recently. The mutual recognition of lawyers' qualification is approached individually for each case, according to the order established in respective Member State.

Estonia is preparing to participate in the EURES system, which will facilitate exchange of information on vacancies in different Member States. The system also enables the procurement of specific information on conditions of social insurance, tax system, working etc.

Concerning the rights of immigrants, Estonia has adopted the laws, which enable the EU citizens residing in Estonia to vote and to stand as candidate in municipal elections. A new Public Service Act enables the citizens of the European Union Member States to be employed in the service as a state or local government official in Estonia<sup>53</sup>.

### 4.3. Challenges of EU Accession Regarding Free Movement of Workers

#### 4.3.1. Migration Potential

Numerous studies have been made on the prospects of labor migration after EU eastward enlargement, when the current regime will be replaced with the right of free movement of labor (see for example Brücker and Boeri, 2000; Sinn *et al* 2001; Walterkirchen and Dietz, 1998; Bauer and Zimmermann, 1999; Hille and Straubhaar, 2000; Werner 1997, 1998; amongst others). Estimates for the long-term migration potential from the CC, based on various research studies, are roughly 1 percent of the EU 15 population. Bertola *et al.* (2001) argue, that future trends in migration from CEE crucially depend on how fast the process of convergence in GDP per

capita levels will occur, and, even more so, on the expectations of residents of the accession countries about the closing of the income gap with the EU.

The outflow of Estonian citizens is not a problem for Estonia at this stage. Looking at the predicted outflows of Estonians, it might bring about some problems in the context of population ageing. Free movement of labor will have rather serious pressure on the Estonian labor market due to possible movement of a better-qualified and flexible labor force. Movers will be mainly the people with good qualifications, also young people with a secondary level education, who do not find a qualified job at home. They are ready to work as blue-collar workers earning salaries, which are relatively higher than they would expect to get in their home country.

At the same time the flows are predicted to be quite low and their impact on the labor market and economy is predicted also to be low (Philips *et al*, 2002; Paas *et al*, 2003). Based on experience of the previous stages of the EU enlargement and the predictions that labor migration will not exceed 0.2 percent of the Estonian population, it is possible to estimate that in the first years of free movement of labor, migration could be about 2,500-2,800 people per year from Estonia (or about 10,000-14,000 during the first four-five years). Over a long-term period (10 years) the labor migration rate will decline (Paas *et al*, 2003). As the predicted migration flows will be quite modest, it will not affect the situation in the Estonian labor market and has little effect on wage levels. However, there will be specific sectors and occupations, which will face greater pressure from migration.

#### 4.3.2. Possible Problems Due to Migration

##### **Migration of high-skilled labor force**

Werner (1997) states that partial imbalances and new opportunities for certain groups of workers may arise and additional, economically motivated migration could occur. Such migration might come about because specialists, managers, technicians and other highly qualified manpower will be in demand in all EU countries and are expected to move across borders more frequently. Increasing qualification requirements, an ageing workforce and lower numbers in the younger population will, in principle, intensify competition within the EU for highly qualified personnel,

<sup>53</sup> To certain positions, which are directly related to the defence of the interests of the county or state, only citizens of the Republic of Estonia will be appointed.

particularly as far as managers and specialist personnel are concerned. As the income gap in these occupations is even larger than average, Estonia may face the "brain drain", leading to an even larger shortage of qualified workforce in the future than it faces today.

### Youth migration

Many younger employees have great interest in the opportunities provided by a larger European labor market. Practice of going abroad at the beginning of their careers, is bringing about a highly qualified, internationally mobile group of people, who are linguistically, technically and culturally flexible and who, with high probability, do not have incentives to return to their home country.

### Commuting in border regions

It is highly probable that cross-border movement in border regions of Estonia will significantly increase after free movement of labor is achieved, especially between regions of North-Estonia and South-Finland. Workers in border areas are particularly fast to react to changes in the neighboring country. In addition, many of the obstacles, which usually play a role in migration across borders, do not apply to these workers or are less important (familiar surroundings, including housing; children can stay in the national school system; the spouse can keep his/her employment; also language problems are relatively minor, because of the proximity of the border). The major incentive to work in the neighboring country is certainly pay. But also other factors, such as taxation, social security or others will play a role in commuting decisions.

The Commission has invited the National Agencies of all countries involved to present cross-border cooperation plans with a view to develop and implement projects and partnerships which will encourage mobility, initiative, intercultural learning and solidarity between young people and other citizens in border regions.

There are several funds available for EU regions bordering candidate countries, in order to finance specific actions to support these regions. Two regions from South-Finland are going to get financial aid from EU funds to deal with cross-border movement. For example, the Finnish YOUTH National Agency has granted a multilateral youth exchange entitled

"COSMO", which involves young people from cross-border regions in Finland, Estonia and Germany. The project aims at preventing social exclusion and increasing the knowledge of Europe amongst young people.

There are also some funds available for candidate countries to deal with cross-border movement. For example, the Special European Investment Bank Program has been developed in response to the lack of adequate small-scale infrastructure identified in the border regions of the candidate countries with the EU. Its overall objective is to contribute to the social and economic development of these border regions and to their integration with their neighboring regions in the current EU Member States. This Program started in 2002, and the funds for Estonia will be available in the near future.

Summarizing the findings about potential migration, Bertola *et al* (2001) conclude, that so far migrants from Eastern countries have been mainly of the high-skill type and they have competed with other foreigners for blue-collar positions in manufacturing or construction and/or low-skilled jobs in the service sector.

**Conclusions:** Different push and pull factors influence the migration from Estonia to current EU Member States. The main factors are a still remarkable income gap, a better situation in the EU Member States' labor markets, and also the need for different specialists (IT specialist, doctors, nurses, midwives, etc) in the EU labor markets. Free movement of labor will put rather serious pressure on the Estonian labor markets due to the possible migration of a better-qualified and flexible labor force. It is predicted that the movers will be mainly people with good qualifications, also young people with a secondary school education, who cannot find qualified jobs at home.

They are ready to work abroad as blue-collar workers, getting relatively higher salaries than they expected to get in their home countries. Migration will put additional pressure on population ageing and even more on financing social protection.

Estonia has not requested any transitional arrangements regarding free movement of workers and Estonia has agreed to a transitional arrangement in respect of the free movement of workers put forward by the EU. Restrictions on the movement of workers

from Estonia to the EU will apply for a minimum two-year period, as of the date of accession, and may remain in force for a maximum of seven years. Estonia is meeting the commitments it has made in the accession negotiations in this field. In order to complete preparations for membership, Estonia's efforts now need to focus on the adoption of outstanding legislation with respect to mutual recognition of diplomas, on bringing curricula and training into line, in particular for nurses and vets, and on further strengthening institutional capacity.

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# APPENDICES

**Table A1. Main macroeconomic indicators**

Indicators	1997	1998	1999	2000	2001	2002
GDP at current prices (millions USD) <sup>1</sup>	4,614.0	5,228.6	5,194.2	5,137.3	5,524.8	-
GDP per head in PPS, % of the EU average <sup>3</sup>	38	39	38	40	42	-
Consumer price index (change over previous year, %)	11.2	8.2	3.3	4.0	5.8	3.6
Current account balance (% of GDP) <sup>2</sup>	-12.1	-9.2	-4.7	-6.0	-6.1	-12.5
Foreign direct investments inflow (% of GDP) <sup>2</sup>	25.7	33.2	49.8	51.0	57.9	-
EEK/USD average annual exchange rate <sup>2</sup>	13.881	14.065	14.695	16.981	17.479	16.6
EEK/USD end of year exchange rate <sup>2</sup>	14.336	13.410	15.561	16.820	17.692	14.936
Gross external debt (millions USD) <sup>1,2</sup>	2,645.818	2,764.856	2,982.838	2,978.494	3,318.657	4,197.843
Gross external debt (% of GDP) <sup>2</sup>	57.3	52.9	57.4	58.0	60.1	-
Domestic government debt (millions USD)	110.27	112.69	121.94	95.36	116.88	-
Domestic government debt (% of GDP)	2.39	2.16	2.35	1.86	2.12	-
Bank of Estonia international reserves at the end of the year (millions USD) <sup>1,2</sup>	784.317	774.668	906.356	914.175	832.776	902.566
TALIBOR <sup>4,2</sup> 3-month interest rates (December %)	15.77%	15.63%	15.42%	12.33%	10.05%	9.57%

<sup>1</sup>Calculation based on annual exchange rate of the Bank of Estonia

<sup>2</sup>Source: Bank of Estonia

<sup>3</sup>Source: Eurostat, *Statistics in focus, Economy and Finance*, Theme 2-59/2002

<sup>4</sup> TALIBOR – Tallinn inter-bank offering rates. Here is presented money market rate as there is no base interest rates presented by Central Bank in Estonia.

- data missing

Source: Statistical Office of Estonia

**Table A2. Socio-demographic data**

Indicators	1997	1998	1999	2000	2001	2002
Population at the beginning of the year	1,405,996	1,393,074	1,379,237	1,372,071	1,366,959	1,361,242
Mean annual population	1,399,535	1,386,156	1,375,654	1,369,515	1,364,101	-
Working-age population (15-64) (annual average thousands)	925.9	919.1	915.6	915.9	916.5	-
Life-expectancy at birth (male and female) (years)	70.44	69.94	70.82	70.69	70.53	-
Life-expectancy at birth (female) (years)	76.0	75.5	76.1	76.0	76.2	-
Life-expectancy at birth (male) (years)	64.7	64.4	65.4	65.1	64.7	-
Disposable income per household member in a year (USD) <sup>1</sup>	1,419	1,630	1,646	1,543	1,571	-
Disposable monetary income per household member in a year (USD) <sup>1</sup>	1,396	1,566	1,576	1,486	1,505	-
Expenditure per household member in a year (USD) <sup>1</sup>	1,437	1,605	1,564	1,579	1,593	-
Expenditure per household member in a year excluding non-monetary consumption (USD) <sup>1</sup>	1,415	1,567	1,520	1,547	1,553	-

<sup>1</sup>Calculation based on annual exchange rate of the Bank of Estonia

- data missing

**Table A3. Structure of household expenditures per household member (% of total expenditure)**

Indicators	1997	1998	1999	2000	2001
Expenditure total	100	100	100	100	100
Food and non-alcoholic beverages	36.97	33.93	32.98	32.06	31.70
..bought food and non-alcoholic beverages	29.87	27.65	27.53	26.80	26.68
..self-produced or received free of charge food and non-alcoholic beverages	7.10	6.27	5.45	5.26	5.02
Alcoholic beverages	1.92	1.90	1.95	2.14	1.92
Tobacco	1.37	1.36	1.59	1.67	1.57
Clothing and footwear	7.10	7.42	7.14	6.77	6.33
Housing	18.75	18.13	17.68	15.30	14.91
Household equipment and operation	5.32	5.10	5.31	5.36	5.58
Health	1.44	1.57	2.02	2.60	2.50
Transport	6.17	6.47	6.18	8.22	8.49
Communication services	2.06	2.72	3.53	4.38	4.82
Recreation, leisure and entertainment	5.90	7.27	7.32	6.34	6.70
..newspapers, magazines and books	1.06	1.13	1.07	0.97	0.91
Education	1.42	1.15	1.00	1.31	1.62
Hotels, cafes, restaurants	2.85	3.42	3.01	3.80	3.48
..eating out	2.82	3.38	2.95	3.68	3.40
Miscellaneous goods and services	5.15	5.45	5.60	6.07	6.19
Non-monetary consumption	1.54	2.34	2.77	2.02	2.50
Consumption expenditure	97.95	98.22	98.09	98.03	98.32
Other expenditure	2.05	1.78	1.91	1.97	1.68

Source: Statistical Office of Estonia

**Table A4. Key labor market indicators (annual average if not indicated otherwise)**

Indicators	1997	1998	1999	2000	2001	2002
Economic activity rate (age group 15-64)	72.3	71.7	70.3	70.4	70.1	69
<b>Employment</b>						
Employment rate (age group 15-64)	65.2	64.5	61.6	60.7	61.1	61.7
Employment in primary sector (%of total employment)	9	9	8	7	7	7
Employment in secondary sector (%of total employment)	33	33	32	33	33	31
Employment in tertiary sector (%of total employment)	58	58	60	59	60	62
Employment in public sector (% of total employment)	31.9	31.1	31.1	28.8	28.7	26.7
Employment in private sector (% of total employment)	68.1	68.9	68.9	71.2	71.3	73.3
Self employed (% of total employment)	0.047	0.047	0.045	0.052	0.048	0.048
Unpaid family workers (% of total employment)	0.008	0.008	0.008	0.007	0.008	0.005
Informal employment <sup>1</sup> (the % of workers in informal employment (in parenthesis average % of wage received informally))	-	-	-	19 (38)	16 (42)	13 (40)
<b>Unemployment</b>						
Unemployment rate	9.6	9.8	12.2	13.6	12.6	10.3
Registered unemployment rate	5.02	4.78	6.71	7.03	8.26	7.46
Youth unemployment rate	14.5	15.8	19.7	23.8	22.2	17.6
Long term unemployment (% of total unemployment)	45.7	47.0	45.8	45.4	48.3	52.8
<b>Employed by educational level</b>						
Below upper secondary education (ISCED 0,1,2)					10.4	-
Upper secondary education (ISCED 3,4)					57.1	-
Tertiary education (ISCED 5,6)					32.5	-
... Postsecondary technical after secondary education (ISCED 5B)					11.8	-
...Higher education, master's and doctor's degree (5A, 6)					20.7	-
<b>Unemployed by educational level</b>						
Below upper secondary education (ISCED 0,1,2)					19.3	-
Upper secondary education (ISCED 3,4)					62.7	-
Tertiary education (ISCED 5,6)					18.0	-
... Postsecondary technical after secondary education (ISCED 5B)					9.5	-
Higher education, master's and doctor's degree (5A, 6)					8.6	-
<b>Labor costs and productivity</b>						
GDP/employed (current prices thousands of USD)	7.48	8.62	8.97	8.97	9.56	-
Average unit labor costs (compensation of employees/GDP)	52.154	50.964	53.781	49.992	49.116	-
Average monthly wage (USD)	257.40	293.28	273.63 <sup>2</sup>	261.47	280.74	-
Change in average monthly gross wages (previous year =100)	119.7	115.4	-	110.4 <sup>3</sup>	110.5	-

<sup>1</sup>Source: Estonian Institute of Economic Research

<sup>2</sup>1998: the recalculated average gross wages and salaries per month are given without health insurance benefits.

<sup>3</sup>Change in the average gross wages (salaries) for 1999 has been presented in comparison with the recalculated data of 1998, which do not include health insurance benefits.

Source: Statistical Office of Estonia

**Table A5. Average monthly gross wages in USD**

Indicators	2000	2001
Average of economic activities	290.4	316.7
Agriculture and hunting	167.0	189.3
Forestry	259.1	290.1
Fishing	210.2	226.2
Mining and quarrying	347.3	393.3
Manufacturing	282.4	295.9
Electricity, gas and water supply	350.1	386.6
Construction	259.1	300.7
Wholesale and retail trade ...	278.5	308.0
Hotels and restaurants	180.7	216.7
Transport, storage and communication	356.6	371.7
Financial intermediation	644.3	704.0
Real estate, renting and business activities	294.7	362.0
Public administration and defence; compulsory social security	372.0	399.9
Education	247.8	274.1
Health and social work	259.6	274.0
Other community, social and personal service activities	247.9	269.9

Source: Statistical Office of Estonia

**Table A6. Expenditures on labor market policies (% of GDP)**

Indicators	1993	1994	1995	1996	1997	1998	1999	2001	2002
Passive labor market policies	0.17	0.11	0.07	0.07	0.08	0.08	0.26	0.25	0.22
Active labor market policies	0.02	0.13	0.10	0.09	0.09	0.08	0.08	0.08	0.08

Source: National Labor Market Board, Statistical Office of Estonia

**Table A7. Replacement rates to average gross wage**

Indicators	1997	1998	1999	2001	2002
Unemployment allowance	0.05	0.07	0.10	0.09	0.08
Old-age pension	0.31	0.28	0.38	-	-

Source: Statistical Office of Estonia

**Table A8. Migration flows and target countries**

Indicators	1997	1998	1999	2001 <sup>1</sup>	2002
Emigration Destination countries	1585 Russia Finland Germany USA	1414 Russia Finland Germany USA	1418 Russia Finland Germany USA	n.a	n.a
Immigration Countries of origin	4081 Ukraine Russia Ukraine Finland Finland Latvia USA	2545 Ukraine Russia Finland Ukraine Latvia Germany	2034 Ukraine Russia Ukraine Finland Latvia Sweden	n.a	n.a

<sup>1</sup> Since 2000 Statistical Office of Estonia does not publish migration data.

Source: Statistical Office of Estonia

**Table A9. Estonian nationals residing in the countries, which are going to apply the EC Council Regulation 1408/71<sup>1</sup> as of 1 January 2001**

Country	Number	Country	Number
Austria	n.a.	Liechtenstein	1
Belgium	72	Lithuania	n.a.
Cyprus	n.a.	Luxembourg	n.a.
Czech Republic	n.a.	Malta	n.a.
Denmark	458	Netherlands	111
Finland	10,839	Norway	301
France	n.a.	Poland	n.a.
Germany	3,429	Portugal	1
Greece	39	Slovak Republic	n.a.
Hungary	33	Slovenia	3
Iceland	25	Spain	52
Ireland	n.a.	Sweden	1,554
Italy	179	Switzerland	90
Latvia	487	United Kingdom	32 <sup>2</sup>
Total		17,706	
of those in countries currently covered by agreements		64	
in countries not yet covered by agreements, %		36	

Sources: Council of Europe, Recent demographic developments in Europe 2001, Strasbourg 2001.

<sup>1</sup> EU Member States, EEA states, Switzerland and EU candidate countries

<sup>2</sup> UK Department of Social Security 1998

**Table A10. Outgoing visitors to European countries, served by Estonian travel agencies and tour operators in 2001**

Country	Number	Country	Number
Austria	4,700	Italy	6,439
Belgium, Netherlands, Luxembourg	5,255	Latvia	14,730
Czech Republic	5,128	Lithuania	6,560
Denmark	4,072	Norway	4,105
Finland	66,462	Poland	1,695
France	8,278	Portugal	1,282
Germany	13,783	Spain	11,654
Greece	4,554	Sweden	23,186
Hungary	2,856	Switzerland	2,506
Ireland	1,402	United Kingdom	21,574
Total		21,0221	
Of those to countries currently covered by agreements	53%	47%	
to countries not yet covered by agreements			

Source: Statistical Office of Estonia

**Table A11.****Social security and social assistance benefits in Estonia**

Scheme and benefits	Persons protected	Type of benefit	Financing
State pension insurance old age pension invalidity pension with flat-rate floor survivors pension with flat-rate floor national pension	economically active economically active social tax economically active social tax residents	partly earnings-related partly earnings-related  partly earnings-related  flat-rate	social tax    general budget
Health insurance medical care  sickness cash benefits maternity cash benefits drug compensations	economically active + certain groups of residents economically active economically active	services earnings-related earnings-related	social tax social tax social tax social tax
Family benefits child benefit child care fee Single parents allowance foster care allowance conscripts child benefit birth grant school grant supplementary benefit for large families (4+)	residents residents residents residents residents residents residents residents residents residents	flat-rate flat-rate flat-rate flat-rate flat-rate flat-rate flat-rate flat-rate flat-rate	general budget general budget general budget general budget general budget general budget general budget general budget general budget
Unemployment insurance unemployment insurance benefit insolvency benefit collective redundancy benefit	economically active economically active  economically active	earnings-related earnings-related  earnings-related	insurance contributions insurance contributions  insurance contributions
Unemployment allowances state unemployment allowance  retraining grant	economically active + certain groups of residents economically active + certain groups of residents	flat-rate  flat-rate	general budget  general budget
Social benefits for disabled disabled child benefit disabled adult benefit carers allowance Disabled parent allowance study allowance Rehabilitation allowance further education allowance	residents residents residents residents residents residents residents residents	flat-rate flat-rate flat-rate flat-rate flat-rate flat-rate flat-rate	general budget general budget general budget general budget general budget general budget general budget
Social assistance subsistence benefit emergency social assistance	residents persons legally present	means-tested services	general budget local budgets
Medical assistance Emergency medical care	persons legally present	services	general budget



Table A12. Levels of social security benefits (as of 01.04.2003)

The type of benefit	EEK	Euro (1)	Net replacement rate
National pension	931	60	18.3 %
Old age pension (average)	1,975	126	38.8 %
Invalidity pension (minimum in case of total invalidity)	1,499	96	29.5 %
Survivors' pension (minimum in case of 3 or more family members)	1,499	96	29.5 %
Sickness cash benefit (⌘)	-	-	80 %
Maternity benefit (⌘)	-	-	100 %
Child benefit (single child)	150	10	3.0 %
Child benefit (second and each following child)	300	19	5.9 %
Birth grant (first child) (*)	3,750	240	73.8 %
Birth grant (second and following child) (*)	3,000	192	59.1 %
Child maintenance fee (up to 1 years)	700	45	13.8 %
Child maintenance fee (2 - 3 years)	600	38	11.8 %
Child maintenance fee (from 3 to 8 years)	300	19	5.9 %
Adoption grant (*)	3,000	192	59.1 %
School grant (*)	450	29	8.9 %
Start-in-life allowance (*)	6,000	383	118.1 %
State unemployment allowance	400	26	7.9 %
Unemployment insurance benefit (during the first 100 days) (⌘)	-	-	50 %
Retraining grant	600	38	11.8 %
Labor market business start-up grant (*)	20,000	1293	393.8 %
Labor market grant to employers	2,160	138	42.5 %
Disabled child benefit (severe or profound disability)	1,020	65	20.1 %
Disabled child benefit (moderate disability)	860	55	16.9 %
Disabled adult benefit (profound disability)	640	41	12.6 %
Disabled adult benefit (severe disability)	420	27	8.3 %
Disabled adult benefit (moderate disability)	200	13	3.9 %
Funeral grant (*)	1,800	115	35.4 %
Minimum guaranteed income benefit (after deduction of normative housing expenses)	500	32	9.8 %
Minimum wage	2,160	138	-
Average gross wage (4 <sup>th</sup> quarter 2002)	6,512	416	-
Average net wage (4 <sup>th</sup> quarter 2002)	5,079	325	-

(1) The exchange rate of the Estonian kroon is pegged to the Euro at the rate of 1 Euro = 15,6466 EEK.

(\*) Lump sum benefits

(⌘) Benefits calculated as a percentage of the former wage

Table A13. Tripartite bodies in Estonia in 2002

The type of social partnership/ tripartite body	Membership	Explanation
<p>National level Tripartite negotiations</p> <p>The coordination of employment and social field draft legal acts</p> <p>Socio-economic Council Advisory body for Government</p> <p>The Board of Estonian Health Insurance Fund Highest governing body of Health Insurance Fund</p> <p>The Board of Unemployment Insurance Fund (the highest governing body of Unemployment Insurance Fund)</p> <p>Estonian ILO Council</p> <p>The Board of the Foundation of Qualification</p> <p>Professional Councils</p> <p>The Board of Foundation of Vocational Education and Training Reform in Estonia</p> <p>Working Environment Council</p>	<p>Delegations based on parity</p> <p>3x6 members</p> <p>5 Government's representatives, 5 employers' representatives, 5 representatives of insured people (incl. 2 trade unions' rep)</p> <p>2 members reports to Government etc.</p> <p>3 trade unions', 3 employers' and 6 Government's representatives</p> <p>2 trade unions' representatives</p> <p>1-2 trade unions' representatives</p> <p>4 Government's representatives, 4 employers' representatives, 2 trade unions' representatives, 3 training institutions</p> <p>3x5 members</p>	<p>Minimum wage Basic exemptions Unemployment benefit Legal acts and their conditions Promotion of social dialogue and partnership</p> <p>Government asks the opinion of employees and employers.</p> <p>Advises Government; has right to include issues into tripartite negotiations Analysis of socio-economic situation and legal acts, promotion of implementation of European social model.</p> <p>Approves the budget; approves the action plans and objectives; reports to Government etc.</p> <p>Approves the budget; approves the action plans and objectives;</p> <p>Carries through qualifications reform.</p> <p>Determines qualification in each council standards.</p> <p>Implementing European projects in VET and employment in Estonia.</p> <p>Advisory body to Government on work health and safety issues.</p>
<p>Various working groups PHARE projects' managing committee</p>		<p>South-Estonia employment North-East Estonia employment Promotion of Social Dialogue on sectoral level Support for labor market services balanced development</p>
<p>Labor Legislation working group The Commission for Evaluating Employment Projects</p>		
<p>SME Council Regional level The Boards of vocational education institutions</p> <p>Labor Dispute Committees</p> <p>Regional Employment Councils</p>	<p>In every county parity membership 5 counties 3 employers' and 3 employees' representatives</p>	<p>Counselling regional public employment services.</p>

Source: Taliga, Kolmepoolsus - institutsioonid ja vormid, 2002

EURO-BALKAN INSTITUTE, REPUBLIC OF MACEDONIA

**EU Enlargement and Its Impact on  
the Social Policy and Labor  
Market of Macedonia**

*Skopje, 2003*



# 1. Macroeconomic Picture and Stage of EU Accession

## 1.1. Macroeconomic Background

After the breakdown of SFR Yugoslavia in 1991, The Republic of Macedonia had entered into a challenging phase of transition toward market economy and democracy. Political efforts for implementation of democracy were more successful than efforts for achievement of economic stability and growth. Indicators in the Table 1 show serious problems in functioning of the Macedonian economy in the last few years, although the problems had existed from before. Due to economic and political reasons they became worse in the last decade. Political instability in the Balkan region causes high level of political and economic risk that had affected Macedonian economy very badly.

Political and economic turbulences on the Balkan region in the last decade were not in favour of Macedonian progress toward EU. The culmination of the events for Macedonia was military conflict within the country in 2001. Seriousness of the situation in the South-east European countries (so called Western Balkans) got a lot of European Union's attention in the last decade, which have resulted in tailor-made Stabilization and Association Process (SAP) for Macedonia, Croatia, Serbia and Montenegro (including Kosovo), Bosnia & Herzegovina and Albania, in regards to EU accession. All these countries are focused to EU accession, but they'll have to achieve stable political environment in the region first, with parallel gradual work on fulfilment on EU requirements (*acquis communautaire*) underlined as compulsory for all accession countries.

## 1.2. Stage of EU Accession

Implementation of SAP includes signing of Stabilization and Association Agreements (SAA) by all afore-

	1997	1998	1999	2000	2001	2002
GDP (in millions USD)	3458	3575	3730	3899	3723	
GDP per capita (PPS) in USD	4305	4483	4724	5018	4482	
Inflation CPI (average)	2.6	-0.1	-0.7	5.8	5.5	1.8
Current Account Balance (as % of GDP)	-7.2	-8.7	-3.0	-3.1	-10.1	
FDI (% of GDP)	0.45	3.29	0.86	4.49	11.89	
Exchange rate-average (DEN/ 1 USD)	42.82	54.45	56.89	65.88	68.04	
Exchange rate-end of the period (DEN/1 USD)	55.4	51.8	60.3	67.63	69.17	62.37
External debt (in millions USD)	1131	1398	1438	1437	1418	1517
External debt (as % of GDP)	30.6	38.5	39.1	40	39.7	
Foreign Currency Reserves (in millions USD)	280	334	478	714	775	733

Source: Ministry of Finance, National Bank of the Republic of Macedonia

mentioned countries with EU, that regulate the main issues regarding the EU association. Macedonia was the first country that signed the Stabilization and Association Agreement, in April 2001, and so far only Croatia has done the same. The other countries from the group are still in the process of negotiations, and SAP doesn't give the expected results so far. SAP differentiates aforementioned countries from the Central and East European countries with status of accession countries to EU. The main difference lays in the status of Western Balkan countries in EU official politics, according to which these countries form

a “third” group on the list for enlargement, with stressed political and economic instability. Free trade agreements with EU go along with the SAA, but free movement of persons (excluding labor force) toward EU is not applied on the “third” group (except Croatia). Considering the progress in the process of European integration of partner countries in the project, Macedonia have to be distinguished as separate case in this project. Process of harmonization of national legislation with EU directives has started in various economic spheres, as well as labor market and social policy.

## 2. Labor Market

### 2.1. Current state: Factors and Problems

#### Demographic trends

The current state on the labor market in Macedonia reflects the economic and political transformation in the country after the breakdown of Former Yugoslavia, although the situation on the Macedonian labor market was unfavorable from before. Demographic trends in Macedonia cannot be distinguished as significant factor for current labor market situation in Macedonia. Changes of the volume and dynamics of total, working-age and active population show that in the period 1981 and 1994, the growth of the total population in the country amounted 7,6 percent, of the working-age population 10,7 percent and of the active population 3,8 percent. Differences are signalling a decrease in the demographic frame of the labor force supply, and decrease of the growth of the active population. Those changes could be explained with the loss of the part of the labor force induced by intensive migratory movements towards abroad, an increase in the number of retired persons because of different reasons, primarily their premature exclusion from the labor contingent during the transition process, as well as by the changes in the professional occupations of part of the active persons (primarily from the agrarian into non-agrarian professions).

Mentioned categories have tendency of continual changes, as shown in table 2 of main socio-demographic data for Macedonia. It could be expected that the unfavorable demographic trends will continue, which can be confirmed by the prognoses on the total and working-age population growth in the Republic of Macedonia in the period until 2020. The projections of the population indicate that after 2010

**Table 2. Socio-demographic data for Macedonia**

	1997	1998	1999	2000	2001	2002
Population (31.12.)*	2002340	2012705	2021578	2031112	2038651	
Population (in mid-year)*	1996869	2007523	2017142	2026350	2034882	
Working-age population (15-64)*	1294505	1305964	1317624	1328752	1339909	
Active population (LFS data)**						
Total	800513	823826	806674	811557	862504	824824
15-64	793375	814835	798819	804048	845885	812650
Crude activity rate (of the total population)	40.0	40.9	39.9	40.0	42.3	
Activity rate of the working-age Population	61.3	62.4	60.6	60.5	63.1	

Note: \* Population estimations

\*\*Labor Force Survey (LFS)

Source: State Statistical Office of the Republic of Macedonia

the average annual growth of the working-age population will have a negative sign. So, the influence of the demographic factor on the labor force formation will be significantly decreased in the future. Those trends are to be taken in mind when planning the economic development and creating the particular policies. However, the current changes in the volume and the structure of the labor force in the medium-term will have unfavourable implications because of the huge growth of the number of the unemployed persons, and limited probabilities of their economic activation. Concerning the demographic trends, it also has to be taken in consideration that life expectancy have continued trend of increase in length (table 3).

**Table 3. Life expectancy in Macedonia**

Life expectancy	1996-1998	1997-1999	1998-2000	1999-2001
Total	72.49	72.49	72.68	73.05
Male	70.37	70.37	70.48	70.68
Female	74.68	74.68	74.77	75.21

Source: State Statistical Office of the Republic of Macedonia

## Employment

Due to transitional problems and various limiting factors (the economic and refugee crises, warlike situations, etc), the employment in the formal sector in Macedonia was encountering an accelerated decrease in the second part of the nineties. In the same time, the informal sector was spreading more intensively and the expansion of the "grey" economy reached huge proportions, but it was tolerated because it served for alleviation of social tensions. Several attempts for estimation of the size of grey economy were made, but results have shown large deviations of the approximated number of employed persons. The administrative data provided by the National Statistical Office (registered employment) do not represent the overall volume of the employed persons in the country (table 4). According to this source, the number of employed persons had decreased from approximately 320.000 in 1997 to 280.000 in 2002.

Solution was sought in the surveys that are carried out starting in 1996. The Labor Force Survey data, which besides formal sector encompasses the informal sector and economically active population in the agriculture, show that between 1997-2002, the number of employed persons amounted between 512 and 561 thousand. In 2002, about 133 thousand active persons in agriculture have been included in the number of employed persons, as well as more than 68 thousand non-paid family workers. Although, the inclusion of the un-paid family workers in the total number of employees doesn't contribute to completely real presentation of labor market situation in Macedonia, LFS data are more reliable and all further indicators regarding the employment are taken from LFS.

**Table 4. Number and structure of employment in Macedonia**

	1997	1998	1999	2000	2001	2002
Registered employment	319453	310213	315792	310213	313558	280989
Total number of employed- LFS	512301	539762	545222	549846	599308	561341
Employee	402372	417966	405991	408698	419843	396680
Employer	17128	19014	43431	23675	38206	38369
Self-employment	66418	57951	39713	57684	55020	57594
Unpaid employees in family business	25101	44831	56087	59789	86239	68698
Employment rate	34.4	35.9	35.9	35.8	38.6	35.8

Source: State Statistical Office of the Republic of Macedonia

The category of unpaid family workers got an importance with the process of privatization in Macedonia, when the ownership structure of the enterprises in Macedonia has changed. Along to that, the share of persons employed in the private sector has tendency of continual increase. In 2002, more than 50 percent of the total employees in Macedonia have worked in the private sector (table 5). Within this process, a change of participation of the self-employed persons (in the total number of employed) had been noticed. So, the value of this indicator is as follows: 13,0 percent (1997); 10,7 percent (1998); 7,3 percent (1999); 10,5 percent (2000); 9,2 percent (2001) and 10,3 percent (2002). But, considering this data, we have to take in consideration the share of unpaid family workers in the total number of employees, which has noticed a significant growth. The percentage is: 4,9 percent; 8,3 percent; 10,3 percent; 10,9 percent 14,4 percent and 12,2 percent, respectively to the aforementioned years.

**Table 5. Employed persons in sectors in Macedonia (%)**

	1999	2000	2001	2002
Private sector	41,6	43,9	50,9	52,4
Other (social, mixed, collective, state, undefined)	58,4	56,1	49,1	47,6

Source: State Statistical Office of the Republic of Macedonia

The educational structure of employed persons (table 6) shows that share of low educated and low skilled labor force is prevailing. Given structure is poor base for reconstruction of the national economy and



economic development of the country. This is not in favour of acceleration of the Macedonian accession to EU. Also, along with the upcoming EU enlargement, the shift of the offshore capital from accession to non-accession countries should be expected. The current trend of movement of capital is toward low-skilled and cheap labor force and labor intensive industries. Macedonian educational level of labor force suits mentioned requirements, so we could expect transfer of part of that capital, as positive effect from EU enlargement.

**Table 6. Educational level of employed as % of total employed in Macedonia**

	1997		1998		1999		2000		2001		2002	
	Number	%	Number	%	Number	%	Number	%	Number	%	Number	%
1. Higher educated, Higher (bachelor, master, Ph.D)	89473	17.5	94022	17.4	97060	17.7	94824	17.2	96141	16.0	102376	18.2
Higher (specialist)	56766	11.1	58525	10.8	59838	10.9	55775	10.1	63120	10.5	71493	12.7
2. Upper secondary	32707	6.4	35497	6.6	37222	6.8	39049	7.1	33021	5.5	30883	5.5
3. Lower secondary, primary and primary unfinished	175981	34.4	189716	35.1	193301	35.5	200676	36.5	216776	36.2	206052	36.7
	238563	46.6	256025	47.5	254860	46.8	254347	46.2	286391	47.7	252913	45.0

Source: State Statistical Office of the Republic of Macedonia

Currently, about 30 percent of the employed work in the industrial sector, and about 20 percent in the agriculture. The industry is mainly labor intensive (that corresponds with the unfavourable educational structure) and agriculture is not compatible with the European standards. The labor force price per hour is about 2,20USD in manufacturing sector, and 2,40USD in services. This is labor price calculated as expenditure for gross wages, while wages are paid in net amount. Based on the existing legislative, the employer is obliged to pay taxes and contributions prescribed by the Law: the contribution for the pension and disability insurance, the contribution for the health insurance, the employment contribution and personal tax. Minimum wage on national level is determined only for public sector, and it is about 87USD (calculated by exchange rates in April 2003). There is no such regulation for other sectors and negative growth of the real salaries could be notified, as shown in table 7.

**Table 7. Salaries in Macedonia**

	1997	1998	1999	2000	2001	2002
Average paid net salary per employee (in denars)	9063	9394	9664	10193	10552	11279
Nominal salaries growth rate	2.8	3.7	2.9	5.5	3.5	9
Real salaries growth rate	0.2	3.8	3.6	-0.3	-1.9	

Source: Annual economic report, Ministry of Finance of the Republic of Macedonia, 1999, 2000, 2001

## Unemployment

Main feature of the current labor market in R. Macedonia is very high rate of unemployment, which was partially inherited from the pre-transitional period. The Republic of Macedonia had entered the transition period with unemployment rate about 20 percent, i.e. more than 150 thousand unemployed persons and with equal number of over employed persons because of the administrative, but unproductive employment done in the previous period. (Elka Dimitrieva, Verica Janeska, 2000). After the breakdown, economic changes had resulted in so called "organizational shock" for the companies, seen as lost of the Yugoslav market with 22 millions consumers. Yugoslav economy was structured with high level of self-sufficiency, and firms were mainly focused on Yugoslav market. Specific standards were developed for this market and its breakdown was estimated as irreversible lost for the companies. Macedonian firms were pressed to focus on domestic market of 2 millions consumers, with reduced purchasing power. Many firms were closed, process of privatization was accompanied with a lot of problems, and many people had lost their jobs.

The rate of unemployment had reached huge dimensions in 1990's. According to the administrative data of the Employment Bureau, the unemployment rate was 44 percent in 1997, and reached 57 percent in 2002 (table 8). This data cannot be considered as real, and more realistic are data from the Labor Force Survey data, according to which, the rate of unemployment was 36 percent in 1997, and decreased to 31,9 percent in 2002. Expert opinion is that unemployment rate is about 30 percent, so all further indicators regarding unemployment are taken from the LFS.

**Table 8. Unemployment rates in Macedonia**

Unemployment rate	1997	1998	1999	2000	2001	2002
Employment Agency*	44.0	47.0	51.3	53.9	54.8	57.1
Labor force survey**	36.0	34.5	32.4	32.2	30.5	31.9

Note: \* Administrative data - persons at the age of 15 up to 59 for women and 64 for men.

\*\* Labor Force Survey data are for the population over 15 years of age.

Source: National (State) Statistical Office of the Republic of Macedonia.

Within the characteristic of unemployment, special attention deserves its structure based on the degree of education. The share of the nonqualified and semi-qualified, as well as of the persons with lower education degree is constantly prevailing (table 9), which is not favourable as potential for economic development.

In addition, very concerning indicator for the unemployment in Macedonia is the unemployment duration. The unemployment duration is manifested with high absolute and relative increase of the number of persons unemployed for a longer time. The Labor Force Survey confirms the longevity of the unemployment. The share of the long-time unemployment (percent of unemployed for 12 months or more of total unemployment) in the observed period (1997-2002) is as following: 83,1 percent (1997); 82,9 percent (1998); 83,8 percent (1999); 83,3 percent (2000); 86,9 percent (2001); 84,5 percent (2002). The problem of long-term unemployment is highly serious be-

**Table 9. Educational level of unemployed in Macedonia, % of total unemployed, LFS, number**

	1997		1998		1999		2000		2001		2002	
	Number	%	Number	%	Number	%	Number	%	Number	%	Number	%
1. Higher educated, Higher (bachelor, master, Ph.D)	21519	7.4	19052	6.7	19036	7.2	20514	7.9	20561	7.9	19537	7.4
Higher (specialist)	13221	4.5	11350	4.0	10857	4.0	12417	4.8	12584	4.8	13515	5.1
2. Upper secondary	8298	2.9	7702	2.7	10857	3.2	8097	3.1	8067	3.1	6022	2.3
3. Lower secondary, primary and primary unfinished	86794	30.1	89915	31.7	90517	34.6	90167	34.5	99023	37.6	92941	35.3
	70352	59.2	175098	61.6	151825	58.1	151030	57.7	143521	54.6	151005	57.4

Source: National (State) Statistical Office of the Republic of Macedonia.

cause the participation of the persons unemployed for 4 years and longer has amounted about 63 percent in 2002.

The causes for the long-lasting unemployment and its terrifying volume should primarily be sought in the insufficient economic development, the stagnating and even contracting economic growth, the discontinued development trends significantly emphasized by the period of transition from one into another socio-economic system. Besides, the employment problem is under the influence of other limiting factors, such as the foreign debt, the problems of structural transformation and structural harmonization, the stabilization etc.

The problem of long-term unemployment exists in all categories of unemployed, without regard to their age. But, there is trend of decrease of the share of the youth unemployed in the total unemployment - from of 35 to 25 percent, for the period 1997-2002. Changes have resulted from the decreased inflow of new working age population in labor force supply and changes in the relative relations due to the increase of the unemployment of the older age groups from the labor pool (because of lost of jobs, bankruptcy of companies, etc.). Even though the percentage of the youth unemployment is decreasing, finding a job remains a serious problem in Macedonia.

**Table 10. Youth unemployment (age group 15-24) in Macedonia**

	1997	1998	1999	2000	2001	2002
Number, LFS	101285	99820	78941	72811	73996	67348
% of total unemployment	35,1	35,2	30,2	27,8	28,1	25,6

Source: National (State) Statistical Office of the Republic of Macedonia.

Long-lasting unemployment represents a huge loss for the nation, not only as a flux of the human capital, but also as a loss of most vital part of the population, on whose generic forces, today and in the future, the development of the country should be based. The example of the Republic of Macedonia is confirming, "the enormous loss of the human resources is a sign of large inefficiency of the economic system and is provoking a deep crisis in the social sphere" (OECD, 1994, p.9). The long-term unemployment is

one of the basic causes of the large poverty increase. According to the latest data, about 25 percent of the total population in the country are poor.

## 2.2. Policies in the Field of Labor Market

During the transition period, the regulation of the labor market in the Republic of Macedonia was set-up on the new basis. The Constitution and the Law on the Labor Relations, which was enacted in 1993, basically regulate the functioning of the labor market. Up until today it is harmonized with the contents of 66 conventions of the International Labor Organization. Except with the mentioned law, other special laws arrange particular issues from the labor area, such as: the Law on the Public Servants, the Law on Protection During the Work Process, and the Law on the Strike. Unfavourable economic situation in the last decade, that induced large changes on the labor market, imposed a need for undertaking the Project for Structural Reforms of the Public Sector and the Labor Market, whose realization begun in 1997 with the financial support of the international institutions.

The aim of those reforms was to improve the labor market flexibility, to increase the demand of new workers, to adapt the availability and duration of the benefits based on the unemployment status, improvement of its payoff, improvement of the organization and technology implementation in the institutions where those benefits are effectuated (Stojan Trajanov, 2002, p.19-22). In this context, two laws were brought: the Law on the Employment and Insurance During the Unemployment Status and the Law on the Social Protection. Legislation is very important for alleviation of the labor market problems, and it contains concept of the main politics regarding labor market, and especially employment.

### 2.2.1. Active Labor Market Policies

Active labor policies are defined within the Macroeconomic policy of the Government, Law on the Employment and Insurance During the Unemployment Status, as well as other programs and projects regarding the labor market. There is strong determination in the Macroeconomic policy of the Government for active approach toward labor market, expressed mostly by operationalization of the Program

for increase of the employment and labor market flexibility. The program contains tasks for improvement of legal frame for employment stimulation, by enacting new or changes of the current legislation. In that purpose, Law for Employment stimulation was enacted in 2003, which contains measures for employers' benefits for employment of certain categories of long-term unemployed persons, through participation into employers' expenditure regarding new employees. Similar Law was already enacted in 1998 and some positive effects were notified.

At the same time, changes for improvement of labor market flexibility have been done on the Law of Labor relations, and Law on the Employment and Insurance During the Unemployment Status. The changes are focused on simplification of the procedures for labor force inflow and outflow from the labor market, financial relieves for the employers, and decrease of the unemployment benefits in order for unemployed to be more stimulated to seek for job.

Active labor market instruments are first of all focused on qualification measures -training and advanced training, retraining, management training, consultancy services and help for start up of small business, etc. Measures aimed at creating employment or preserving jobs, e.g. wage subsidies, employment programs, financial support for business start-ups, and subsidies for the employment of particular groups, were presented in a lesser extent. In that regard, the Project for Development of Small and Medium Enterprises that has begun in 1996 is of great importance. Ministry of Economy of Republic of Macedonia coordinates the project, with participation of few competent institutions. The aim of the project is identification of initiatives, preparation of new projects and their realisation, in order of job creation. As result of this project, certain number of SME's was established, but there is evident need for financial support for start up of new businesses, as precondition for better achievements within this initiative.

Besides aforementioned project, active labor policies also are implemented by realisation of the Project for Social Reforms and technical support, financed by the World Bank. This project has started in 1997 and should end in 2003. Within different programs covered with this project, more then 31.000 unemployed persons got an employment, and more then 11.000 of them, have kept their jobs. Also, employment of 3.300 unemployed people was realised

within the PRISMA Project for local development in R. Macedonia, through promotion of partnership, capacity building and municipality development in the country. Time frame of the Project is September 2000 - September 2003, and it is realized by the Ministry of labor and Social Policy of Macedonia and other competent institutions, with Financial support of USA Ministry for Labor and USAID.

In April 2003, another project focused on employment and labor market flexibility had started. It's in the frame of CARDS Program, with aim to set base for the National Action Plan for Employment. The project should last two years, with possibility for another two years. The National Action Plan for Employment should contain defined active policies and measures for employment, based on four pillar system of EU regarding the employment and organizational promotion, as well as institutional capacity building for implementation of the active labor market policies and measures.

### 2.2.2. Passive Labor Market Policies

Passive labor market policies and measures are mainly defined in the Law on the Employment and Insurance During the Unemployment Status. It have to be stressed that most of the most of the state efforts in the past few years, were focused on pecuniary compensation for the temporarily unemployed persons and insurance in the case of unemployment. With the Law on Employment and Insurance in the Case of Unemployment (1997), the rights on insurance in the case of unemployment are defined, as well as the rights on health insurance for the unemployed persons that do not have health insurance. There also belong the beneficiaries of pecuniary compensation and the right on pension and disability insurance for the beneficiaries of the pecuniary compensation.

The workers that lose their jobs are applying in the Employment Office and in compliance with the mentioned Law, they realize the rights on the pecuniary compensation in the first year in the amount of 50 per cent of the salary that they earned in the last 12 months, and 40 per cent in the second year and latter on. The period of use depends on the probation years and this kind of compensation can be used between 3 and 14 months. As for the workers that have lost their jobs and are at the age of more than

55 and have a probation of more than 15 years, they can use this right until they obtain a new job or until they acquire a retirement rights.

For the persons that are beneficiaries of the pecuniary compensation, the health protection and pension and disability insurance are provided based on the mentioned Law.

The funds for the pecuniary compensation and other expenses for those persons are provided by the Employment Office - from the employment contributions, and from the Budget of the Republic of Macedonia. There is a tendency of growth of the number of beneficiaries of pecuniary compensation as follows:

**Table 11. Number of beneficiaries of unemployment allowance in Macedonia**

	1997	1998	1999	2000	2001	2002
Beneficiaries of unemployment allowance	49,881	40,713	32,362	35,246	41,375	46,772

Source: Employment Bureau of the Republic of Macedonia

Activities in the field of the employment policy and labor market policy were up until now financed by contribution-based funding, tax-based funding i.e. funding from the government budget and other, primarily foreign sources (foreign financial institutions, PHARE-programs, grants etc.). By contribution-based funding via the employment contribution, which is amounting 1,6 percent of the gross salary, around 22 percent of the expenses related to the activities in the area of labor relations are financed. The foreign funds, inflowing by the various sources, are not too large, but having in mind the financial situation of the country, they cannot be neglected. Greatest part of the activities in the field of the employment and labor market policy were financed from the government Budget, which is high burden for the state.

## 2.3. Challenges of EU Accession Regarding Labor Market Flexibility

### Preconditions

The main challenge of Macedonia on its path to EU integration is achievement of political stability and economic growth. The second one is directly linked with the human resource capacities within the country and the rate of their utilization. That presupposes activation of human resource potential, i.e. increase of productivity and competitiveness that will result in increase of living standard in R. Macedonia.

In unfavourable constellation of labor market, Macedonia will face a very difficult task to accomplish balance between the level of employment protection and necessity of labor market flexibility. Thereby, **Macedonia has the following tasks** (Dimitrieva, Janeska, 2000, pp.80-81):

- Adverse situation in the employment distinguishes the need for dynamization of the economic development and creation of jobs. Labor market functioning is almost impossible without increase of the labor force demand.
- Considering the large participation of the informal sector - grey economy, it is necessary to decrease its dimensions, which will result negative influence on the formal sector to be avoid. At the same time, it will lead to decrease of the differences in the number of employed in both sectors.
- Elimination of the institutional inflexibilities of the labor market, highly influenced with the aforementioned tasks.
- Continual investment in the human capital in the country that should be consistent with the needs and development orientation of the country. At the same time, it presumes permanent education compatible with the EU standards.
- Enhancement of the professional mobility of the labor force, as important factor for the labor market flexibility.

Fulfilment of the aforesaid preconditions is very important in the process of association of Macedonia to EU. In that aim, political strategy and measures regarding employment, labor market, legislation, education, etc. are essential.

### Directives

With the Stabilization and Association Agreement, Macedonia undertook the obligation for gradual harmonization of its legislation with the EU directives. Because of the complexity and time consumption of that process, the harmonization goes along with the Program of the Government of the Republic of Macedonia for the Approximation of the National Legislative to the Legislative of the European Union. Within the group of directives that are to be harmonized in priority, in the part concerning the bylaws in the area of labor, harmonization of the following directives is scheduled for the 2003:

- The Directive of the Council 75/117/EEZ - on the principle of equal salaries for men and women.
- The Directive 76/207/EEZ - on the equal accessibility to jobs, education and equal working conditions.
- The Directive 80/391/EEZ, dated 12.06.1989 - on safeguarding the health of the workers.
- The Directive 97/80/EEZ, dated 15.02.1997 - on the obligations in evidence in the case of gender discrimination.
- The Directive 92/58/EEZ - on the measures in improvement of the security and health of the pregnant mothers.

Within undertaken activities, the Directive 80/391/EEZ and the Directive 92/58/EEZ are already accepted and embedded in the Law on the Protection of the Work Place. Implementation of other three Directives (76/207/EEZ, 97/80/EEZ and 75/117/EEZ) in Macedonian legislative is underway. In that aim, the Government of the Republic of Macedonia in March of 2003 accepted the changes and supplements on the Law on Labor Relations, where the supplements in that direction are provided for.

In the Law on Labor Relations a clause is included by which any discrimination of the employers toward persons seeking for job is forbidden. In the same clause, it is defined that the men and women must be provided with equal treatment in the phases of employment, advancement in their career, work insurance, work conditions, working time and in canceling the job agreements. Besides this, the mentioned Law contains another clause by which the employer is obliged to pay the equal salary for the same conditions on the work place.

Besides the aforementioned Directives, in the next phase of the Governmental Program for Approximation, other directives regarding employment are included. They include basic and directions of the strategic aims of employment, as well programs for their realization. All that is based on four pillar system of 19 EU Directives.

**The first pillar** devoted on increase of the employment include few Directives (job creation, prevention of long-term unemployment, replacement of passive with active labor market measures, development of social partnership, life-time learning system, stimulation of occupation schools work, etc.)

**The second pillar** includes few directives linked stimulation of entrepreneurship, third pillar comprises the Directives regarding the enterprises and employees flexibility, and forth pillar includes Directives for equal employment opportunities for gender, compatibility between the professional and family life, inclusion of persons with disability on the labor market, etc.

**The Directives** contain the politics, strategies, measures and objectives of the labor market. The Directives aim is to help the countries in harmonization of the legislation, introduction and implementation of strategy for labor market development, as well shaping of instruments for active labor market measures that will comprise economic and social objectives.

## 3. Social Policy

### 3.1. Current State: Factors and Problems

#### 3.1.1. Social Insurance

The negative economic movements during the transition period, which led to a significant decrease in the number of employed persons, on the one hand, and increase in the number of the unemployed persons, on the other hand, did result in drastic changes in the social security in the country. Social security in Macedonia is provided by organized system of insurance that includes: pension and disability insurance, health insurance and insurance in the case of unemployment. They are partially financed by the contributions paid on the salaries, and partially from the Budget of Macedonia.

The contributions are calculated as a particular percentage of the gross salary, and they are amounting

- 21,2 percent for the pension and disability insurance,
- 9,2 percent for the contribution to the health insurance and
- 1,6 percent for employment.

Health insurance is not subject of interest in this project. Below, we'll comment pension and disability insurance, because insurance in the case of unemployment is already explained as part of the passive labor policies.

#### **Pension and disability insurance**

The pension system in the Republic of Macedonia was not immune to the changes that happened in the country in the last decade. In 1993, the Law on Pension and Disability Insurance was enacted, and came into force in January 1994. Several changes

and supplements have been done afterwards.

Adverse movements in the economy in the last decade had generated: decrease of the number of employed persons, increase of the number of unemployed and increase of the number of retired persons. The number of pension beneficiaries was 158.964 persons in 1990 and grow to 249.421 pension beneficiaries in 2002. Analogous, the ratio between the retired and employed person has changed. In 1990, one retired persons did relate to 3.19 employed persons, in 1996 - 1,53 and in 2002 the ratio was one to 1,12 employed persons. Such circumstances led to the decrease of the revenues and increase of the expenditures of the Pension and Disability Fund and high degree of illiquidity in the pension payoff. For the sake of overcoming such situation several measures in consolidating the Fund were undertaken. Most important among them are: the increase of the contribution rate, the introduction of the excise tax on oil derivatives, the revenues on the security sale, the restriction on the claims on the pension and disability insurance and exception of part of the claims on the pension and disability system as a social claim.

With the undertaken measures, some positive effects concerning the financial consolidation of the Fund were achieved. The influx of new beneficiaries and the amount of pension were decreased, so that the relative expenditure on the pension and disability insurance was also decreased. The regularity of the pension payoff was also improved. But, with these measures only the short-term results can be obtained, having in mind the demographic movements in Macedonia in favor of population aging. There is awareness in Macedonia that long-term results in pension system could be achieved only with its reform. The preparations for reforms were carried out

in collaboration with the World Bank. The framework for a multilayer pension system was prepared and legally established within the changes and supplements of the Law on the Pension and Disability insurance enacted in March of 2002. The changes were focused on the obligatory pension and disability insurance of the employed persons and other persons performing economic activity. Also, the basic of the capital financed pension insurance was defined. The new system of the pension and disability insurance is composed of three pillars:

- **Compulsory pension and disability insurance** based on the generational solidarity (the first pillar). This pillar is organized on the principle of the current financing with defined pensions, which resembles the current system. This kind of insurance will provide the realization of the pension and disability rights in the case of old age, disability and death,
- **Compulsory capital financed pension insurance (second pillar)**. This pillar represents a capital financed system with defined contributions. This insurance is provided for the pension insurance in the case of old-age, i.e. old-age pension will be paid. This kind of insurance is on the principle of collecting the funds by paying the contributions on the personal (private) accounts. The funds will be further invested, and together with the yield will be accumulated on the accounts. After the retirement, the accumulated funds will be paid off by the means of annuities or programmed drawings, and
- **Voluntary capital financed pension insurance (third pillar)**, where all the persons that want to ensure higher amount of material security than with the compulsory insurance, as well as all the citizens that are not encompassed with the compulsory insurance, could be included.

Within the reform of the pension system, the Law on Compulsory Capital Financed Insurance was enacted in May 2002, with which the compulsory capital financed insurance, the establishment and functioning of the pension reforms and the pension funds management societies as part of the system of the pension and disability insurance and establishment and functioning of the Agency for the Supervision of the Capital Financed Pension Insurance are arranged.

Preparation of secondary legislative for the implementation of the new system is underway. The aim of the reforms in this area, i.e. the introduction of the multi-pillar system is safeguarding the liquidity of the Fund and certitude of the rights in the medium and long-term.

The pension insurance rights are: the right on old-age pension; the right on disability pension; the right on the allocation to another work place; the right on adequate employment; the right on retraining and retraining and the right to equate allowances; the right on the family pension; the right on allowance for the physical accident and the right on the pension threshold.

The right on old-age pension is effectuated when the insured persons will reach an age of 64 (for the man) and an age of 62 (for the woman) and at least 15 years of probation, so that the condition for the age of the woman is increased every year by half a year until the woman reaches an age of 62 up until 31.12.2007. It is allowed by the Law that the insured woman that on 1.09.2000 did have a pension probation of over 30 years and the insured man that did have pension probation of over 35 years, to be able to realize the right on old-age pension under the conditions of the former Law, i.e. when the woman will reach 35 years, and the man 40 years of probation, irrespective of age.

The Law defines the highest and the lowest amount of pension. To preserve the real value of the pensions, the possibility to adjust the pensions to the increase of the average salary in the Republic of Macedonia is provided. The funds for the pension insurance and the rights based on this insurance within the first pillar are provided, i.e. are realized in the Pension and Disability Fund of the Republic of Macedonia.

### 3.1.2. Social Assistance

The Law on Social Protection, enacted in 1997, regulates the social protection in the Republic of Macedonia. Before, the annual Programs of the Government of the Republic of Macedonia defined social protection for the Protection of the Socially Vulnerable Population, based on the Bylaws in this area. The right on the social aid was defined according to the revenues of the household. Every household with



smaller revenues than the threshold, defined by the Bylaw, did have a right to a social aid. The portion of the aid was from 25 percent for one-member family up to 50 percent of the average salary in Republic of Macedonia for five (or more) members household.

In 1996, a new Program on the Social Protection was prepared in cooperation with the World Bank. Preparation of the Program was part of the project for reform of the social sector in Macedonia that has started in 1995. Criteria, Levels, Manner and Procedure in Effectuating the Social Aid were defined within the Program for Social protection. The Program was based on the research for the poverty level in the country, carried out on the generally accepted international standards.

The new system of social protection was legally established in 1997, when the Law on Social Protection was enacted. Its aim is to enable the efficient manner in satisfying the social needs of the citizens. It's applicable to all the population in the Republic of Macedonia, and its implementation goes via 30 Centers for Social work and 11 institutions for social protection. Funding is provided by the Budget of the Republic of Macedonia.

The Law on Social Protection is prescribing several kinds of social protection, out of which, the most important are social benefits. The social benefits are encompassing different kinds of social aid: social pecuniary aid, permanent pecuniary aid, pecuniary compensation for the aid and care and other social benefits. Most significant among them is social pecuniary aid.

### **Social pecuniary aid**

Social pecuniary aid has primary role in the system of social protection in Macedonia. It is focused to alleviate the social position of the most socially endangered population, i.e. persons that cannot provide funds for their subsistence and the subsistence of their families' members. Importance of social pecuniary aid is confirmed with huge number of users. Number of households - beneficiaries of social assistance has been increased to a great extent in the last few years. In 1997, about 65.000 households were beneficiaries of social aid, while in 2002, the number was around 81.000 households! Bearers of the right for social aid are most often: unemployed persons, employed persons that do not get salaries in prolonged period of time, the retired persons that get

low pensions, as well as other households without income.

Conditions, criteria, amount and procedure in obtaining the right on social aid are defined in the special Bylaw, as documents that precise certain issues prescribed in the Law for Social Protection. The Government of Macedonia adopted bylaw in 1998.

As said above, the criteria in the Bylaw are prepared in cooperation with the World Bank. They are as follows:

- Unique level of social aid (for the urban and rural areas).
- The amount of social aid depends on the size of the household, i.e. the number of members of the family, as well as revenues.
- Time limitation of the social aid. The aid can be used in full amount only in the first two years of gaining the right; in the third, fourth and fifth year the amount is reduced by 30 percent, and in the sixth year the aid is reduced by further 20 percent.

The time frame is defined so that the beneficiaries will be motivated to seek for job, i.e. it comprises their inclusion in the labor market. The exception from this rule is made only for particular categories of households, prescribed with the Bylaw.

Based on the criteria contained in the mentioned Bylaw, all the citizens of the Republic of Macedonia have the right on the social aid. The basic provision for this right is a material and tenement status of the household. In proving the material status the following revenues of the household are taken into account: the salaries and descendants on the salaries, pensions, child benefits, unemployment benefits, permanent pecuniary aid, the revenues based on the property and property rights, revenues from the agricultural activities, revenues from the economic and professional activities done with the personal work, revenues from the temporary work abroad, alimonies, dividends, savings interests, civil disability aid, bonds based on the savings in hard currency and other revenues. The household, whose members, except the house or apartment where they live, are in a possession of any kind of real estate or registered motor vehicles, cannot obtain the right on social pecuniary aid.

The amount of aid is calculated based on the num-

ber of persons in the household and based on the relative poverty line. In the moment of defining the level of the social pecuniary aid in 1998, the sum for five (and more)-member household amounted 45 per cent of the average monthly salary by the worker in the Republic of Macedonia. In December of 2002, it amounted 36,4 percent of the average monthly salary by the worker in the Republic of Macedonia.

**Table 12. Social assistance beneficiaries in Macedonia**

Year	Number of households - social assistance beneficiaries	Total expenditure in millions denars	Total expenditure in millions USD*
1997	64,486	2,413	43.54
1998	62,712	2,327	44.89
1999	68,087	2,521	41.78
2000	75,277	2,442	37.38
2001	77,309	2,273	32.86
2002	81,026	2,302	39.28

Note: \* Calculated by the exchange rate on 31.12. of National Bank of the Republic of Macedonia

Source: Ministry of labor and social policy of the Republic of Macedonia

In analysing the social pecuniary aid one can notice that it does have a positive influence on the poverty decrease.<sup>54</sup> This is confirmed by the information obtained in the analysis of data of the Survey of the household consumption in 2000, based on which 32.8 percent of the households in the group with lowest income are social aid beneficiaries. If the social aid to poorest group would be exempt, the percentage would amount 42.9. The social aid is participating with 19.1 percent of the total revenues of the households - social aid beneficiaries, whereas within the poorest households this participation is significantly higher and is amounting 32.6 percent.

The structure of households based on the bearers of the right for social aid shows that the largest part (92 percent) of them is unemployed persons. Based on the age, largest part of the bearers are aged between 30-40, or about 37 percent, and at the age less than 30 - about 27 percent. Based on the qualification structure, highest is the percentage of the bearers with low qualification structure (non-qualified, semi-qualified and with basic education) - about 60 percent. Based on the size of the household, about 50 percent are with four and five household members.

The specified data are reflecting the adverse situa-

tion on the labor market, which is alarming the need to undertake the measures by which it would be possible to employ the bearers of the social aid rights. In that context, there are activities undertaken for adoption of the special Law on Employment Stimulation, by which a particular benefits are given to the employers who will employ social aid beneficiaries. According to that Law the employer who will employ the social aid beneficiary, will be reimbursed of the payment of the contributions for the newly employed person within the period of two years.

### 3.1.3. Social Dialogue

Social dialogue in Macedonia had been pursued on bipartite and three-partite level. In the last few years, bipartite dialogue was quite intensive and two general collective accords were signed, first one for the economic sector (between the employees and trade Union) and the second one for the so-called public sector (between Government and the Syndicate). Also, about 30 collective accords for particular sectors of the economy were signed. Within this period, institutional and legal base for three-partite dialogue was set. In that aim, Agreement for the formation of the Economic-Social Council was signed in 1996 that should function as a tripartite body consisting of nine members, representing the Government, the Syndicate and the employers. Each social partner has three representatives in the Council, elected on four years.

The Economic - Social Council is crucial body for the social dialog in Macedonia. It deals with different economic and social issues, highly important for the Macedonian citizens. The Council considers problems with macroeconomic nature, and suggests recommendations and solutions. Especially important are considerations of measures for economic development, labor market problems, social security, employment, job conditions and job protection, health, education, social and children protection, etc. The Council is in charge of peaceful solution of the collective employment disputes, coordination of the work among social partners and development of the mechanism for tripartite cooperation.

The cooperation between the social partners is realized through preparation and implementation of the labor market projects, participation the social partners representatives in the Executive Board in the Employment Bureau, involvement in organization of

<sup>54</sup> Dr. Robert Ackland, Macedonia Technical Assistance for Poverty Monitoring Consultancy, Final Report, March 2002.

seminars regarding social dialogue, on national and international level, etc. In December 2002, the members of the Council have agreed on and signed Social Agreement for the further directions, activities and measures that social partners should focus on in the upcoming period.

In aim for better achievements in the work of the Council, there is continual cooperation with the International Labor Organization, Stability Pact and Council of Europe regarding different issues related to international law regulation, especially related to social dialogue. In the frame of international cooperation, few ILO conventions were ratified, and activities for signing and ratification of the Convention for Social Dialogue and Convention for Social Insurance are undertaken. It is expected that cooperation with international organization will act in favor of promotion of social dialogue in the country and will contribute to solution of the most problematic issues on the labor market. Also, decentralization of the social dialogue is set as tasks within the activities in local self-government, where experiences for other countries, especially EU countries would be helpful.

#### 3.1.4. Policies

Within the policy in the system of social protection, several measures have been undertaken to decrease the poverty in the country. In the frame of the undergoing "SPIL" project of the World Bank, an analyse of the procedures and criteria for certain social benefits, as well as organizational structure of the programs for social protection should be done. Main aim of this project is improvement of administration of the benefits; in order more justified distribution of the social aid to be provided, i.e. toward poorest categories of the Macedonian population.

The activities and measures in the social protection system during 2003 and later on, will be focused and realized within the Macroeconomic policy, the implementation of the National Strategy for Poverty Alleviation and the Program on the Measures in Increasing the Employment and the Labor Market Flexibility.

Besides the specified measures, part of the measures in the area of social protection will also arise from the implementation of the undergoing PHARE project: Development of the Social Sector and the

Employment, Capacity and Institution building and Development of Social Care and Protection, and other projects of the CARDS Program, as well as the projects related to the social sector reforms within the arrangements with the international financial institutions.

### 3.2. Challenges of EU Accession Regarding Social Policy (Social Insurance, Social Assistance and Social Dialogue)

Considering the current stage of Macedonia in EU accession, big changes in Macedonian social situation and social policy shouldn't be expected. There are no specific EU Directives in the sphere of the social system that are defined as priority for harmonization with the Program of the Government of the Republic of Macedonia for the Approximation of the National Legislative to the Legislative of the European Union. But, already mention Directives 75/117/EEZ - on the principle of equal salaries for men and women and 76/207/EEZ - on the equal accessibility to jobs, education and equal working conditions contain regulations for certain social security issues.

There are few bilateral conventions in the area of the social insurance. In the last few years, Macedonia has signed conventions with Austria, Switzerland, Denmark, Slovenia, Croatia, SR Yugoslavia, Bulgaria and Turkey. Conventions with Germany, Holland, Czech Republic and Poland are about to be signed, and negotiations with several other countries are undertaken. Conventions with the aforementioned countries were signed in purpose to arrange the social status of the citizens that live in the other, signing country. Usually, the financial transactions among Social Funds in Macedonia and Social Funds in other countries are asymmetrical, i.e. number of Macedonian citizens that live abroad or have right on pension from another country is far bigger. Issues regarding right of pension and disability insurance, health insurance, insurance in case of unemployment and health protection are regulated with the mentioned Conventions. There are no particular problems in use of signed Conventions and they contribute to better relations between the signing countries.

EU regulation for social insurance serves as base for

new Conventions. EU regulation is respected as part of the efforts and activities for undertaken process for Harmonization of Macedonian legislation with EU laws. Very important part of the process of Harmonization is activities for signing the European Social Agreement of the Council of Europe. As one of the basic legal documents of EU, regarding the socio-economic and labor market issues, European Social Agreement is considered as base for improvement and promotion of Macedonian legislation, having in mind that all the regulations in Agreement are binding.

## 4. Migration Policy

Concerning the international population and labor force mobility, the Republic of Macedonia is distinguished from the accession and non-accession countries by its specificities. International migrations of Macedonia were gradually liberalized and have reached significant intensity in the second half of XX century. They are characterized with the varying volume and dynamic of immigration, and with the continued increase of emigration. Big changes in the intensity and types of this migration were noticed in the period of social and economic transition. Having in mind the huge volume of emigration<sup>55</sup> as well as the large migratory potential, the stress of the analysis is on emigration. Also, brain drain is located as hot issue in Macedonia and within this project, a survey for migration intentions of the students from Electrical Engineering Faculty (ETF) and Mechanical Engineering Faculty (MF) had been carried out.

The analysis of the contemporary international migratory movements showed that, because of the lack of comprehensive data from the domestic and foreign sources, it is very difficult to determine the amount and dynamics of the immigration and emigration.

### 4.1. Push and Pull Factors

#### 4.1.1. Demographic Processes

Concerning the demographic processes we can conclude that, for the country as a whole, they are not significant push factor for the emigration movements. In the last two decades the natural population increase noticed continuous decrease, which was particularly emphasized during the transition period.

<sup>55</sup> The quantification of the total number of citizens that left the country since 1945 up until now, made on all available administrative and statistical data sources, show that it is between 525 and 540 thousand persons. The approximation of the total number of the Macedonian citizens that currently live abroad showed that it is very large, amounting between 320 and 350 thousand persons (Verica Janeska, 2001, pp. 172-178). Today it represents between 16,1% and 17,6% of the total population present in the country.

The low birth rates, i.e. fertility rates since 1994, do not provide simple population reproduction, meaning generation reproduction of the total population. The analysis show that in the last decade the development of population does not have evolutionary and normal trend, but it was under influence of many external factors (social and economic transition, emigration, wars in former Yugoslav Republics, economic sanctions, military conflicts in Macedonia) (Elka Dimitrieva, 2002, pp. 37).

In the national framework, the population development by regions is characterized by different level of bioreproduction of the population. So, the rise in the number of migrants in part of the areas with high natality from the western part of the country, among the other things, is under the influence of increased population concentration, especially the agricultural population.

The population projections up to 2020, for Republic of Macedonia as a whole, show that the demographic processes will not be significant push factor for the labor force emigration in the future, because of the expected decrease of the average annual growth of the working-age population.

**Table 13. Average annual growth of the working age in Republic of Macedonia, 1994/96 (medium projection variant)**

Period	Without migrations	With constant migrations	With reduced migrations
1994/96-2000	12.706	5.747	7.566
2001-2005	10.962	4.346	5.155
2006-2010	7.284	273	1.954
2011-2015	1.926	-5.688	-2.664
2016-2020	-1.068	-8.969	-4.469

Source: Statistical Office of the Republic of Macedonia, Population Projections of the Republic of Macedonia until 2020, by Age and Sex, 1998

The accomplishment of the projection variant without migrations is impossible in the current circumstances. The really accomplishing one would be a third version, but with presupposition that the corresponding measures and activities would be undertaken. On the contrary, the Republic of Macedonia will face minimal growth in the near future, and latter on high negative growth of working-age population.

#### *4.1.2. Labor Market Situation*

As elaborated in the part for labor market, the main problem in Macedonia is very high rate of unemployment. In the nineties, the transition lead to significant employment decrease and enormous rise in the unemployment rate, which, based on all the estimates, is higher than 30,0 percent. This is one of the significant reasons for intensifying emigration from the country in the last decade. Huge supply of the labor force on the labor market, on one hand and low demand of the other, is determined by lack of job creation and low flexibility of the labor market. All this is affected by deep economic crises in the country and low investment rate influenced by high political risk of the region in the past few years.

High unemployment rate of the highly educated persons is contributing the most for emigration decision of this category of citizens. Besides the unemployment, the important factor which is influencing the decision of employed highly educated persons and young specialists to leave the country is seriously disrupted system of values in the last decade - lack of respect to the work, workmanship underrate, limited possibilities of professional promotion, lack of responsibility which is accompanied with highly developed system of privileges etc.

Long-term unemployment is one of the main reasons for emphasizing of the unfavourable situation of the labor market that had enormous influence on the living standard, and poverty increase in the past decade. As mention before, about 25 percent of the total population in Macedonia are under poverty line.

#### *4.1.3. Income Gap*

As result of the long-lasting economic crises in Macedonia, reduction of the dynamics of the economic growth and numerous social disruptions had happened. The development stagnation, and deep

social and economic crisis were inherited from the 1980's, and were accentuated in the transition period. All this lead to continuous deepening of the income gap between developed countries and Macedonia.

One of the indicators for identifying income gap is the difference in hourly labor price in developed countries and Macedonia. For example, the labor price of unskilled labor force in manufacturing is: 31,88USD in Germany, 29,28USD in Switzerland, 24,18USD in Nederland, and 16,48USD in Italy (World Bank Investment Report, 2001, pp.45), while in Macedonia, the labor price of unskilled labor force in manufacturing is 2,21USD. Normally, big income differences are strong stimulants for the emigration from Macedonia, considering the determinant influence of the incomes on the living standard.

#### *4.1.4. Qualification of the Labor Force and Demand for Services*

The educational structure of labor force in Macedonia, where low educated persons prevail is not vital push factor for emigration. The number of emigrants, as well as their educational structure is determined mostly by the development and immigration policies of the receiving countries. Having in mind the increased selectivity in the receiving countries, it is easier for the highly educated persons to emigrate from the country, although their share in the total available labor force is not high. Regarding that, emigration from Macedonia couldn't produce notable pressure on the labor market in the receiving countries.

Also, emigration is determined by the restricted movement of macedonian citizens, because of the rigid visa regimes. Free movement of persons within the EU is not applied on Macedonia, in spite of the treatment of other accession countries. That could be treated as a factor of difficulty for the Macedonians to establish contacts for work, as well to follow the demand for labor force in EU countries.

As for the demand of services, there is Convention between Macedonia and Germany for temporary employment of construction workers. Also, there are few other initiatives for signing of similar Conventions with Greece, Italy and Slovenia that are determined by the need of labor force in specific sectors in these countries.

#### 4.1.5. Proximity

A specific characteristic of the emigration from the Republic of Macedonia is the traditionally large share of the overseas countries. The census data are showing the migrants' main destinations, even though they do not show their real amount. Namely, the total number of Macedonian citizens in the European countries could be estimated at around 170.000 persons, and in the overseas countries at between 150.000 and 180.000 persons. We can conclude that so far, geographical distance and transport costs were not significant push factor for emigration. This conclusion is also valid for the receiving EU countries, having in mind that macedonian citizens have emigrated more in Germany, then in Greece or Italy - geographically closer to Macedonia.

#### 4.1.6. Traditions and Networks

The tradition, the formation of numerous Macedonian communities and the established migratory links represent important, if not crucial determinant of the contemporary emigration from the traditionally emigration areas and, after 1981, from the municipalities in the western part of the country.

The economic emigration started in the first half of the sixties with the temporary employment abroad and permanent emigrations in the overseas countries. The greatest part of the migrants were from the traditionally emigration municipalities, the areas from which the migratory movements toward abroad last from the beginning of the century.

In the last decade a relatively large number of persons with lower education level succeeded to find an employment abroad, primarily in the receiving European countries (Germany, Switzerland, Italy). It is mostly a result of the established migratory networks, by the employment in the preceding decades, mediated by the employment bureaus. The significant increase of the number of the Macedonian emigrants in these countries since 1996, is result of the changes in the Bylaws of these countries that have enabled reception of the family members of the migrant workers.

The influence of the tradition and migration networks is confirmed and by applying the method of multiple straight-line regression and correlation<sup>56</sup>, used for

research of the emigration and socio-economic development of Macedonia. The results of the sample from thirty municipalities in the country in 1971, as well as for the sample from the twelve municipalities with high emigration intensity in 1971 and 1981, showed that the selected independent variables represent the significant determinant of those movements. Based on the analysis of 1981 for the first sample and of 1994 for both samples, the majority or none of the selected variables in the model did not have statistical significance. So, we can conclude that the emigration rise in the last decade is under the influence of some other factors - tradition, migration links, disrupted system of values, etc.

#### 4.1.7. Ethnic and Political Problems

The volume and intensity of the migratory movements of Macedonia were also determined by the political turmoil in the region and in the country, in the last decade. Because of the wars on the territory of Former Yugoslavia, Macedonia had face with two refugee crises that induced increase of the immigration. Significant part of the refugees remained in the country, and they are burden for the state, having in mind the economic crises and high unemployment of Macedonian citizens.

The political events and political instability in the country, as well as war conflict in 2001 had big influence of the Macedonian citizens to leave the country permanently or temporary. In the 1990's, there is an increase of the permanent emigration of big number of families in the overseas countries. At the same time, the political instability was reason for many workers migrants that were living alone in receiving European countries, to pull their families in those countries.

#### 4.1.8. Cultural and Linguistic Barriers

The cultural and linguistic barriers could not be estimated as important factor for emigration. Macedonian language belongs to the group of the Slavic languages, but Slavic countries had never been attractive destination for Macedonian citizens. Macedonians have been and still are focused to emigration in the developed European, as well overseas countries. Also, the young student population, where the specific brain-drain migration potential could be located, has high level of knowledge of English language. Anyhow, the attraction of the desti-

<sup>56</sup> The correlation between the emigration and Gross Domestic Product per capita, the unemployment rate, the crude rate of natural population increase, the agrarian population, the realized investments per capita and the share of employed in the total population was analyzed (Verica Janeska, 2001, pp. 253-261).

nations for migration is determined by the estimations of possibilities for employment of potential migrants and migration policies of the receiving countries.

Regarding the immigration movements, language and culture could be considered as factor for immigration, especially in the period up to 1980, when the most intensive immigration in Macedonia was notified from Kosovo. The immigrants were mostly Albanians that have settled in the North-western part of the country, where most of the Albanians in Macedonia live, that mean population with the same language and culture. Also, when the Kosovo refugee crisis was over, the refugees that remain in the country, stayed in the areas where Albanians live.

## 4.2. Migration Processes

### 4.2.1. Emigration

The changes in the size and the character of the emigration, in second half of the XX century, are corresponding to the phases of the social and economic development of the country and the changes of the migration policies of the receiving countries. The time frame since the gain of the independence of the Republic of Macedonia up until now is observed as a separate period, when the largest emigration wave since the start of the economic emigration was encountered.

More than 100.000 persons emigrated during the 1990's. According to the Census data the number of migrants in 1994 reach an amount of 173.611 persons. About 50.000 of them left the country between 1989 and 1994. The emigration continued in the second half of nineties with the same intensity. The available data of the Council of Europe on the number of Macedonian citizens in particular European countries confirms those tendencies.

The changes in the structure of migrant workers based on the education are corresponding to selectivity criteria of the receiving countries. The number of highly educated labor force that left the Republic of Macedonia is at least twice as much as the registered one (about 11.000 persons according to the 1994 Census data). Those are highly educated and skilled persons of the different specialties, especially those of the technological and natural sciences. Part of them having in mind their profile (engineers, infor-

mation and technology specialists, etc.), is more easily included in the labor market in the receiving countries and find suitable employment. But, besides the knowledge and qualifications, because of the fact that their diplomas are not recognized in the receiving countries, very frequently their work is valued less. Large number of them, because of the same reasons, are forced to accept lower qualification assignments, even though, based on their qualities, they do not lag behind the specialists of the domicile countries (it is especially true for the doctors of medicine, dentists, etc.)

**Table 14. Macedonian citizens in particular countries**

Country	1996	1997	1998	1999	2000
Belgium				826	
Denmark					1415
Finland		53	80	116	131
Germany	33984	38774	42550	46167	49420
Island			3	6	10
Italy		11596	13456	16647	
Liechtenstein		71	71	77	
Nederland		449	482	507	500
Norway		113	140	178	207
Portugal		1	1	1	4
Romania					1
Slovenia		2200	2412	2277	3565
Spain		19	33	36	58
Sweden		1303	1594	1676	1819
Switzerland		45234	48604	51142	54042

Source: Recent Demographic Development in Europe, Council of Europe Publishing, 2000, 2001

The Republic of Macedonia does not have relevant information about the number of scientist that left the country. Based on the cognition on the flux of young highly educated persons and scientists from some faculties, and especially the intentions of larger part of young high specialists in the technical and technology sector to emigrate, one can conclude that the issue of "brain drain" in our circumstances should be treated as a highly concerning.

Today, the Republic of Macedonia is characterized by a very large migratory potential. The numbers of Macedonian citizens that temporarily or permanently leave the country is continually increased and reach panic dimensions. The potential migration consist of the unemployed persons, primarily with the University diplomas, younger highly educated persons and employed specialists that are not satisfied with their status in the country, part of the young scientists on some faculties, the final year students on the faculties of the natural and technology discipline. The spe-



cial groups of potential migrants are persons educated abroad.

### Brain-drain

The results of the survey on the migratory intentions of the students in final year of their education, on the faculties of the technology disciplines, undertaken within this project, confirm previous conclusion. The survey questionnaire consists of three groups of questions: personal data, migratory intentions and undertaken activities for realization of the migratory plans. The survey sample consists of 117 students from Electrical Engineering Faculty (ETF) and 76 students from Mechanical Engineering Faculty (MF). These Faculties have been chosen because they produce cadres that could relatively easily find an employment abroad. Similar survey, on the same faculties was done by Macedonian Academy of Sciences and Art in 1994, but with smaller sample - 59 (ETF) and 25 students (MF). Anyhow, the results from our survey shown that migration intentions of the students from mentioned faculties are even more emphasized.

On the question **“do you plan/think to leave the country”**, the results are as follows:

- In 1994, about three quarters of the students of ETF (76 percent) and MF (77 percent) were thinking or planning to leave the country.
- In 2003, this indicator is even higher, about 88 percent of the students of ETF and MF are thinking or planning to leave the country.

In spite of the high percentage (88 percent) of students with intentions to leave the country, relatively small number of them, have intention to leave the country permanently - 12,8 percent (ETF) and 13,2 percent (MF). Most of the students from MF are planning or thinking to leave the country for temporary employment abroad - 35,5 percent, while for the students from ETF, this indicator is even higher 39,3 percent. Very high number of the students from ETF are planning or thinking to leave the country because of the bigger opportunities for professional promotion - 43,6 percent, while this indicator for MF is 26,5 percent. Also, the share of the students from both Faculties, considering continuation of the education (on master or doctoral studies) abroad - 8,5 percent (ETF) and 5,3 percent (MF) is worth mentioning.

On the question **“in which country you would like to emigrate”**, about two thirds of the students

from ETF questioned in the survey, have pointed EU, as destination for their emigration. The most attractive countries are Germany, United Kingdom, Greece, France, Italy. Germany is focus country for about one third of the students from MF, and for the other third, some other EU country is indicated as favourable destination.

Very high percentage of the students from the survey sample has notified knowledge of English language - about 95 percent (ETF) and 85 percent (MF). Some of the students from both Faculties have also declared knowledge of another language. About 10 percent of them speak German, while French language is spoken by 10,3 percent (ETF) and 3,9 percent (MF).

In the questionnaire, a possibility for **determination of the three most important reasons for emigration** was given. The students ranging of the reasons is as following:

- Possibilities for higher salaries and higher living standard abroad.
- Better opportunities for employment abroad.
- Possibilities for professional promotion abroad and high technological job equipment.
- Economic crises and political instability of the country.

Also, students responded to the question **“What the society should do to prevent the emigration of young people”** and most of them consider that state should really put efforts for job providing (ETF - 49,6 percent and MF- 43,4 percent) and increasing of living standard (ETF - 41,0 percent and MF - 31,6 percent) as well. Improvement of professional standards of work is distinguished as important precondition for emigration prevention, too (ETF - 24,8 percent and MF - 18,4 percent). In that context, students consider the advancement of the treatment of the professionals in the country as significant.

The transformation of the potential migration into definite one will depend on the future development processes in the country, changes in the personal appraisal of the persons intending to move abroad, and at a great extend, immigration policies of the potential receiving countries. Having in mind the realistically achievable slow dynamics of the economic growth and the small possibilities in resolving the

unemployment problem, one can estimate that on the short and medium term, the Republic of Macedonia will face comparatively large migration potential and still intensive emigration.

#### 4.2.2. Immigration

The number of immigrants has significantly decreased in the eighties and in the nineties. The mentioned census data do not reflect the real situation of the total number of immigrants in Macedonia in the period up until 1994. The cognition based on the number of issued citizenships, as well as of those that still do not have citizenship is confirming that this number is significantly higher.

Immense changes have been encountered in the nineties, especially in the kinds of the immigration movements. Based on the data from the research mutually done by the Ministry of Interior and the State Statistical Office on the immigrated and emigrated persons, the number of immigrated between 1997 and 2001 was 5.854 persons. Those data do not reflect at all the real situation. In those data the persons that remained in the Republic of Macedonia after the two refugee crises in the region - the Bosnian and Kosovar - are not enclosed. The number of those persons could be estimated at about 20.000 persons. Besides that, the characteristic of the immigration movements of the last decade is a tendency of the growth of illegal and transit immigration. In the absence of the relevant data and profound research, its number would be hardly estimated.

First results of the Census on Population, Households and Dwellings, conducted in November 2002, show that the number of foreign citizens presents in the Republic of Macedonia less than a year, refugees, humanitarian cared persons and other amounted 23741 persons. Although they are only a first results, these data indicate a significant growth of the above-mentioned categories of immigrants.

As for the labor force immigration, it should be stressed that it doesn't have big volume in Macedonia, having in mind that the country is not attractive destination. One can conclude that is basically characterized by the unfavourable qualification structure compared to the emigration.

### 4.3. Policies Regulating Labor Migration

In the last four decades, the Republic of Macedonia did not have consistent policies regulating population and labor force migration, as well as measures regarding the regulation of labor emigration and immigration. It greatly highlighted the negative effects of the international migration. The volume of the immigration was more or less uncontrolled. In the same time the emigration was at large determined by the migration policies of the receiving countries. In current circumstances of large migratory potential, if those countries would be less restrictive, the extent of the emigration would be even larger.

Anyhow, the awareness for regulation of migration issues in Macedonia was increased in the last few years. At the end of 2002 the main elements of National Action Plan on Migration and Asylum for Republic of Macedonia, were defined.

In the framework of the Stability Pact for South Eastern Europe there is a Migration and Asylum Initiative (MAI), which should contribute to the creation of national and regional regimes, providing of orderly migration and alleviation of irregular and illegal flows. Also it should contribute to the ongoing establishment of migration and asylums systems. As important areas are identified: asylum, legal migration, illegal migration, border control, visa policies and entry policy.

Nowadays Western Balkan is a corridor for people smuggling and trafficking in human beings. It is acknowledged that present and future migration and asylum challenges require a truly regional response. So, the MAI is based on the work on Action Plans of five countries, out of which one is for Republic of Macedonia.<sup>57</sup>

The main objectives of the National Action Plan of the Republic of Macedonia correspond to the objectives of the Stabilization and Association Process. General objective is to set the migration and asylum systems, including on return, border management, integration and citizenship, essentially in conformity with international and European standards. Another objective is to enhance regional co-operation in this field. A basic approach is reform in the policy areas,

<sup>57</sup> The MAI Support Unit and the international organisations within the Country Team provide assistance. The Country Team for Republic of Macedonia consists of this country and the partner countries Sweden (lead country), Bulgaria, Denmark and Norway, with the participation also of United Nations High Commissioner for Refugees (UNHCR), International Organisation for Migration (IOM) and International Centre for Migration Policy Development (ICMPD).

establishment of relevant laws/regulations and institutions as well as effective management of the whole migration and asylum chain.

The existing legislation and bylaws on migration management does not meet the requirements of the international and European standards. According to the Macedonian National Action Plan a draft Law on migration should be prepared before the end of 2003, in order for a new Law to enter into force on 1 January 2005 at the latest. Concerning the migration process, the visa control system should also be developed. Draft legislation on asylum has been prepared and it should enter into force not later than 1 January 2004. Bylaws, guidelines and handbooks should be drawn up and adopted within six months after the adoption of the above-mentioned laws.

A necessary precondition for a successful implementation of the National Action Plan is training of all staff concerned from various ministries and authorities i.e. preparing a skilled staff of civil servants with professional and good ethic attitudes.

Having in mind the lack of comprehensive data for the international migratory movements, in the Macedonian Action Plan is pointed out that it will be necessary to introduce well functioning data system on migration and asylum. By new data system, all migration issues and whole asylum process should be covered. Also new technical equipment for effective managing of migration should be provided.

Concerning the integration policy of recognized refugees and other legal immigrants, equal rights in principle already exist on e.g. the labor market. A review of the legislation on citizenship is on going. Amendments to the law are to be approved by the end of 2003.

#### 4.4. Challenges of EU Accession Regarding Free Movement of Workers

##### **Expected changes in the emigration and the immigration**

Having in mind the current situation and the expected changes in the international migration movements, from the point of view of the European Union enlargement and its influence on the Republic of Macedonia,

we could emphasize the following considerations.

The characteristic of the international migrations is a tendency of continued increase of the emigration, especially labor force emigration from the Republic of Macedonia into the European Union countries. In the last decade it encountered emphasized intensity, with especially large volume of permanent emigration of highly educated labor force. After the accession of the transition countries into the European Union it can be really expected to diminish the possibilities for the Macedonian citizens to immigrate into the European Union countries. But, when there are numerous communities and broadly spread networks of the Macedonian citizens, especially in some of those countries, it is possible that the emigration will continue, but with smaller intensity and with emphasized selectivity. As for the highly educated emigration, we think that it will continue depending on the needs of the labor market in the Union for specific professionals. In any case, the doors of the Union for the most qualified cadres, especially from the technical and natural sciences, will remain open, according to the labor market needs in those countries.

The current legislative concerning the employment of foreign persons in the Republic of Macedonia is incomplete and inconsistent, so the changes to secure the provisions for free labor force mobility are inevitable. Because of the adverse conditions on the labor market, one cannot expect more intensive employment of foreign persons in a foreseeable future. But, having in mind the intention to attract the foreign direct investments and joint ventures, as well as the special services based on the long-term industrial cooperation, it is necessary to adequately regulate labor force immigration (Elka Dimitrieva, Verica Janeska, 2000, pp. 90). It primarily implies a compatibility with the regulation of the European Union countries. As for the labor force, in issuing the permits for stay, the Republic of Macedonia will have to respect the criteria of the equal employment treatment and conditions, payment and other work conditions, duration of stay and work engagement, as well as to ensure the security and health conditions.

The illegal and transit immigration in the second half of the nineties is encountering an increase. In the present circumstances of transition and insufficient economic development, one can expect intensification of those movements. With the current enlarge-

ment of the European Union in 2004 with new six member countries, and latter with the other countries scheduled for the second enlargement phase, the presupposition is real that large part of the illegal and transit migration from those countries will be into non-accession countries, including the Republic of Macedonia. In such circumstances the need to formulate a suitable immigration policy and to alleviate this unfavorable situation is urgent. Having in mind the tendency toward Euro-integration, it should contain the criteria for free population and labor force movement in accordance with the policy of the European Union.

### **Directives**

In this phase of approximation of the Macedonian legislation to the legislation of the European Union, and in accordance with the Program of the Government of the Republic of Macedonia, the directives concerning the freedom of movement of persons are not subject of approximation. Those are concerning: the Shengen Agreement, the European citizenship, the rights on residence, the social insurance, the right to acquire real estate by the citizens of the Union, the professional training etc.

Having in mind the mentioned problems about the recognition of the diplomas of the highly educated cadres that are appearing on the labor market in the European Union countries, it is important to underline the need to change and improve the quality of education. It implies timely undertaking the activities and measures to modify the education programs whose aim would be the recognition of diplomas and qualifications. In accordance with the Stabilization and Association Agreement between the European Union and the Republic of Macedonia in the section of the education, science and technology, it is foreseen that until 2004 an appropriate number of Directives concerning the recognition of the qualifications will be implemented. Those are Directive for free movement and mutual recognition of diplomas of the doctors (93/16/EEZ); dentists (78/687/EEZ); pharmacists (85/432/EEZ); veterinary surgeons (1027/78/EEZ); architects (85/384/EEZ); nurses (77/453/EEZ); baby bearing nurses (80/155/EEZ). The aim of its implementation is to secure similar education for those professions within the Union and to define minimum education criteria.

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# APPENDICES

**Table A1. Main macroeconomic indicators**

Indicators	1997	1998	1999	2000	2001	2002
GDP (in millions USD)	3458	3575	3730	3899	3723	
GDP per capita (PPS) in USD	4305	4483	4724	5018	4482	
Inflation CPI (average)	2.6	-0.1	-0.7	5.8	5.5	1.8
Current Account Balance (as % of GDP)	-7.2	-8.7	-3.0	-3.1	-10.1	
FDI (% of GDP)	0.45	3.29	0.86	4.49	11.89	
Exchange rate-average (DEN/ 1 USD)	42.82	54.45	56.89	65.88	68.04	
Exchange rate-end of the period (DEN/ 1 USD)	55.4	51.8	60.3	67.63	69.17	62.37
External debt (in millions USD)	1131	1398	1438	1437	1418	1517
External debt (as % of GDP)	30.6	38.5	39.1	40	39.7	
Foreign Currency Reserves (in millions USD)	280	334	478	714	775	733

Source: Ministry of Finance, National Bank of R. Macedonia

**Table A2. Socio-demographic data**

Indicators	1997	1998	1999	2000	2001	2002
Population (31.12.)*	2002340	2012705	2021578	2031112	2038651	-
Population (in mid-year)*	1996869	2007523	2017142	2026350	2034882	-
Working-age population (15-64)*	1294505	1305964	1317624	1328752	1339909	-
Active population (LFS data)**						
Total	800513	823826	806674	811557	862504	824824
15-64	793375	814835	798819	804048	845885	812650
Crude activity rate (of the total population)	40.0	40.9	39.9	40.0	42.3	-
Activity rate of the working-age Population	61.3	62.4	60.6	60.5	63.1	-

Note: \* population estimations

\*\*Labor Force Survey (LFS)

Source: State Statistical Office of R. Macedonia

**Table A3. Life expectancy in R. Macedonia**

Life expectancy	1996-1998	1997-1999	1998-2000	1999-2001
Total	72.49	72.49	72.68	73.05
Male	70.37	70.37	70.48	70.68
Female	74.68	74.68	74.77	75.21

**Table A4. Households' incomes and expenditures in R. Macedonia (in USD)**

Indicators	1997	1998	1999	2000	2001
Total income	1232.55	968.76	1039.16	967.3	897.4
Total expenditure	1227.72	963.78	1037.11	966.77	898.12
Monetary income	1128.91	892.07	974.02	906.13	819.03
Monetary expenditure	943.13	759.72	840.13	759.11	713.21

**Table A5. Structure of household expenditures in R. Macedonia**

Indicators	1997	1998	1999	2000	2001
Personal consumption	85.1	87.7	88.3	85.7	87.9
Contributions, membership fees and other	1.3	1.5	1.6	1.9	1.4
Expenditures on dwelling house and property	2.1	1.5	1.7	3.1	2.6
Savings	11.5	9.3	8.5	9.3	8.1

**Table A6. Key labor market indicators**

Number and structure of employment for R. Macedonia	1997	1998	1999	2000	2001	2002
Registered employment	319453	310213	315792	310213	313558	280989
Total number of employed-LFS	512301	539762	545222	549846	599308	561341
Employee	402372	417966	405991	408698	419843	396680
Employer	17128	19014	43431	23675	38206	38369
Self-employment	66418	57951	39713	57684	55020	57594
Unpaid employees in family business	25101	44831	56087	59789	86239	68698
Employment rate	34.4	35.9	35.9	35.8	38.6	35.8

Source: State Statistical Office of R. Macedonia

**Table A7. Employment in agriculture, industry and services**

% of total employment in	1997	1998	1999	2000	2001	2002
Agriculture - LFS	16.4	17.6	18.6	19.7	21.9	/
Industry - LFS	32.0	32.2	29.7	30.7	31.8	/
Services - LFS	/	/	/	/	/	/

**Table A8. Employed persons in sectors in R. Macedonia (%)**

Indicators	1999	2000	2001	2002
Private sector	41,6	43,9	50,9	52,4
Other (social, mixed, collective, state, undefined)	58,4	56,1	49,1	47,6

Source: State Statistical Office of R. Macedonia

**Table A9. Self-employed and unpaid family workers as % of total employment**

Indicators	1997	1998	1999	2000	2001	2002
Self-employed	13.0	10.7	7.3	10.5	9.2	10,3
Unpaid family workers	4.9	8.3	10.3	10.9	14.4	12.2

**Table A10. Unemployment rates in the R. Macedonia**

Unemployment rate	1997	1998	1999	2000	2001	2002
Employment Agency*	44.0	47.0	51.3	53.9	54.8	57.1
Labor force survey**	36.0	34.5	32.4	32.2	30.5	31.9

Note: \* Administrative data - persons at the age of 15 up to 59 for women and 64 for men.

\*\* Labor Force Survey data are for the population over 15 years of age.

Source: National (State) Statistical Office of the Republic of Macedonia.

**Table A11. Youth unemployment (age group 15-24) in R. Macedonia**

Indicators	1997	1998	1999	2000	2001	2002
Number, LFS	101285	99820	78941	72811	73996	67348
% of total unemployment	35,1	35,2	30,2	27,8	28,1	25,6

Source: National (State) Statistical Office of the Republic of Macedonia.

**Table A12. Long-term unemployment (% in total unemployment)**

Indicators	1997	1998	1999	2000	2001
Long-term unemployment	83.1	82.9	83.8	83.3	86.9

**Табле A13. Educational level of employed as % of total employed**

Indicators	1997		1998		1999		2000		2001		2002	
	Number	%	Number	%	Number	%	Number	%	Number	%	Number	%
1. Higher educated Higher (bachelor, master, Ph.D)	89473	17.5	94022	17.4	97060	17.7	94824	17.2	96141	16.0	102376	18.2
Higher (specialist)	56766	11.1	58525	10.8	59838	10.9	55775	10.1	63120	10.5	71493	12.7
2.Upper secondary	32707	6.4	35497	6.6	37222	6.8	39049	7.1	33021	5.5	30883	5.5
Lower secondary, primary and primary unfinished	175981	34.4	189716	35.1	193301	35.5	200676	36.5	216776	36.2	206052	36.73
	238563	46.6	256025	47.5	254860	46.8	254347	46.2	286391	47.7	252913	45.0

Source: State Statistical Office of R. Macedonia

**Table A14. Educational level of unemployed, % of total unemployed, LFS, number**

Indicators	1997		1998		1999		2000		2001		2002	
	Number	%	Number	%	Number	%	Number	%	Number	%	Number	%
1. Higher educated Higher (bachelor, master, Ph.D)	21519	7.4	19052	6.7	19036	7.2	20514	7.9	20561	7.9	19537	7.4
Higher (specialist)	13221	4.5	11350	4.0	10857	4.0	12417	4.8	12584	4.8	13515	5.1
2.Upper secondary	8298	2.9	7702	2.7	8449	3.2	8097	3.1	8067	3.1	6022	2.3
Lower secondary, primary and primary unfinished	86794	30.1	89915	31.7	90517	34.6	90167	34.5	99023	37.6	92941	35.33
	170352	59.2	175098	61.6	151825	58.1	151030	57.7	143521	54.6	151005	57.4

Source: National (State) Statistical Office of the Republic of Macedonia.

**Table A15. Salaries in R. Macedonia**

Indicators	1997	1998	1999	2000	2001	2002
Average paid net salary per employee (in denars)	9063	9394	9664	10193	10552	11279
Nominal salaries growth rate	2.8	3.7	2.9	5.5	3.5	9
Real salaries growth rate	0.2	3.8	3.6	-0.3	-1.9	



**Table A16. Social security and social policy**

<b>Social security contribution:</b>	<b>2002</b>
Pension and disability insurance	21.2%
Health contribution	9.2%
Unemployment contribution	1.6%
Replacement rate of unemployment allowance/unemployment insurance	1.35
Replacement rate of average old-age pension (as % to monthly gross wage) - calculations are based on data regarding January 2003	35%

**Table A17. Emigration of Macedonian citizens in particular countries**

<b>Country</b>	<b>1996</b>	<b>1997</b>	<b>1998</b>	<b>1999</b>	<b>2000</b>
Belgium				8 26	1415
Denmark					131
Finland		53	80	116	131
Germany	33984	38774	42550	46167	49420
Iceland			3	6	10
Italy		11596	13456	16647	
Liechtenstein	71	71	77		
Netherlands		449	482	507	500
Norway		113	140	178	207
Portugal		1	1	1	4
Romania					1
Slovenia		2200	2412	2277	3565
Spain		19	33	36	58
Sweden		1303	1594	1676	1819
Switzerland		45234	48604	51142	54042

Source: Recent Demographic Development in Europe, Council of Europe Publishing, 2000, 2001



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## **CHAPTER TWO:**

# **Conclusions and Recommendations**



## Conclusions and Recommendations: Bulgaria

As far as **labor market issues** are concerned Bulgaria should give special attention to the youth unemployment, long-term unemployment, the educational and qualification levels of the unemployed, the grey economy, the low collection of the social security contributions to the “Pensions” fund and the so-called “brain-drain” process. The government acknowledges the important role of the small and medium-sized enterprises in the job creation process in the country but it hasn’t implemented yet an encouraging tax policy towards these enterprises.

The significant role of the municipalities in the job creation process should be recognized. Municipalities could create risk capital funds and guaranteed funds at a local level for facilitating the access to the financial resources of the local small and medium-sized enterprises. They could attract national and foreign investments for the sake of the local business by effectively advertising the local community and its potential. There is a need for raising the awareness of the municipalities of the European Employment Initiatives. A branch labor market survey is necessary for providing statistical data regarding the effects on employment of investments in one or another economic branch so that the local labor force could pre-qualify and respond on time to the labor needs of the entrepreneurs. A new long-term vision for the right qualification of the labor force is needed. The labor market and the education system in the country should be transformed in regard to the future labor needs of the national and EU member states entrepreneurs. In this regard a profound survey of the future labor needs of the business is inevitable. A regular monitoring on the results of the undertaken labor market policy (active and passive) in the country is necessary for raising the effectiveness of the labor market policy. Strengthening the administrative capacity is an important prerequisite for the successful

management of the structural and cohesion funds after EU accession of Bulgaria.

Regarding the **social insurance system**, the transition to the market economy that required creation of effectively functioning market institutions in all areas of the socio-economic life, the aging of the population and the high unemployment rate as a result of the privatisation and transformation processes, imposed the reforming of the pension system, which was a pay-as-you-go-type of system. Now the pension system consists of three pillars. The first pillar is still a pay-as-you-go-type of insurance but the other two pillars consist of privately managed pension funds. The insured individuals in these funds have individual accounts and their social insurance instalments are invested in different financial instruments although there are still high state restrictions regarding the investments of the pension companies aimed at ensuring better security for the insured individuals. The future of the Bulgarian pension system depends on solving the problems with the high unemployment rate, the low collection of the social insurance instalments, the great size of the shadow economy labor force, the existence of a discrimination among the insured individuals in the Social Security, the high social insurance burden on employers and employees and not lastly the comparatively low pension incomes.

The questions in the field of social insurance are dealt with in Chapter 2 “Free movement of people” of the European legislation. The European Union does not require harmonization of the social insurance legislation between the current member states and the accession countries, but coordination of the social insurance systems. The mobility of workers and citizens in general will strongly depend on the portability of the social security and pension schemes. From this point of view, application of EU social security

coordination rules requires extending relevant administrative structures in Bulgaria. Bulgaria should keep on signing bilateral social security agreements with EU countries in the pre-accession period. The country has so far signed 11 bilateral social security agreements.

The **social protection system** in Bulgaria should be more connected to the regional disparities in the means of livelihood so that the funds of the social protection system to be distributed more fairly.

The main factors influencing **labor migration** from Bulgaria to the European Union are the labor market situation in the country, the income gap, the traditions in migration and proximity to the country of destination. The preferred destinations by Bulgarian labor migrants are the EU countries like Germany, Greece, Spain, Great Britain and Italy. For the sake of avoiding the initial pressure on the labor markets of the abovementioned countries Bulgaria should continue signing bilateral labor exchange agreements. The country has so far signed such bilateral agreements with the following EU member states: Germany, Portugal, The Czech Republic and Luxemburg. In recent years there is a tendency for signing bilateral labor exchange agreements together with bilateral social security agreements and bilateral readmission agreements. Bulgaria has so far signed bilateral readmission agreements with all European countries except for Great Britain. According to a national survey on the potential migrants, conducted by the National Statistical Institute in 2001 about 80 percent of the population do not intend to leave the country in the near future which means that these people are not potential migrants to the EU labor markets. The undertaken measures regarding labor immigration are directed mainly to protection and development of the labor market, control over the employment of foreigners and equal treatment of legally hired foreign labor with the national labor.

The challenges in the field of free movement of workers include signing bilateral labor force exchange agreements and bilateral social security agreements with all member-states of the European Union and with the new future member states that are going to enter the Union in May 2004, increasing the police and customs cooperation between Bulgaria and the EU member states by intensive data exchange, analysis and implementation of joint research regarding

the migration flows in the period till the EU accession of Bulgaria and in the transition period as well, and improving the control of the external boundaries of the country for the sake of a more effective fight with illegal labor migration. Special attention should be given to the push and pull factors, which could provoke labor migration from Bulgaria to the EU member states in order to motivate young people to find their professional realization at home thus ceasing the process "brain-drain".

## Labor market

- Although government acknowledges the important role of the small and medium-sized enterprises for solving the high unemployment problem, a purposeful tax policy for encouraging the development of the SME sector still lacks in Bulgaria.
- A greater initiative on a local level and a more intensive cooperation among the state authorities, local authorities, business representatives, social partners and non-government organizations are necessary in order to be developed successful local policies for encouraging employment and entrepreneurship accordingly the specification of the municipality, local business and the available labor force.
- Municipalities could create risk capital funds and guarantee funds as well in order to be improved the access of the SMEs to financial resources and in order to be encouraged employment on a local level. An active advertisement on a local level is very essential for the business community aiming at attraction of local and foreign investments.
- Municipalities should receive more information about the EU labor market policies and the applying procedures for the European employment projects. In order to be raised the active role of the municipalities in solving the unemployment problem state authorities should ensure a real competition among the employment projects of different municipalities and transparent procedures for accessing the projects as well.
- A long-term vision for the proper qualifications of labor force is needed and adapting of the qualification and pre-qualification systems with a view to the next 20-25 years in order to be increased

the competitiveness of the Bulgarian labor force in the enlarged European Union.

- National “Long-life learning” programs should be developed.
- A regular survey of the future labor needs of the entrepreneurs and a better coordination between the educational system and the labor needs of the entrepreneurs are of great importance.
- A regular monitoring of the results of different implemented active and passive labor market measures should be developed.
- Further efforts for solving the problem with the youth and long-term unemployment should be encouraged.
- A better coordination among the labor market policy, wage policy, social assistance policy and social dialogue will help for the better functioning of the labor market in Bulgaria.
- Reinforcing the administrative capacity is an important prerequisite for the future successful management of the structural and cohesion fund after EU accession of the country.

## Social policy

### Social insurance

- Government should extend relevant administrative structures as EU social security coordination rules require.
- Signing bilateral social security agreements with all current and future EU member states is a prerequisite for increasing labor mobility and lessening the concerns of the European countries regarding the expected massive immigration from the Central and Eastern European Countries.
- Raising the collection of the social security contributions to the Social Security funds and thus ensuring higher pension levels and opportunity for future lowering of the social insurance burden on employers and employees.
- Raising the social insurance contribution to the universal pension funds in order to ensure sufficient future pension income and motivate the participation of the young people in the pension system.

### Social assistance

- A decentralization process in the financing and management of the system for social services should be encouraged.
- The administrative capacity of the social assistance system should be improved and the coordination between the different structures on a national, regional and municipal level by establishing a single information system should be encouraged as well.
- The implementation of a Charter for the Rights and Obligations of the Socially Assisted People and an Ethic Code for the Social Worker will raise the effectively functioning of the social assistance system.
- A regular monitoring on the social assistance system is needed for identification of the problems and solving them on time.
- A better coordination between the wage policy, the social assistance policy and the employment policy is necessary.
- The social protection system in Bulgaria should be more connected to the regional disparities in the means of livelihood so that the funds of the social protection system to be distributed more fairly.

### Social dialogue

- Government should encourage the establishment of Branch Councils for Tripartite Cooperation in other ministries on the example of the Ministry of Economy, Ministry of Interior, Ministry of Regional Development and Public Works, Ministry of Transport and Communications and Ministry of Health in order to be enhanced the participation of the social partners in the EU integration activities of the country.
- The establishment of workers’ councils in the private sector for a better coordination of the owners’ and workers’ interests should be encouraged as well.
- Government should stimulate the active role of the social partners in the creation and implementation of the employment policy.
- Social dialogue should be strengthened not only on

a national level but on a branch and enterprise level.

- Social partners should be prepared for an active participation in the social dialogue on an European level regarding the future EU integration of the country.

### **Labor migration**

- Signing bilateral labor force exchange agreements together with bilateral social security agreements and bilateral readmission agreements with all current and future member-states of the European Union should be encouraged.
- Increasing the police and customs cooperation between Bulgaria and the EU member states by intensive data exchange, analysis and implementation of joint research regarding the migration flows in the period till the EU accession of Bulgaria and in the transition period as well is needed.
- The control of the external boundaries of the country for the sake of a more effective fight with illegal labor migration should be improved.
- The push and pull factors of labor migration should be carefully examined and appropriate measures for ceasing the process "brain drain" should be taken.
- Regular monitoring of the implementation of the EU legislation in the field of labor migration is inevitable.



## Conclusions and Recommendations: Slovakia

Throughout the 1990s, the Slovak Republic has launched most reform steps, which economists perceive as crucial for a successful transition from planned to a functioning market economy. Principal reforms have been completed, however, several demanding components of the reform scenario are yet to be addressed. Among them, the reform of the social protection system – including public health, labor market policies, social insurance, social support and social assistance – which should remove the remaining system deformations and adjust social policy to the changing economic, social and demographic environment.

The Slovak labor market is marked by several distinct features. Perhaps the most pronounced is the high rate of economically active persons without official jobs. Unemployment became the weakest point in the economy and is constantly viewed by the public as the most pressing societal problem. The 2001 unemployment rate of 19.2 percent was far more than double of the European Union average (7.4 percent). Young people belong to the most severely affected groups by unemployment. Another disturbing fact is the high share of long-term unemployed, who make up more than 50 percent of the unemployed. A “hard core” of unemployable persons with insufficient education and qualification has emerged, placing a growing pressure on public funds. Immense regional differences and low mobility between the regions complete the picture of a rigid labor market.

Experts agree that the setup of the social protection system contributes to the persisting problems in the labor market. The social system, as a whole, acts rather as a trap for unemployed, instead of motivating them to take an active approach. Centrally regulated pillars of social policy (such as the minimum wage and subsistence minimum) and the different

social transfers (such as social assistance benefits and unemployment benefits) have disincentive effects on the behavior of their recipients mainly in regions with lower average wages.

A high degree of redistribution is typical for the Slovak social protection system. The tax and payroll burden placed on employees and employers is among the highest in OECD countries. Contributions to different social funds range as high as 50.8 percent of the gross wage and create a wedge between labor costs and wages. The situation is particularly burdensome for employers (contributing with 38 percent), who bear also the administrative costs. High social security burden indirectly supports activities in the informal economy and impacts on the level of tax and payroll collection. Eventually, extensive labor costs discourage employers from job creation and contribute to growing unemployment. The pension scheme with the dominant public unfunded pillar is based on principles of extensive solidarity and redistribution. The individual merit is subordinated to these principles; the connection between the contribution into the system (insurance premium) and the benefit (pension) is reduced to a minimum. The system is particularly demotivating for higher income groups, which are not adequately rewarded for the invested security payments. Contributions into the fund are deemed high to be a stimulus for employees and mainly employers to act actively in the formal labor market, at the same time, benefits are deemed low to provide for a moderate subsistence in old age.

The policy responses to the crucial labor market problems have, so far, not brought substantial positive change. Traditional tools of labor market policies were dominated by passive measures (unemployment benefits and contributions on behalf of registered unemployed). However, the effectiveness of

active measures has neither been astonishing; the success rate of finding stable job opportunities after participating in active labor market programs has been relatively low. This is not merely the result of restricted budgets, but also of the lacking organizational and institutional capacity and not least the dissatisfactory educational attainment of unemployed.

Mobility of Slovak citizens, both in internal and international terms, is generally low. Internal mobility in 2001 accounted for less than 1.5 percent of the entire Slovak population. Migration due work is concentrated within districts and/or regions. Surveys suggest that it is unemployed who are most resistant to labor mobility. There is an obvious lack of understanding of the importance of mobility due work; mobility is by a large stock of the labor force not viewed as a means for job search and take up.

Based on official data, about 2.2 percent of the total number of employed were working abroad in 2000. The actual number of persons working abroad is estimated to be significantly higher. The most attractive destination for Slovak citizens is the neighboring countries (Czech Republic, Austria, Hungary) and Germany. To facilitate international migration of labor force, Slovakia has made efforts on the part of adjusting domestic legislation, as well as by concluding bilateral agreements and coordinating policies with both EU candidate and member countries in the field of employment policy, education policy, social protection, etc. Adoption of new pieces of legislation has not always led to higher flexibility of labor market and social system in Slovakia (e.g., the new Labor Code).

The reforms of labor market policies and of social protection in general are of highest priority. They would have been priority agenda even if Slovakia was not applying for EU membership. However, EU accession impacts significantly upon the reform process in candidate countries by opening new prospects and opportunities but also by posing new challenges.

There is no uniform model of social security in the EU. On the contrary, Member States apply different schemes and rules, while using open method of coordination to facilitate migration and transferability of the schemes between the countries. With the ten new members the EU social policy will become even more diversified.<sup>58</sup> Despite the considerable diversity within the EU, Member States face common challenges with regard to social systems, and social security in par-

ticular. They also share common objectives and are committed to a number of principles, amongst which are equity and social cohesion, which characterize the European social model.

The modernization of social security systems in the EU is made urgent mainly by demographic aging and its impact on the old age dependency ratio. Although the reform of social security systems remains the responsibility of the Member States, co-operation at EU level has intensified – in particular through the Social Protection Committee.

The Slovak Republic is expected to enter the European Union along with nine other accession countries in May 2004. It becomes clear that Slovakia will enter the Union with some of the important sectors unreformed and/or in the ongoing process of reform. It is therefore desirable that the parameters of the reforms are adjusted to ease the entry and the membership in the Union. The setup of the reforms must take into account the principles of the common market, mainly the freedom of movement.

Reforms that would enhance mobility of Slovak citizens in an enlarged European Union, include the following areas:

- Social security (pension)
- Social support and assistance
- Labor market (employment) policies
- Health care
- Tax policy
- Educational system
- Housing policy
- Public administration (decentralization)

The following policy recommendations refer mainly to labor mobility.<sup>59</sup> Certainly, this is not an exhaustive list, however, it offers space for further discussions on labor mobility in an enlarged EU.

## Social policy

### Social insurance

The mobility of workers and citizens in general will strongly depend on the portability of their social security and pension schemes. This is an important incentive for the Slovak reform agenda. One of the

<sup>58</sup> See e.g. GVG (2002)

<sup>59</sup> This does not mean that the issues of labor mobility should be understood separately from other components and aspects. On the contrary, integrated approach rather than partial measures are a precondition for positive changes in the sited areas.

key features of the reforming social system in Slovakia should be therefore its compatibility with Member States' schemes. Slovakia may also face competition from other social security systems: if there are strong financial incentives built into the various retirement income systems, these could induce people to move to other countries. The old age dependency ratio in most developed economies will be substantially higher in the future. In many Member States, funded pension provision will be expected to play a greater role.

### **Social support and social assistance**

Adjusting current social support and assistance schemes to regional differences in the costs of living would be beneficial in promoting geographical migration towards areas with relatively strong labor demand. Measures in the field of social assistance should be coordinated with passive and active labor market policies and poverty/social exclusion reduction strategies. An important aspect is the reduction of the misuse of the social system. Failing to remove the disincentives could lead to higher rigidity, lower mobility, and increasing shadow economy. Transferability of social benefits is also an issue to be addressed.

### **Labor market**

Measures to widen job opportunities and fight labor market distortions do not solely comprise traditional tools of labor market policies, although their importance is not questioned. Nevertheless, these labor market tools need a re-assessment of their contribution towards a proper labor market. Transparent and flexible labor legislation, improvement of the business environment, simplified conditions for establishing and operating of enterprises, consistent enforcement of law, careful reduction of tax and payroll obligations, decentralization of the social framework – these measures are among the necessary steps to reform the labor market. Continuous improvements in the flow of information on job vacancies and opportunities, aided by the creation of private job placement and temporary agencies, can enhance the job- and skill-matching processes in the economy. The utilization of structural funds is expected to assist in addressing regional disparities; a precondition is im-

proved management of the funds by responsible ministries, improved access to information, training courses, etc.

**Health care.** Health systems in EU Member States differ considerably as regards the methods of provision of services, the means of financing the overall system, and reimbursement mechanisms for provided services. However, the European Commission emphasizes three objectives of modernization reforms: access to health care for all, a high level of quality in health care, and ensuring the financial viability of each health care system. With respect to current development of health-related policies within the EU<sup>60</sup>, Slovakia might experience serious problems in assuring reimbursement of services and goods obtained abroad. Portability of health insurance seems to be a key issue when it comes to increased mobility.

**Tax policy.** Carefully designed reduction of tax and mainly of social security contributions could help boost job creation and reduce shadow employment. Such reductions would diminish the wedge between gross and net salaries, increasing both labor demand and incentives to work.<sup>61</sup> Such measures can not remain isolated from other reform steps, mainly the reform of the pension system, business environment improvement, labor market reforms. Tax policy offers possibilities to stimulate mobility in many areas, including housing market and transport. The burden of the high transport costs discouraging commuting could partly be reduced by making it tax deductible. Similarly, tax incentives on housing construction could help to attract necessary private investment.

**Educational policy.** One of the most emphasized functions of the school system is the preparation of students for a successful entry into the labor market. However, this role of the educational system is often neglected. Mechanisms enabling schools to respond more flexibly to the changing needs of the labor market must be initiated. This requirement becomes even more urgent with respect to the changing environment in the common market of the EU.

<sup>60</sup> For instance the recent judgements of the Court of Justice on obligation of national health insurance system to cover services performed within other Member States.

<sup>61</sup> World Bank (2001)

**Housing policy.** Experience of countries with sound housing sectors shows that a proper link between housing, mobility and employment can only be provided for by a functioning market environment along with an appropriate involvement of the public sector. The list of measures to make the housing market in Slovakia more flexible and to boost new housing construction, is rich. It includes abolishing of administrative controls on prices and rents, simplifying procedures connected with construction pursuance, exemption of land for housing purposes, etc.

**Public administration.** A properly designed decentralization of the provision of social transfers to the municipal level could help to efficiently target services and react to regional differences. It may eventually display in a reduction of the number of recipients and/or of the level of social transfers (particularly of social assistance benefits), but also in a better targeting of public support and assistance to those in real need. To provide for equality of chances, it will be necessary to secure awareness of local people concerning these processes and perspectives of regional development, to enable them to take and correct their work-related (and more generally, life-related) decisions.

**“Brain drain”:** is very high in Slovakia, and can only be effectively addressed within comprehensive national and regional economic development strategies, which are currently lacking.

**“Brain exchange”:** a better targeted immigration policy which stresses the labor market demands of the host country, i.e. it has an influence not only on the size but also on the composition of immigrants, may help improve both their labor market performance and public image, thus also catalyzing their social integration in the host economy.

## Conclusions and Recommendations: Estonia

Estonia has created a well-structured market economy with an average growth of GDP of around 5% over the last five years. Estonia is characterised by an open and liberal economy. Estonia has signed an accession treaty with the EU and will probably become a member of it in 2004.

**Labor market:** The Estonian labor market has been characterised since the beginning of the transition period by declining labor force participation and employment rates. The unemployment rate that has declined for two years now remains high at 10 percent. Compared to the EU average it could be one motivation for labor emigration. Generally, the Estonian labor market problems are the same as those within the EU Member States. Youth unemployment and unemployment of ethnic minorities are higher than average, and there are big regional differences in labor market performance. In addition, Estonia suffers from high levels of long-term unemployment. Also, Estonia unlike the EU countries has unemployment levels for women, which are lower than that of men. Against this background the Estonian labor force is ageing and Estonia could face, if current trends continue, a shortage of labor supply.

The reasons of the labor market problems can be largely attributed to fast economic and structural changes. People are not able to keep their skills and qualifications in-line with the labor market needs. Also the public policies (labor market policy and education policy) have not developed enough to bring people who are unemployed efficiently back to the labor market. As there is no state-financed system to support adult training (excl. unemployed, civil servants, teachers) the creation of supported in-service training of the workers and opportunities for re-training are the key factors in further fighting structural un-

employment.

The financial allocations for employment policies have been extremely low, lagging behind EU levels by around 8 times. The supply of active policy programs has been small, so that only a small percentage of unemployed can participate. The accession to the EU will bring about big financial support to Estonia, which will include allocation for employment policies. In this context the administrative capacity of public employment services to use these funds should be evaluated carefully. There is no regular monitoring of the effectiveness of either active or passive labor policy measures. Thus there is no possibility to conclude whether the choice of a particular policy set is justified or not.

Social partnership is also relatively weak in Estonia. This is mainly due to their low representation. While there has invariably been social dialogue on a national level, there is no social dialogue on a regional or sectoral level. As the Government is the strongest partner in any social dialogue, the final decision on implementation of negotiated issues rests with them. In order to promote social partnership, which can conform to European Social Models, the general attitude and participation in employees' organisations should be promoted and encouraged.

While there are no rapid changes envisaged in the labor market, due to accession to the EU, there may be an improvement in the unemployment situation if the financial aid is used effectively.

**Social policy:** The Estonian social protection scheme is characterised by almost universal coverage; with a substantial role of flat-rate benefits, which have relatively low replacement rates; a few earnings-related benefits and reliance on contributory based

financing. Social protection expenditures both in absolute terms and as a share of GDP are lower in Estonia than in the EU states, but this gap could be linked more to the general differences in wealth, and less to a specific lack of social protection.

Currently the social security coordination, in the case of movement of workers, is regulated by bilateral agreements. There are also some provisions in the Europe Agreement, signed in 1995, but these have never been implemented. From the date of joining the EU the EU Regulations will be applied to economically active people (and their family members), replacing the bilateral agreements. For other people the bilateral agreements will still apply. Although there is no obligation to harmonise bilateral agreements with the EU Regulations, the discrepancies may cause substantial administrative problems.

Application of the EU's social security co-ordination rules requires extending relevant administrative structures both at Ministry level as well as within the implementing bodies. Also, the existing bilateral agreements need revision to avoid extra administrative complications. In this respect, the principles of co-ordination of the EU Regulations could be bilaterally extended to all persons who are currently in the personal scope of bilateral agreements. The Government could also make an effort to conclude arrangements on mutual waiving of reimbursement of the costs of medical services, with some of the EU Member States, in order to ease administrative burdens associated with the implementation of the EU Regulations.

The direct effect of accession upon social protection systems and policies will be rather limited, but there will be important indirect implications. Social security co-ordination extends the rights of Estonian citizens moving across Europe. While currently pensions and other benefits are paid on the basis of residence, after accession pensions must be paid also to persons who have obtained insurance periods in Estonia, but reside in any other Member State. The EU co-ordination rules will add a certain degree of financial constraint to existing schemes of pension and health insurance. The additional burden is estimated to be about 0.5 to 3 per cent of respective budgets.

It appears that with accession to the EU from the state's perspective, the most problematic social se-

curity schemes are residence-based benefit schemes, which offer universal flat-rate benefits with no qualification period. As access to these benefits is relatively easy, co-ordination can increase costs, depending on the flow of migrants. As universal flat-rate benefits have also been the predominant type of cash benefit in Estonia, accession may force a tightening of some of the eligibility criteria.

**Migration and migration policies:** The Estonian labor market is currently in a situation where several factors act as push factors for migration. The main features are high unemployment, high unemployment amongst young people, a relatively high educational level of the Estonian labor force and big income differentials.

The outflow of Estonian citizens is not a problem for Estonia at this stage and there is probably no need to restrain the migration after joining the EU. The migration flows are predicted to be quite low and their impact on labor market and economy is predicted to be low as well.

The majority of migration is predicted to be temporary and short-term or seasonal. This kind of migration has some good aspects. During their stay abroad, people can accumulate new knowledge and skills and when they return to Estonia, their human capital value is increased and they are more valuable in the Estonian labor market. Young people, who do not find a job after graduating in the Estonian labor market, are often looking for a job in other countries. If they are able to find a job, they do not have to start their working career with a frustrating unemployment period (keeping in mind that the unemployment of the young is particularly high in Estonia), they can get work experience and the social security system does not have to support their unemployment or non-activity period. At the same time young people are the ones who have the weakest propensity to come back.

Predicted outflows of Estonians reveal, that it might bring about some problems in the future. In the next ten years, Estonia is facing the problems of an ageing population and the challenge of maintaining a sufficient workforce. Faced with given demographic trends, there is a need to maintain a sufficient labor force, a sustainable dependency ratio and also to diminish the emigration potential from Estonia through

reducing the unemployment rate and increasing the participation rate. This is also tightly connected with supporting the job creation process and self-employment initiatives. In order to reduce emigration potential the income differential must decrease. This might be a policy option if there are severe consequences of free movement of workers in some occupations (e.g. medical doctors).

The general system for facilitating free movement of workers is under way. The preparations are ongoing for implementing the European Employment Services System in Estonia. The arrangements for mutual recognition of diplomas and qualifications have been made, and the legislation for coordination of social security systems has been adopted.

Estonia has not requested any transitional arrangements regarding free movement of workers and Estonia has agreed to a transitional arrangement in respect of the free movement of workers put forward by the EU. Only five European countries have announced the freedom of free movement of workers for Estonia: Denmark, Sweden, Netherlands, UK and Ireland. Restrictions on the movement of workers from Estonia to the EU will apply for a minimum two-year period as of the date of accession and may remain in force for a maximum of seven years. At first in two years and then in three years the Member States must justify the maintenance of the transitional period. Estonia should prepare for protecting its interests in these cases by evaluating the migration trends continuously.

### **Employment policy**

- The accession will double spending on active labor market measures due to support from Structural Funds. In this context the administrative capacity of public employment services (PES) should be evaluated. Currently, there is no clear vision of how much and how efficiently the PES can offer active labor market measures.
- As the generation of new programs must be justified a system must be created for regular evaluation of ALMP. There is no evidence currently on the effectiveness of these programs.
- As there is no state-financed system to support adult training, the creation of public in-service training and re-training services is crucial in fighting

structural unemployment.

- Also a system must be developed for evaluating passive labor market measures. More specifically - recently launched systems of early retirement and unemployment insurance should be evaluated regarding work incentives.
- Social partnership is not developed enough for carrying out social partnership and social dialogue, which is an integral part of the European social model. In order to change this, the emphasis should be placed on strengthening the administrative capacity of social partners and prioritising the social partnership approach in society.

### **Social protection**

- The administrative capacity concerning the implementation of social security co-ordination rules must be improved.
- The Government should try to conclude arrangements with other EU Member States on mutual waiving of reimbursement of the costs of medical services.
- The existing bilateral social protection agreements need revision to avoid possible conflicts between the EU Regulations and bilateral agreements. In this respect, the principles of co-ordination of EU Regulations could be bilaterally extended to all persons who are currently in the personal scope of bilateral agreements.
- Accession to the EU may force a tightening of eligibility criteria of some of the current universal flat-rate social security benefits, to prevent increase of expenditure.

### **Migration policy**

- There is no need to restrain migration of workers on behalf of Estonia in the short-term as the predicted migration flows are low. Therefore the expected impact of migration on the labor market and wages is also low. At the same time, in some areas of economic activity or occupations, Estonia may face the shortage of qualified workers and therefore the careful monitoring of migration flows and the analysis of their impact on the labor market is needed.

- Long-term measures to cope with the impact of the ageing of population on the labor market and social protection systems, could include migration policies (attracting foreign labor, restraining outflow of domestic labor).
- If many young people migrate in the future, incentives will be required for enticing them home.
- In some cases (for some occupations) it might be necessary to reduce push factors of migration, e.g. income differential (concerns mainly occupations financed by Government).
- As the transitional agreements in Member States are reviewed and justified after two and then three years, Estonia should prepare for protecting its interests in these cases. Therefore continuous collection, supervision and analysis of migration data should be done.



## Conclusions and Recommendations: Macedonia

**Labor market:** During the transition period the development of the labor market in Republic of Macedonia faces a number of problems. Some of them should be outlined as being most important.

First and most important problem is unemployment. Very high unemployment rates and significant long-term unemployment that Macedonian labor market faces are result of the registered employment decrease and the high labor force supply compared with the low labor demand,

The second problem concerns the lack of job creation. The privatisation process, the economic reforms and the restructuring of the economy, as well as poor investment, in the last decade lead to a continuous job destruction instead of job creation.

The third problem is related to lack of employment policy and relatively small participation of the active market-market policies.

The next problem results from the unclear division of responsibilities between different levels of governmental structures and civil society in establishment, implementation, management and monitoring of market activities.

Particular problem is lack of valid market statistics and information system on employment development as prerequisite for good prognosis of the true dimensions of the unemployment problem.

Having in mind the size and the character of the unemployment in the Republic of Macedonia, a basic presupposition for its decrease is the development and the economic growth. In that context, within the development strategy of the country special care should be taken to the development of the industrial and agrarian sector. Because of insufficient economic development, opening the new jobs will primarily be under the influence of the new investments – domes-

tic and foreign. In that sense the government would primarily have to generate a new conditions to stimulate the development of the market economy and intensification of the investment activities in the country.

Concerning the complexity of the unemployment problem, the Republic of Macedonia would have to build an employment-oriented strategy as soon as possible. It should be funded on a coordinated and integrated approach that the factors in the institutional and macroeconomic framework include both employment and labor-market policy interventions.

Macedonia needs consistent employment policy as a cross-sectoral policy that include all policy field, affecting directly or indirectly the employment of labor force as a factor of production. Concerning the sectoral policy spheres particular attention should be devoted to the regional, industrial and agricultural policy. Within the regulative and macroeconomic spheres of the economic policy adequate employment and labor market-related measures in the financial policy (taxes, contributions, subsidies) should be taken. Also, adequate measures in the monetary policy (for further preserving maintaining monetary stability) and in the wage policy (use of the minimum wage as an instrument of social policy) should be taken (Verica Janeska, 2003).

The qualitative characteristics of the labor force are increasingly becoming the important precondition for the modern organized production. The changes in the education system in Macedonia should largely be coordinated with the development orientation of the country. So, within the education policy particular attention should be devoted to the professional orientation and the permanent education.

The labor market policies should primarily be oriented toward active measures and programs, par-

ticularly in job creation. As for the passive measures on the labor market, the need of its more sizeable use will also remain in the medium term. It will be under the influence of the size of the current unemployment, of the solution of the problem of the enterprises-losers, the pressure that is expected because of the liberalization of the labor market, as well as of the inflow of new job seeking persons.

In Macedonia valid labor market statistics and information system on employment development are necessary for good analysis and prognosis of the true dimensions of the unemployment problem. In the same time this is prerequisite for creating an employment-oriented policy and labor market policy, as well as for special programs for particular risky groups on the labor market (young persons seeking for job for a longer time, the persons with higher and high education, persons with lower education level, persons belonging to adult groups seeking for job etc.).

**Social Policy:** Unfavourable situation on the labor market had caused changes in the social sphere, especially in the field of social benefits. Increase of the number of unemployed persons had lead to the increase of the number of household - beneficiaries of the social pecuniary aid because over 90 percent of bearers of this aid are unemployed persons. This situation is an indicator of the high level of dependency between the unemployment and poverty in the country. Programs, measures and activities for decrease of unemployment are necessary for poverty alleviation in Macedonia. As primary goal in the macroeconomic policy of the Republic of Macedonia for 2003 is creation of policies that should result in active involvement of the social aid beneficiaries in the labor market. The legal aspects of this program are contained in the mentioned Law for Stimulation of Employment. Also, the need for increase of the flexibility of the labor market is already shaped into the Program for increase of employment and flexibility of the labor market. The main aim of the Program is promotion and implementation of different measures and projects focused on active labor market policies, in purpose of alleviation of poverty by employment of the most jeopardized groups of social bearers.

Alongside to the Program, activities should be undertaken for improvement of the system of social protection, in function of more justified distribution of

the social aid and it's transmission toward the poorest categories in Macedonia. That means, revision of the criteria for rights on social aid, in order of their stimulation for employment and active participation on the labor market.

The reform the social protection system should be according to the European standards, with introduction of the pluralism in the social protection. Also, general international standards should be respected, especially in the process of deinstitutionalization of social protection that is underway in Macedonia. All this is important in the accession process to EU, as well as experience of other countries that are in the first two groups for EU enlargement.

**Migration policy:** Concerning the consequences and implications of upcoming EU enlargement on the international migrations of Macedonia, it could be stressed that most probably, the possibilities for legal migration of Macedonian citizens to the EU countries, especially low skilled, will be smaller, due to the enlargement of the labor market of the Union. But, beside that, the migration will continue with some volume and dynamics, because Macedonia has already very strong migration networks in few countries of EU. As far as the migration of the highly educated labor force is concerned, especially from certain professions will continue without particular problems. Therefore, the existing problem of brain drain will remain.

Further intensive emigration of the highly educated persons will contribute to the serious distortions in the structural and sectoral labor force distribution in Macedonia, which is one of the most significant factors for the country's socio-economic development. In those circumstances, defining and acquiring the consistent and transparent long-term migration policy is imposed as inevitable. It should be directed toward overcoming the current situation of extensive permanent moving away, especially by the young persons with higher education levels. For that aim, the appropriate measures and instruments are necessary to be included in the migration policy.

The problem of the intensive labor force emigration could not be overcome by the partial short-term measures. The solution should be sought in a well-defined short-term and long-term development policy. It is influenced by numerous limitation factors. They impose the selective approach to the problem

and a socially rational priority selection. In that context, the need for socio-economic measures, which on the medium-term should get a priority, is inevitable. Those are: the overcome of the social and economic crisis, the creation of the conditions for the employment increase, the alleviation of the problem of the unemployment, the creation of the real conditions for the intensification of the return streams, stimulation and support of the science and research etc.

Migration policy should be also directed toward the labor force immigration and overcoming of growth of the uncontrolled, particularly illegal and transit immigration. Concerning the labor force immigration, a Law on employment of foreign citizens should be drafted and enacted. The regulation of illegal and transit immigration is extremely important, because of expected increase of its volume, due to the restrictions of their volume in the new members of EU. In the Macedonia, a National Program against people smuggling and trafficking in human beings already exists. So, the effective implementation of the program must be ensured.

Within the laws on migration and asylum the return policy and procedures should be developed. Existing readmission agreements should be implemented in accordance with EU standards.

Effective border management is of high importance for the migration and asylum system as a whole. To achieve this aim it is necessary: clearly demarcated borders; a sound legal basis; non-military structures; well trained, equipped and managed services; good co-operation with the services of neighboring countries; bilateral and multilateral co-operation. Activities for improved border control are already on going through the Integrated Border Management Project funded through the CARDS program.

As far as provision of relevant data and information for the international migratory movements is concerned, a well functioning data system on all migration issues is necessary to be introduced as soon as possible. As for the managing migration and asylum issues, special projects for an information system including new computer equipment should be initiated.



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# **EU Enlargement and Its Impact on the Social Policy and Labor Markets of Accession and Non-accession Countries**

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