

Employment and Development in South-East Europe in the Context of Economic Globalization

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Foreword

The objective of this paper is to map recent economic and social developments in South-East Europe (SEE) in the context of economic globalization. Particular attention is paid to employment, in terms of the quantity and quality jobs. Policies and institutions impacting on employment are reviewed showing achievements and deficits of recent public and private interventions, and further necessary policy reforms. Finally, a plea is made for more cooperation of responsible actors, both at the national and the international level, to attain a consistent and coherent employment strategy.

From the perspective of the ILO employment is central to development. In the SEE region employment performance has been unsatisfactory during the last one and one-half decades. Enhancing job opportunities in general, and for young people in particular, would seem to be of crucial importance for securing peace in the West Balkan region that was struck by civil strife and armed conflict in the 1990s. Employment is a key ingredient to combating poverty and promoting greater income equality, both within and across countries. Economic convergence and social cohesion are central goals of the policies of the European Union to which all SEE countries that are not yet members are seeking access.

For the purposes of this paper SEE comprises the twelve nation states that were invited to participate in the conference (= SEE-12). They include Albania, Bosnia and Herzegovina, Bulgaria, Croatia, Greece, Romania, Serbia, Moldova, Montenegro, the Former Yugoslav Republic of Macedonia, Slovenia and Turkey. Montenegro declared its independence from Serbia on 2 June, 2006. As most of the statistical data presented below relates to the period prior to the separation, Serbia and Montenegro are treated as one state in part of the analysis. Where this is the case, reference will be made to the SEE-11.

I. South-East Europe in the Global Economy

In 2004, the total resident population of SEE-11 was 141 million, up from 130 million in 1990. Turkey alone makes for slightly more than half of it (Table I-1). Not counting Serbia&M, the region's (unweighted) average *gross domestic product (GDP) per capita*, in purchasing power parity (PPP) terms, had reached 8,686 US \$ in 2003, which was 9,4 % above the average value for CEE-CIS countries, roughly 5,6 % more than the world average product, and 34 % of the OECD average (see Table I.1).

Table I.1): Population Size and Gross National Income

Country	Population (million)			GDP per capita (US \$, PPP) 2003	GNI per capita (US \$) 2004
	1990	2004	2015		
Albania	3.3	3.1	3.5	4,330	2,120
Bosnia&H	4.3	3.9	4.2	5,637	2,040
Bulgaria	8.7	7.8	7.2	7,304	2,750
Croatia	4.8	4.4	4.3	10,468	6,820
Greece	10.2	11.1	11.0	18,850	16,610
FYR Macedonia	1.9	2.0	2.2	6,419	2,420
Moldova	4.4	4.2	4.1	1,426	720
Romania	23.2	21.7	21.1	6,875	2,960

Serbia&M	10.5	8.1	10.7	--	2,680
Slovenia	2.0	2.0	2.0	19,150	14,810
Turkey	56.2	71.7	81.2	6,398	3,750
EU-25	451.4				
EU-15	378.1				
CEE+CIS				7,939	
OECD				25,915	
World				8,229	

Sources: UNDP, Human Development Report, 2005; World Bank, World Development Indicators, Country Profiles, April 2006.

Looking at the eleven countries individually, we find an enormous variation by population size and income level. The number of residents varies from about 2 million in FYR Macedonia and Slovenia to nearly 72 million in Turkey. Four countries (Albania, Bosnia&H, Croatia and Moldova) were in the range of 3 to 4.5 million. The span of prosperity measured by GDP per capita (in purchasing power parity terms) is between 1,426 US \$ in Moldova and 18,850 US \$ in Greece. Moldova plummeted to the level of a low-income country during the 1990s. In seven of the SEE-11 the average per capita income is less than 8,229 US \$ which was the average citizen's income in the world as a whole in 2003. A similarly large differential in the standard of living between the region's countries is revealed by the data on *gross national income (GNI) per capita* in 2004 (Table I-1). This indicator captures total valued added from domestic and foreign sources. The level of economic and social development countries is measured by UNDP's *Human Development Index (HDI)*. Of a total number of 177 countries surveyed, the HDI of 2005 places Greece in the 24th position. Slovenia ranked no. 26, Croatia no. 45, Bulgaria no. 55, FYR Macedonia no. 50, Bosnia&H no. 68, Albania no. 72, Turkey no. 94, and Moldova no. 115 (UNDP 2005). In addition to average income, the HDI includes mean educational attainment and mean life expectancy at birth to form a composite measure of the degree of human development.

Table I.2: Structure of Employment by Economic Sector, 1990-2004

Country	Agriculture			% Employment in Industry			Manufacturing			Services		
	1990	2000	2004	1990	2000	2004	1990	2000	2004	1990	2000	2004
Albania	--	71.8	58.5	--	6.6	13.6	--	3.2	6.0	--	21.5	27.6
Bosnia&H	--	---	---	--	--	--	--	--	--	--	--	--
Bulgaria	18.5	26.2	9.7	44.2	28.3	33.1	32.9	20.7	23.9	37.3	45.5	56.7
Croatia	--	14.5	16.4	--	28.8	29.8	--	20.0	19.3	--	56.5	53.7
Greece	23.9	18.6	16.5**	27.7	22.3	22.4**	19.4	13.8	13.1**	48.3	59.1	61.1**
Macedonia	--	--	16.8	--	--	32.8	--	--	22.2	--	--	50.1
Moldova	--	50.9	40.5	--	13.9	16.2	--	9.0	10.3	---	35.2	43.2
Romania	--	42.8	31.6	--	26.2	31.2	--	19.1	22.4	---	31.0	37.2
Serbia&H	--	--	--	--	--	--	--	--	--	--	--	--
Slovenia*	10.7*	9.5	9.6	44.1*	37.4	35.9	--	--	--	45.1*	52.3	53.2
Turkey	46.9	36.0	34.0	20.7	24.0	23.0	14.8	16.9	17.4	32.4	40.0	43.0

Source : KILM 2006 * 1993 ** 2003

The inter-country gap in development is also reflected in the sectoral composition of employment and output. A low percentage of employment in agriculture and a high percentage of employment in services are usually seen as signs of advanced development. In 2004, the proportion of employment in agriculture amounted to 58 % in Albania, 40 % in Moldova, 34 %

in Turkey and 32 % in Romania. The remaining countries had 17 % or less. The mirror image of this pattern is the proportion of employment in services. While in Greece, Bulgaria, Croatia, FYR Macedonia, and Slovenia, more than 50 % of all employees hold services jobs, the proportion is less than one half in the other countries, and especially low in Albania (28 %) (Table I-2).

Next to large socio-economic disparities, SEE is characterized by major ethnic, cultural and religious diversity. In fact, there are few regions on globe that match the region's incidence of cultural pluralism. Cultural diversity tends to have both positive and negative implications. It may enrich the dynamism of business and the quality of life, but it may also induce conflicts when it comes to a "clash of civilizations" (Samuel Huntington). As we know from the novel *Na Drini Caprija* (« The Bridge on the Drina », 1945) of Nobel prize laureate Ivo Andric, a native of Bosnia, peoples in the Balkan, despite enormous cultural heterogeneity, were co-existing relatively peacefully for centuries before nationalist sentiments flared up in the region – as elsewhere in Europe - the course of 19th century to emerge in a century of tensions and wars ending as late as 2001 after the conflicts in Bosnia and Macedonia. The term « Balkanization » became synonymous with political fragmentation and economic segmentation.

Whether or not the current fragile peace in the West Balkan region will last, or whether new conflicts emerge, will in large measure depend on the region's future economic and social development. We owe it to an invaluable insight gained in the 20th century that peace between nations presupposes social peace within nations. It was this very idea on which the ILO as a peace promoting institution was founded under the Treaty of Versailles in 1919.

Table I.3: Trade of Goods and Services

Country	Average annual % growth		Imports		Exports		% High	Trade Balance	Growth Real
	Exports	Imports	Imports	Exports	% of GDP	Tech-Exports	% of GDP	Trade less	
	1990-2000	2000-04	1990-2000	2000-04	2003	2003	2004	Real GDP %	
World	7.0	5.0	6.0	3.3					
Middle Income countries	7.2	10.1	6.3	9.3					
Albania	17.9	16.9	15.8	16.8	42	19	1	-22.1	12.8
Bosnia&H	-	5.3	-	2.3	59	25	--	-52.2	-3.8
Bulgaria	3.9	9.1	2.7	11.7	63	53	4	-18.6	5.8
Croatia	5.9	6.1	4.6	8.6	57	47	1	-25.0	4.0
Greece	7.6	-0.4	7.4	1.1	28	20	12	--	3.7
Macedonia	4.2	-2.3	7.4	0.1	53	35	--	-23.4	4.6
Moldova	0.7	16.3	5.6	16.0	88	54	3	-	11.4
Romania	8.1	12.5	6.0	14.8	39	33	4	-12.5	8.5
Serbia&M	-	14.5	-	23.1			--	-30.8	--
Slovenia	--	8.4	--	7.0	60	60	6	-4.2	1.9
Turkey	11.5	12.1	11.0	10.9	31	21	2	-9.2*	7.0

Source, UNDP, Human Development Report, 2005 ; UNECE, Economic Surveys of Europe, No. 2/2005
*in 2003

The economic and social destiny of SEE – similar to that of virtually any other region – is closely connected with its capacity to cope with the challenges of economic globalization. International economic integration has advanced in the majority of the region's countries. This is

evident from the fact that international trade grew faster than output. Both in the 1990s and the period 2001-04, the annual rates of growth of imports and exports exceeded the annual rates of GDP growth. The only exception is FYR Macedonia that saw an absolute decline of imports and exports despite modest GDP growth in the period 2000-04. The rate of growth of real trade less the rate of growth of real GDP which is used as standard indicator of integration of a country with the global economy shows positive values for all SEE-11 economies for 1990-2004, except for Bosnia&H. Particularly large advances of economic integration were made by Albania, Moldova, Romania and Turkey (see Table I.3). Economic openness is also signalled by the volume of trade (imports plus exports) as a proportion of GDP. In percentage terms, this was more than 100 in Moldova, Bulgaria and Croatia. In FYR Macedonia, Bosnia&H, and Romania, the share was between 70 % and 100 %. In large part, trading remains within the SEE region, and between the region and the EU-25 and the European CIS countries. Some trade extends beyond Europe. Turkey, for instance, has close economic ties with the countries in Central Asia.

Table I.4: FDI Inflows, 2003-04

Country	FDI as % of GDP*			FDI per capita (Euro) 2004***	Cumulative FDI inflows in % of GDP 1988-2004	FDI as % of fixed capital formation 2003
	2003*	2003**	2004**			
Albania	2.9	3.2	4.5	440	18.7	--
Bosnia&H	3.2	5.5	7.3	390	18.9	24.6
Bulgaria	7.1	10.5	8.3	740	35.0	33.7
Croatia	6.9	7.4	3.6	2370	32.2	25.7
Macedonia	1.0	2.1	2.9	590	22.2	38.5
Moldova	3.0	4.0	5.5	--	38.0	50.2
Romania	3.2	3.9	9.0	600	16.9	--
Serbia&M.	-	7.7	4.4	700	15.6	37.6
Slovenia	1.2	0.9	2.6	2760	19.5	xx
Turkey	0.6	0.7	0.9	xx	6.1	xx
<u>For comparison :</u>						
Czech Republic				4120	43.8	
Hungary				4660	43.4	
Poland				1230	26.1	
New EU members (8 countries)				2280		
CEE						13.9
World						9.8

Sources: * UNDP-HDR 2005; ** UNCTAD World Investment Report 2004, p.73; UNECE; *** WIIW;

Increasing volumes and per capita rates of inflow of *foreign direct investment (FDI)* to SEE are a further sign of advancing economic integration, albeit the level of cumulative FDI is still comparatively modest in most of SEE, compared to countries like the Czech Republic and Hungary (Table I.4). In the wake of FDI flows, the region gets more deeply immersed in the international division of labour. It becomes part of transnational production networks and value adding chains. As these are organized and governed by transnational companies, national governments tend to lose autonomy to run the national economies.

Moreover, SEE countries have become more internationally integrated in institutional terms, by being affiliated with regional and global organizations. Table I.5 shows that each of the SEE-11 countries is a member of the ILO, the World Bank Group, and the International Monetary Fund (IMF). All countries except Bosnia&H and Serbia&M hold membership in the World Trade Organization (WTO). Barring Bosnia&H, each country belongs to the Council of Europe. All countries except Turkey, Greece and Slovenia are covered by the Stability Pact for South-East Europe. Greece and Turkey belong to OECD, Moldova is member of the Commonwealth of Independent States (CIS). Greece became a member of the European Union in 1981 when the Union expanded its Southern rim. Slovenia joined the EU in May 2004, and will be part of the EURO-zone from January 2007. All other SEE countries look for accession to the EU which implies the free flow of goods, services, capital and people – with some restrictions on the mobility of labor. To date, the EU is the most integrated region in the world, both in economic and political terms. Romania and Bulgaria are expected to join the EU in 2007. Croatia and the Former Yugoslav Republic of Macedonia are EU candidates. Turkey has started negotiations about membership. A Stabilization and Association Agreement between the EU and FYR Macedonia entered into force in April 2004. The EU Commission has begun talks with Albania, Bosnia and Herzegovina, and Serbia and Montenegro that are to lead to similar agreements. Progress on integration will be conditional on the prospect of the candidate countries reaching EU standards, including employment and social standards (« Standards » before « Status »).

Table I.5: Membership of SEE countries in International Organizations or Regional Cooperation Frameworks, 2004

Country	ILO	WB	IMF	WTO	Council of Europe	EU	OECD	CIS	SEE Stabil.Pact
Albania	x	x	x	x	x				x
Bosnia&H	x	x	x						x
Bulgaria	x	x	x	x	x				x
Croatia	x	x	x	x	x				x
Greece	x	x	x	x	x	x	x		
Macedonia	x	x	x	x	x				x
Moldova	x	x	x	x	x			x	x
Romania	x	x	x	x	x				x
Serbia&M		x	x		x				x
Slovenia	x	x	x	x	x	x			
Turkey	x	x	x	x	x		x		

Source : ILO 2005a, p. 64

Membership or institutional association with international organizations facilitates and promotes integration of SEE countries into the European economy, respectively the global economy. It can to some extent offset the process of political and economic disintegration that marked former Yugoslavia during the 1990s. International institutional integration makes a country subject to international rights and obligations and, in some cases, conditionalities as we shall see below.

II. Employment and Development

1. Statistical Profiles and Trends

Economic Growth

Turkey and Albania enjoyed respectable, but highly volatile, economic growth during the last 15 years. Despite a major fall of output during successive economic crises, the *average annual rate of real GDP growth* in the two countries was far above average world growth in the 1990s, and also in the 2000-04 period. Slovenia had fairly steady annual GDP growth around 3 %. Greece experienced significant growth of its national product after 2000. The remaining countries showed conspicuously varying growth patterns since 1990 (Table II.1). Because of transition from centrally planned to market economies and armed conflicts in the West Balkans, they suffered economic decline in the 1990s. In the second half of the 1990s, all SEE-11 economies, except Bulgaria and Romania, turned to positive growth, and from the year 2000, the national product in each economy increased substantially, except in FYR Macedonia where growth remained modest. For 2000-04, average increase of GDP in the eight Stability Pact countries was 5 %. This rate of growth sounds impressive, but it must be seen against the low base from which the economies took off after the large shrinkage before the 1990s.

Table II.1 : Real Gross Domestic Product: Rates of Change

Country	Real GDP Annual Growth (%)					Cumulative Change 1989-2004
	1990-2000	1995-99	2000-04	2003	2004	
Albania	3.5	5.3	5.4	5.7	5.9	30.1
Bosnia&H	--	22.9	4.9	3.2	4.0	229.9*
Bulgaria	-1.8	-0.8	4.8	4.5	5.6	-8.0
Croatia	-1.6	3.4	4.5	4.3	3.8	-5.3
Greece**	2.2	--	4.3	4.7	4.2	49.5
Macedonia	0.8	3.0	0.7	2.8	2.9	-16.5
Moldova	-9.6	--	7.0	6.6	7.3	-55.6
Romania	-0.6	-1.3	5.9	5.2	8.3	0.8
Serbia&M	-1.5	0.4	4.7	2.1	8.0	-46.3
Slovenia	2.7	--	3.2	2.5	4.6	--
Turkey	3.8	--	4.2	5.8	8.9	78.7
SEE Stability Pact countries (without Moldova)***		-2.9	5.0	4.9	4.2	-6.5
EU-25***					2.4	
World***		2.9	2.5			

Sources: World Bank, World Development Indicators 2006, Table 4.1 ;

UNECE, Economic Surveys of Europe, No. 2/2005, Tables 4.2.1 and 5.2.1, Appendix B.1

* 1995=100 ** 1992-2004 *** Aggregation of countries is performed on weights based on purchasing power parity

In five of the SEE Stability Pact countries, namely Bulgaria, Croatia, FYR Macedonia, Moldova and Serbia and Montenegro, real GDP in 2004 remained below the 1989 level (Table II.1). Actual growth must also be judged in relation to potential growth, indicated inter alia by the size of the population. Between 1990 and 2004, the *size of the resident population* increased strongly in Turkey and moderately in Greece and FYR Macedonia. It shrank in the other seven SEE countries, partly due to mortality rates exceeding birth rates (as in Bulgaria, Croatia, Moldova, Romania and Serbia&M), and partly due to high rates of emigration. Projections of population change from 2004 to 2015 indicate a declining number of residents in five countries, and growing population size also in five SEE countries. The forecasted increase for Turkey is 13 %,

that for Serbia&M 32 %. (Table I.1). Thus, some countries in the region face a young and growing population, while others are confronted with a declining and ageing population.

Labour Force and Employment

In stark contrast to the increasingly positive growth performance, the state of the labour market in most of SEE-11 looks bleak. All Stability Pact countries recorded a volume of employment in 2004 substantially below its level in 1989. The range of loss was between 21 % in Serbia&M and close to 50 % in FYR Macedonia (Table II.2). Not counting Moldova, the average decline was 28 % (UNECE 2005b, Appendix Table B.5, p. 73). Some of the shrinking employment can be explained by the loss of output in the early transition phase. Yet, except in Croatia, the atrophy of jobs continued in the second half of the 1990s and the years after 2000, when the economies had recovered and GDP growth was thriving. In the period 2000-04, the number of employed persons diminished in Albania, Bosnia, FYR Macedonia Romania, and Serbia&M. In Bulgaria and Croatia employment increased, yet this growth fell much short of the rates of growth of GDP. In Turkey, the number of recorded jobs in 2004 was 17 % higher than in 1989, but between 2000 and 2004, mainly due to the 2001 economic crisis, the country saw its employment shrinking by 0.8 % (according to UNECE data) or 1.8 % (according to EUROSTAT). In the same period, Turkey's population aged 15-64 increased by 7.1 %. Greece and Slovenia registered job growth during the 1990s and thereafter.

Table II.2: Change of Total Employment

Country	2004 over 1989	1995- 1999	2000- 2004	2003 LFS*	2003 Establ.**	2004 LFS*	2004 Establ.**	2000-04 Establ.**
Albania	-35.3	-1.6	-2.7	--	0.9	--	-0.4	-3.1
Bosnia&H	-38.5	30.2	-1.0	--	-1.7	--	0.2	-1.0
Bulgaria	-25.9	-1.9	1.1	3.4	6.9	3.1	2.7	1.0
Croatia	-25.8	2.3	0.7	0.6	3.2	1.7	1.9	0.7
Greece	14.3ç	--	0.7	--	1.4	--	3.1	0.3
Macedonia	-49.8	-2.7	-3.9	-2.9	-4.4	-4.1	-5.4	-3.9
Moldova	-24.2	--	--	-9.9	0.4	-3.0	-0.4	-2.5
Romania	-28.2	-0.4+	-1.7	-0.1	0.1	-0.7	1.0	-1.6
Serbia&M	-21.4	-1.2	-0.9	-4.5	-1.3	--	0.7	-0.9
Slovenia	0.3ç	0.2	0.6	-0.4	--	5.1	--	--
Turkey	17.2	--	-0.8	-1.0	--	2.0	--	-0.6

Source : UNECE, Economic Survey of Europe, 2005/2, p.73

*Labour Force Survey data

**Establishment based data

+ 1996-99

ç 1994-2004

For comparative purposes, the level of employment is of limited value unless it is related to other indicators of employment. The number of recorded jobs varies for several reasons, including the size of the population, the size of the labour force, the demand for labour, the population's health and educational attainment, and labour market regulation. In order to take account of these factors, various numerical (key) indicators are available:

- The *rate of labour force participation* measures the proportion of a country's labour force (employed and unemployed) at working age (15 years and older; or age 15-64) that is

economically active. It provides an indication of the relative size of the supply of labour available for the production of goods and services. The inverse indicator of labour force participation is the inactivity rate.

- The *employment-to-population ratio* (also called *employment rate*) is defined as the proportion of an economy's working age population that is employed. It is equal to the labour force participation rate after deducting the unemployed from the numerator of the rate. It provides information on the ability of an economy to create jobs.
- The *unemployment rate* indicates the proportion of the labour force that does not work but is available and actively looking for work. Its value as an indicator is diminished by the extent to which employment is informal, or workers have no incentives to report their unemployment, or employed workers have an incentive to register as unemployed to get access to social benefits.
- The *rate of informal employment* measures employment in the informal economy as a percentage of total employment. The informal economy comprises household enterprises, informal own-account enterprises, and enterprises of informal employers. Where the proportion of informal employment is large, the indicative value of the the rates of employment and unemployment is diminished.

The *labour force of age 15+* increased in Greece, Turkey and Slovenia in the the period 1990-2004. It stagnated or declined in the remaining SEE-11 countries. The *rate of labour force participation (age 14-65)* diminished for both men and women in Albania, Bulgaria, FYR Macedonia, Moldova, Romania, Serbia&M, Macedonia and Turkey. In Bosnia&H, Croatia, and Slovenia, labour force activity declined for men, but increased for women. In Greece, labour force activity rose for both sexes. In 2004, labour force participation of men in each SEE economy was below average global and middle income country levels. Women labour force activity could match these benchmarks some SEE countries (Table II.3). In Bosnia&H, labour force activity increased since 2001.

Table II.3: Labour Force Activity (Participation) of Working Age Population

Country	Rate of Participation of Labour Force (age 15-64)				Percentage growth of Labour Force (15+) 1990-2004
	Male		Female		
	1990	2004	1990	2004	
Albania	86.3	76.4	63.3	55.1	-1.0
Bosnia&H	82.4	78.3	66.1	69.4	-0.7
Bulgaria	77.8	63.0	72.3	53.3	-2.5
Croatia	76.9	71.4	55.0	57.4	-0.9
Greece	76.7	78.6	43.1	54.8	1.4
Macedonia	77.5	73.2	52.8	47.8	0.1
Moldova	81.5	75.8	70.4	65.4	0.0
Romania	77.2	68.8	61.1	55.6	-0.4
Serbia&M	77.0	75.9	54.9	53.3	0.0
Slovenia	76.9	75.2	63.3	66.1	1.3
Turkey	84.5	80.3	36.2	29.0	1.7
Middle Income Countries	85.8	84.3	64.0	62.7	1.4
World	85.5	83.9	58.9	57.8	1.6

Source : World Bank, World Development Indicators 2006, Table 2.2

The *aggregate employment rate* declined in the majority of SEE nations. Decline was reversed in Bulgaria and Croatia in 2002, and in Turkey in 2004 (Table II.3). In Bosnia&H, the employment rate increased from 40 % to 46 % in the period 2001-04 (World Bank 2005b). In the latter country, however, both labour force participation and employment continue to trail population growth. In almost all SEE countries, employment-to-population ratios remained much below the average of the EU, which in 2003 amounted to 64,4 % total, 72,6 % for men, and 56 % for women. The gap is particularly large for FYR Macedonia where the aggregate employment rate reached the 40 % mark only during a few years. The SEE ratios also missed by a large margin the EU target rates set for 2010 (now called “Lisbon” rates), which are 70 % in total, more than 60 % for women, and more than 50 % for persons aged 55-64 years. Slovenia is once more exceptional. It already reached the EU target for women employment by 2004 by attaining a rate of 60.5 %, and is within 5 percentage points of the EU target of the total employment rate (Table II.4).

Table II.4: Rates of Employment between 1996 and 2004

(Number of employed persons in % of working age population 15-64)

Country	1996	1997	1998	1999	2000	2001	2002	2003	2004
Albania									
Total	60.3	59.0	57.0	56.0	55.1	52.1	52.1	51.1	
Male	72.6	74.0	71.0	69.0	66.0	64.0	63.9	62.6	
Female	47.9	45.0	43.0	42.0	44.1	39.6	39.7	39.1	
Bulgaria									
Total	54.0	54.1	53.7	51.2	49.9	49.2	50.6	52.5	
Male	57.7	58.0	57.5	55.1	53.6	51.8	53.7	56.0	
Female	50.4	50.3	49.9	47.5	46.3	46.8	47.5	49.0	50.7
Croatia									
Total	61.6	59.5	58.1	55.4	53.2	51.6	53.1	53.1	54.7
Greece*									
Total	55.0	55.1	56.0	55.9	56.5	56.3	57.7	58.7	59.4
Male	72.7	72.1	71.7	71.7	71.5	71.4	72.2	73.4	73.7
Female	38.7	39.3	40.5	41.0	41.7	41.5	42.9	44.3	45.2
FYR Macedonia									
Total	41.7	38.7	40.3	40.8	40.8	42.6	40.4	38.5	
Male	52.7	49.8	50.7	50.2	50.4	50.6	48.6	45.6	
Female	30.7	27.9	29.8	31.2	31.3	34.5	32.0	31.3	
Romania									
Total	65.5	65.9	64.2	63.5	63.3	62.6	57.6		
Male	72.6	72.8	70.9	69.6	69.1	68.2	63.6		
Female	58.4	59.3	57.7	57.7	57.1	51.8	51.5	52.3	
Serbia&M**									
Total	51.3	49.5	50.4	49.6	50.0	49.9	48.5	47.4	
Slovenia									
Total	61.6	62.6	62.9	62.2	62.8	63.8	63.4	62.6	65.3
Male	66.0	67.0	67.2	66.5	67.2	68.6	68.2	67.4	70.0
Female	57.1	58.0	58.6	57.7	58.4	58.8	58.6	57.6	60.5

Turkey									
Total				54.5	48.9	47.8	46.7	45.5	46.1
Male				76.9	71.7	69.3	66.9	65.9	67.9
Female				32.9	26.2	26.3	26.6	25.2	24.3
EU-15									
Total	60.3	60.7	61.4	62.5	63.4	64.1	64.3	64.4	64.7
Male	70.4	70.7	71.3	72.0	72.8	73.1	72.8	72.6	
Female	50.2	50.8	51.6	52.9	54.1	55.0	55.6	56.0	
EU-25									63.3

Sources : Eurostat; OECD-Employment Outlook 2005, Appendix.

* Working population aged 15-64; ** Employment rate for males: 15-64 years; for females: 15-59 years ;

Unemployment

The level of unemployment in most SEE countries is high. LFS-based *rates of open unemployment* are double-digit except in Romania and Slovenia. Rates of joblessness in Bosnia&H (nearly 45 %), FYR Macedonia (37 %) and Serbia&Montenegro (27.5 %) are among the highest worldwide. Compared to 1997, unemployment in 2004 was lower in Bulgaria, Croatia, and Slovenia, and higher in Bosnia&H, FYR Macedonia, Romania, and Serbia&H (Table II.5).

Table II.5: Rates of Unemployment (in % of Labour Force 15+)

Country	Aggregate			Gender			Youth (15-24)		Long-term unemploy.*		
	1997	2000	2004	Male	Female	Total	Male	Female	Male	Female	Total
				2000-04			2000-04		2000-04		
Albania	14.9	16.9	14.4	13.1	18.3	15.2	42	27	--	--	--
Bosnia&H	39.0	39.4	44.9	--	--	--	--	--	--	--	--
Bulgaria	14.4	16.7	11.7	14.1	13.2	13.7	31	25	--	--	--
Croatia	17.6	16.1	13.6	13.1	15.7	14.3	35	40	--	--	56.4
Greece	--	--	10.5	6.4	15.9	10.2	19	36	49.2	61.0	56.5
Macedonia	36.0	32.2	37.2	37.0	36.3	36.7	65	67	--	--	64.8**
Moldova	--	--	--	9.6	6.4	7.9	17	13	--	--	--
Romania	5.3	6.8	7.6	7.5	6.4	7.0	18	19	--	--	--
Serbia&M	25.6	26.6	27.5	14.4	16.4	15.2	--	--	--	--	82**
Slovenia	6.9	6.6	6.0	6.2	6.6	6.6	3.4	3.6	13.7	18.0	15.5
Turkey	--	--	10.3	10.5	9.7	10.3	20	19	37.0	45.6	39.2
EU-25	--	8.6	9.0				18	19			
EU-15	9.8	7.6	8.1						41.5	43.3	42.4
OECD									31.9	32.0	32.0

Sources: OECD, Employment Outlook 2005, Table G; World Bank, World Development Indicators 2006, Table 2.5; EU, Employment in Europe 2005 * more than 1 year unemployed **Cazes and Nesperova 2006

Unemployment rates for women are in excess of those for men in Albania, Croatia, Greece, Serbia&M, and Slovenia, and lower for women compared to men in Bulgaria, Macedonia,

Moldova, Romania, and Turkey. Rates of *youth unemployment* in SEE are high by international standards. Extremely high rates were recorded for young women in Macedonia (67 %), Croatia (40 %) and Greece (36 %) in the period 2000-04. In 2002, according to data listed in CREPs, youth joblessness in the Stability Pact countries in 2002 was 22.4 %, compared to 14.5 % in the EU-15 and 30.7 % in the EU-10. In Serbia, youth joblessness stood at 48 % (see CREP for Serbia). Data on *long-term unemployment* in SEE countries are not available for a number of countries. Long-term unemployment as a percentage of total unemployment averaged more than 56 % in Croatia and Greece, and 24 % in Turkey in the 2000-04 period (Table II.5).

In some SEE countries, *rates of registered unemployment* are higher than LFS-derived rates (Table II.6). One reason for the gap is that a number of workers register their joblessness in order to have access to health and other public social benefits.

Table II.6 : LFS-based and Registered Unemployment Rates

Country	2003		2004		
	LFS	Registered	LFS	Registered	
Albania	--	15.0	--	14.4	
Bosnia&H	--	44.0	--	44.9	
Bulgaria	13.7	13.5	12.0	12.2	
Croatia	14.3	18.7	13.6	18.5	
Greece	9.7	--	10.5	--	
Macedonia	36.7	45.3	37.2	45.6	
Moldova	7.9	1.2	8.1	1.4	
Romania	7.0	7.4	8.0	6.2	
Serbia&M	20.8	28.0	--	--	
Slovenia	6.7	--	6.3	--	
Turkey	--	10.5	--	10.3	--

Source : UNECE, Economic Survey of Europe, 2005/2, p. 34.

Informal Employment

Informal (or unregistered or undeclared) employment is high in large parts of SEE. In some countries it tends to exceed the level of employment in the formal economy. Unfortunately, statistical data on this indicator is incomplete and varies significantly depending on the definition and source of the information. In Turkey, for example, the share of informal employment in year 2000 was 9.9 % according to the national definition, and 50.9 % according to the harmonized definition used in the HLFS (ILO-KILM 2006). The first measure excludes agriculture, the second excludes paid domestic workers. By the third quarter of 2004, unregistered employment in Turkey had risen to 55.4 %. The 1999 HLFS for FYR Macedonia put the level of informal employment at 28 % of total employment, while other sources quote a rate of 60 % (Novkovska 2006). The share of informal jobs in Serbia is estimated at between 31 and 35 % (see CREP report). The recorded percentage of informal employment is 30.4 in Bulgaria, 24.3 % in Romania, and 14.5 % in Moldova. The figures relate to different years between 1999 and 2004, measured at varying years after 1999 (Table II.7). Most of the recent gains in employment in Bosnia&H came from the informal sector, whose share increased from 37 % in 2001 to more than 42 % in 2004. (World Bank 2005b, p. 1 and 5).

The proportion of informal employment in SEE exceeds those in Central European countries.

In 2000, both the Czech Republic and Slovakia recorded 19 %, and Hungary 25 % informal employment (Gligorov et al. 2003).

Table II.7: Size of Informal Economy and Informal Employment

Country Year	Share of Informal Economy (% of GDP)		Share of Informal Employment (%)
	National accounts discrepancy method	Currency demand method	
Albania (2002)	28	35	--
Bosnia&H (2003)	53	37	42
Bulgaria (2003)	22	38	30.4
Croatia (2000)	7	35	11.8 (2002)
Greece	--	--	--
Macedonia (1999)	14	36	28*
Moldova (2000)	31	49	--
Romania (2000)	21	37	24.3
Serbia&M (2004)	35	39	--
Slovenia	--	27**	--
Turkey	--	--	50.9***
OECD		16	

Sources : UNECE, Economic Survey of Europe, 2005, No. 2, p. 24 * Cazes and Nesporova 2006
 ** Gligorov et. al. 2003 ***KILM 2006 (harmonized definition)

For a number of countries in the region we know the share of the informal economy as a percentage of GDP (see Table II.7). For the year 2000, the highest relative values of informal activities were recorded for Moldova (49 %), Bulgaria (38 %), and Bosnia&H, Albania and Croatia (between 35 % and 38 %). Several CREP reports indicate that employment and income related to the informal economy have been on the upturn. The shares of the shadow economy in SEE countries run much higher than in the average OECD country (= 16 %).

Migration

Next to seeking work in the informal economy, leaving the country to find employment abroad is a prevalent response of workers to unemployment or unsatisfactory job offers at home. Where public income support for the jobless is low, outmigration may be seen as a survival strategy of workers.

Statistics on the incidence of outmigration of labour from SEE in recent years is scant and scattered. For some countries we know only the volume of total migration. But it can be safely assumed that the majority of the emigrants are labourers. According to the Turkish Ministry of Labour and Social Protection, an estimated number of 3.5 million Turkish citizens, i.e. close to 5 % of the population, are living abroad (http://www.calisma.gov.tr/yih/yurtdisi_isci.htm). The 2004 migration survey of Moldova yielded that in addition to the 400 thousand migrants (over 10 % of the population), an estimated 171 thousand Moldovans had worked overseas in the years before and intended to leave again. Another 119 thousand families surveyed intended to send members abroad within six months of the survey, bringing the total migrant potential to 690,000, out of an economically active population in the country of approximately 1,5 million (World

Bank, Moldova at a glance, 2005-06, May 2005) According to the Albanian Population and Housing Census of April 2001, the share of emigrants was estimated at about 25 % of the population. Ninety % the emigrants left for economic reasons. Fifty % of the migrants were illegal and had no employment contracts (Hana and Telo 2004, p. 27-28). Another source claims that between 400 thousand and 800 thousand Albanians were working abroad in 2003, most of them in Italy and Greece (EIU Albania country Profile 2004). The estimated share of Albanian labour migrants amounts to between 55 % and 73 % of the domestic labour force registered in 2003. Many migrants were among the young and most productive workers. The country is said to have lost 40 % of its university professors and researchers (Vidovic 2005). An outflow of young and qualified workers was also reported for FYR Macedonia. **Does Sandrine have figures on Macedonia ????** The National Statistical Office of Bulgaria reported that about 9 % of the population of that country emigrated between 1989 and 2004. The predominant reason for leaving the country was economic hardship. Nearly two thirds of the emigrants were male, well educated young persons, many of them holding tertiary education degrees (as compared to earlier periods when proportionately more migrants were poorly educated). It was found, moreover, that 43 % of young people aged 18-30 were willing to migrate; because of the emigration of skilled workers, the Bulgarian economy could not be upgraded to higher value-added activities as desirable; the acquisition of vocational skills of emigrants abroad was small because many worked below their educational level in menial jobs, such as care for children and the elderly, housekeeping, agriculture and construction; and finally, the drain of workers discouraged increases in investment in education and VET because of the risk of losing the return to the investment at home (Rangelova and Vladimirova 2004, p. 7-30).

Evidently, emigration has aggravated the skill and age structure of the domestic labour forces in SEE. The emigration of young and highly skilled labour has become a serious concern. Six of the eight Stability Pact countries have expressed worries that their emigration levels were too high (ILO 2005b, p. 79).

Quality of employment

Data on measures of the *quality of employment and conditions of work* is largely missing. There is scattered information in the CREP reports. There are hints of labour market segregation and discrimination in employment and occupation on grounds of sex and ethnicity. A summary indicator of the disadvantaged status of women in the labour market is the *ratio of female to male earned income*. The values are as follows: Albania 0.56 ; Bosnia&H 0.46 ; Bulgaria 0.67 ; Croatia 0.56 ; Greece 0.45 ; FYR Macedonia 0.56 ; Moldova 0.65 ; Romania 0.58, Slovenia 0.62, and Turkey 0.46. These values can be compared to benchmark ratios for the following best performing countries in Europe: Norway: 0.75 ; Finland 0.72 ; and Sweden 0.69 (see Table II.10 below). It can be concluded that gender based labour income equality in Bulgaria and Moldova is not far off the best performers in Europe while Bosnia&H, Greece and Turkey are considerably behind.

Information on *child labour* is available for Albania, Moldova, and Bosnia&H. In these countries, the share of children of age 7-14 that were economically active in the year 2000 amounted to 36.6 %, 33.5 %, and 20.2 % respectively. Of those children in Albania that were active, 43.1 % worked without attending school, whereas 56.9 % combined work and study. The respective figures for Moldova were 3.8 % and 96.2 %. For Bosnia&H, the proportions were 4.0 % and 96.0 %, and for Turkey 66.8 % and 33.2 % respectively. (World Bank, *World Development Indicators 2006*, Table 2.4).

Since the beginning of the 1990s, some of the region's countries have seen a rapid increase in the *trafficking of persons* for the purpose of sexual exploitation and forced labour. For example, women from Albania and Moldova have been deceived about job opportunities abroad and forced into prostitution. Children are trafficked for various purposes, such as begging, street vending and prostitution (ILO 2005b, p.79). A report on coercive trafficking in Bosnia&H found that this country had emerged as a significant destination for women trafficked from nearby countries, especially Moldova, Romania and Ukraine. Other types of forced labour or debt bondage remain hidden in the grey areas of the economy (See *Trafficking in human beings in Bosnia&H.*, Summary Report of the Joint Trafficking Project of the UN Mission in Bosnia&H and the Office of the High Commissioner for Human Rights, May 2000).

Hardly any statistical data exists for SEE on daily, weekly and annual *hours of work*, and other indicators of terms of employment and working conditions.

Wages and labour productivity

Nominal monthly wages and labour productivity, measured in terms of GDP per employed person, vary greatly across SEE countries. In 2004, they were substantially below levels of Central European countries. Exceptions include Croatia whose labour productivity is comparable to that of the Czech Republic and Hungary, and whose wages are above the plateau of the Central European countries, and Slovenia whose productivity level is nearly one third higher than that of the CEE countries and more than three times that of Albania. Slovenia's level of wages is more than twice that of the CEE countries (see Table II.8). *Average annual earnings* in Bulgaria in 2002 were just below 5,000 Euros, whereas in Romania they had reached just over 5,000 Euros. This compares with an average level of over 30,000 Euros in the EU-15, a value of 33,500 Euros in Germany, and 37,200 Euros in Luxembourg, the top wages in Europe (see : European Commission 2005, p. 167). The earnings were measured using purchasing power parity (PPS), a unit which reflects differences in national price levels. **Add Greece and Turkey**

Table II.8: Wages and Productivity, 2004

Country	Actual monthly Wage (US \$)	Average Net Nominal Wage Increase 2000-04 (%)	GDP at PPP per Employed (US \$)
Albania	236	71	17,417
Bosnia&H	475	35	27,600
Bulgaria	190	29	20,998
Croatia	992	28	37,800
Greece	xx	xx	xx
Macedonia	421	17	25,657
Montenegro		103	
Romania	253	37	19,261
Serbia	350	325	19,310
Slovenia	1,478		54,446
Turkey	xx	xx	xxxx
For comparison :			
CZ	701		37,047
Hungary	719		38,121
Poland	627		33,517

Source : Economist Intelligence Unit, Report on Serbia and Montenegro, Jan 2006 ; World Bank 2005, Appendix.

In 2004 and 2005, and also in the period 2000-04, nominal wages increased by sizeable margins in some of the SEE countries. Exorbitant wage hikes observed in Serbia and Montenegro (Tables II.8 and II.9 and CREP for Serbia&H). Moldova and Romania showed double-digit rates of nominal wage increase in 2004 and 2005. *Real wage growth*, however, was moderate during these two years, except in Moldova. In Turkey, real wages even declined by more than 2 % in 2004 and 2005. (Table II.9). *Labour productivity* increased by big margins, and more than wages, in Bosnia&H and Bulgaria, so that unit labour costs, both nominal and real ones, diminished. Turkey and Croatia registered a decline of real unit labour costs as well. Unit labour costs increases were large in Moldova and Romania, and much in excess of the growth rates of labour productivity. Real wage costs were rising in Moldova, and falling in nearly all other SEE countries. Nominal and real wages there grew at a very high rate, and in excess of productivity. Thus, Moldova sticks out as the country in the region that in the last couple of years faced a clearly adverse trend of its cost competitiveness. It should be stressed, however, that longer time periods of observation would be required in order to permit sound judgements on the movement and impact of wages and labour productivity.

Table II.9: Percentage Change of Wages and Unit Labour Costs, 2004 and 2005

Country	Nominal gross wages		Real wages*		L-Productivity		Unit labour costs		Real unit labour costs	
	2004	2005	2004	2005	2004	2005	2004	2005	2004	2005
Albania	--	--	--	--	-18.9	--	--	--	--	--
Bosnia&H	1.8	3.6	-0.6	1.7	15.3	--	-11.7	--	-13.7	--
Bulgaria	5.9	7.0	-0.1	0.7	15.5	8.9	-8.3	-1.8	-13.4	-7.5
Croatia	4.9	4.4	1.3	-0.6	3.4	1.0	1.5	3.3	-2.0	-1.6
Macedonia	4.0	2.9	3.1	0.6	2.6	--	1.3	--	0.4	--
Moldova	22.0	18.3	15.9	13.3	8.7	4.3	12.2	13.5	6.7	8.7
Romania	23.0	15.5	3.1	1.9	2.9	2.9	19.5	12.2	0.1	-1.0
Serbia&M	--	--	2.8	2.3	7.3	--	--	--	--	--
Slovenia	7.1	5.0	2.7	0.6	6.0	1.5	1.1	3.5	-3.1	-0.9
Turkey	12.1	8.0	-2.1	-2.6	7.6	1.5	4.2	6.4	-9.1	-4.1

Source : UNECE, Economic Survey of Europe, 2005/2, Table 3.3, p. 20; Eurostat;

*real product wages, defined as nominal wages deflated by producer price index.

The CREP on Croatia informs us that real wages in that country rose above GDP growth between 1994 and 2001, but below GDP growth thereafter. Serbia saw its real wage dropping due to the war in the late 1990s, followed by a strong rise until 2004 when the wage level was about twice as high as 1999 (see CREP). Wage dispersion is high. In some labour-intensive industries, pay is only about a quarter of the average wage in the economy. Real wages in Albania fell by almost 50 % in the early 1990s, grew between 1994 and 1996, fell again in 1997, and increased between 1999 and 2002.

Statutory minimum wages per month in 2003-04, in terms of purchasing power (PPP), amounted to less than 99 \$ in Moldova, between 100 \$ and 199 \$ in Albania, between 200 \$ and 499 \$ in Bulgaria, Croatia and Romania, and between 500 \$ and 999 \$ in Bosnia&H, Greece, Slovenia and Turkey (see ILO Minimum Wage Fixing data base, Eyraud and Saget 2005, p. 121; Eurostat

2005). In the SEE-12 region, Greece and Slovenia have the highest minimum wages of 3,86 Euro, and 3,03 Euro respectively (Eurostat, July 2006). In the SEE Stability Pact countries, the level of statutory minimum wages is in the order of between 15 % (in Moldova) and 55 % (in the Federation of Bosnia&H of average wages (World Bank 2005b, p. 12). They fall short of the normative standard of 60 % of average wages set by the European Social Charter. In Albania, the level of minimum wages declined heavily from 93 % of the average wage in 1991 to 44 % in 2001. In Turkey it increased from 34 % in 1999 to 42 % in 2004 (World Bank 2006b, p. 2-27). The legally stipulated minimum wage is not actually paid everywhere. In Bosnia&H, the minimum wage is not fully binding. About 20 % of the employees on formal employment report earnings less than the minimum wage. Evasion of the minimum wage floor is said to be high (World Bank 2005b, p. 19). In some of the SEE countries, social benefits are pegged to the level of minimum wages. This is the case for unemployment benefits in Greece and Romania, for pensions in Romania, for disability benefits in Bulgaria, Greece and Romania, and for special payments in Albania, Bulgaria, Greece and Romania (Eyraud and Saget 2005, p. 44-45).

Income inequality and poverty

According to the most recent World Bank Poverty Assessments, all Stability Pact countries are characterized by low incomes and a high incidence of poverty. Poverty may result from low employment rates, high unemployment, low productivity, low real wages, low minimum wages, wage arrears and high wage and income inequality. *Wage inequality* has reached extremely high levels in in Serbia (Rutkowski and Scarpetta 2005, p. 98). Table II.10 shows that in comparison with industrialized countries, *income inequality* is low in Slovenia, moderate in Albania, Bosnia&H, Croatia, Romania and Serbia, and high in Greece, Moldova and Turkey. This is indicated by the ratio of the richest 10 % to the poorest 10 % of the population, that of the richest 20 % to the poorest 20 %, and the Gini-index. Gini coefficients are below 30 for five of the SEE-10, comparable to the egalitarian EU countries. Greece, Turkey, FYR Macedonia and Moldova had Gini-values of .36 or .37, comparable to the UK and the US which are rated as countries with highly unequal income distributions.

Table II.10: Poverty and Income Inequality, 2004

Country	Year	Poverty Rate* in %	% Population below 2 \$ a day	Richest to Poorest 10 %	Richest to Poorest 20 %	Gini-Index	Ratio of Female/Male Earned Income
Albania	2002	23	11.8	5.9	4.1	0.31	0.56
Bosnia&H	2001	19	--	5.4	3.8	0.25	0.46
Bulgaria	2001	12	6.1	9.9	5.8	0.28	0.67
Croatia	2001	8	<2	7.3	4.8	0.29	0.56
Greece	1998	--	--	10.0	6.2	0.36	0.45
Macedonia	1998	11	<2	6.8	4.4	0.36	0.56
Moldova	2002	55	63.7	10.3	6.5	0.37	0.65
Romania	2002	33	12.9	8.1	5.2	0.28	0.58
Serbia&M	--	9	--	-	-	0.28	--
Slovenia	1998	--	--	5.9	3.9	0.28	0.62
Turkey	2000	28	18.7	13.3	7.7	0.37	0.46

For comparison :

Czech Rep.				5.2	3.5	0.25	0.64
------------	--	--	--	-----	-----	------	------

Poland	8.6	5.5	0.31	0.62
Norway	6.1	3.9	0.27	0.75
Germany	6.9	4.3	0.28	0.54
UK	13.8	7.2	0.34	0.62
US	15.9	8.4	0.38	0.62
EU-25	--	--	0.29	--
EU-15	--	--	0.30	--

Source : UNDP, Human Development Report 2005 ; EU-Commission 2005, p.123 ; World Bank, World Development Report 2006, p.280.

* Percentage of population below national poverty line.

According to Grigorov, income inequality in SEE has been on the rise in recent years (Grigorov 2005, p. 14). One of the empirically confirmed effects of greater inequality is that it diminishes the effectiveness of economic growth in reducing poverty (UNDP 2006, p.87). The share of the population below the national *poverty* line varies greatly between the SEE countries. It ranges from a low of 8 % in Croatia to a high of 55 % in Moldova. In the latter country, 63.7 % of the population lived on less than 2 US \$ a day in 2002 (Table 10).

Large and growing disparities of development

Looking at all eleven SEE countries together, we observe strikingly large differentials in the economic and social conditions. The inter-country development gap tends to be widening rather than narrowing. Moldova is clearly trailing the other countries. Its income inequality and poverty rate is substantially above the other SEE countries. Albania, FYR Macedonia, Bosnia&H and Turkey also exhibit salient features of developing countries, such as small modern sectors, large employment shares remaining in agriculture, a strongly negative trade balance and a negative balance of payments, high unemployment, large informal employment, low real wage levels, high rates of poverty, and large emigrant labour populations. The remaining three countries in the region are better situated in terms of the standard indicators, with Greece and Slovenia being well ahead of Croatia. Slovenia is the most advanced transition country in Europe, showing impressive values on nearly every socio-economic indicator. It sticks out positively on employment and unemployment rates, including those for youth and long-term unemployment, which are favourable compared to the majority of EU-15 countries. Slovenia has, furthermore, reached a standard of labour rights – including individual and collective rights and supervision of compliance – significantly superior to the average EU-25 country (van Gyes et. al. 2006).

Taking Greece and Slovenia apart, all SEE countries have in common a poor, and partly deteriorating, employment record and, in particular, low rates of employment, and high unemployment in the aggregate and for youth.

2. Jobless growth: Real or statistical illusion?

Recent studies on Central and Eastern Europe have shown that employment has been little responsive to economic growth (Rutkoswki and Scarpetta 2005; Cazes and Nesporova 2006). Measured by the *elasticity of employment in relation to output*, CEE exhibits the lowest employment intensity of GDP growth of all world regions after 1991. In the 1991-95 period, a change of 1 % of output was associated with a change of 0.24 % of employment. In the period 1995-99, the employment elasticity rate was down to 0.01, and in the 1999-2003 period, it fell to -0.19, signalling a steady decline of the employment intensity of growth (Table II.12). Also, unemployment has remained stubbornly high even when allowance is made for possible time

lags in the reaction to growth. UNECE found that there was hardly any statistical association between output growth and changes in unemployment in 2003-2004 (UNECE 2005b, p. 33).

Table II.12: Employment Elasticities, 1991-2003

Country	Total Employment Elasticity			Youth Employment Elasticity		
	1991-95	1995-99	1999-2003	1991-95	1995-99	1999-03
Albania	0.00	-0.65	0.66	-0.26	-1.38	1.15
Bulgaria	1.99	0.19	0.50	3.30	0.77	1.25
Bosnia&H	--	--	--	--	--	--
Croatia	0.33	-0.22	0.47	0.33	0.10	0.25
Greece	1.36	0.28	0.27	-0.11	-0.19	-0.62
FYR Maced.	0.75	-2.62	-3.54	1.05	-6.22	-7.59
Moldova	0.06	0.83	0.25	0.04	1.63	0.55
Romania	0.51	0.11	-0.13	0.36	0.97	-1.09
Serbia&H	--	--	--	--	--	--
Slovenia	1.49	0.14	0.05	4.85	0.41	-2.20
Turkey	0.37	0.06	-0.16	-0.24	-0.39	-1.15
<u>For Comparison:</u>						
Czech Rep.	-0.40	-0.31	-0.04	-0.57	-1.58	-2.88
Hungary	-0.02	0.29	0.03	0.33	0.56	-2.40
Poland	-0.29	0.09	-0.57	-0.57	0.00	-1.60
CEE	0.24	0.01	-0.19	0.00	-0.22	-1.26
CIS	0.19	0.28	0.18	0.22	0.35	0.15
Western						
Europe	-0.09	0.36	0.42	-3.38	-0.30	-0.35
Global	0.34	0.38	0.30	-0.02	0.11	0.06

Source: Kapsos 2005, Tables A.2.1 and A..2.3, pp. 31-33.

In the SEE region, by contrast, employment has been fairly elastic to GDP growth in some countries, but not in others. Elasticity values for Albania, Bulgaria, Croatia, Greece and Moldova were in the “normal” range, at least during part of the transition period. In Romania and Turkey, employment elasticity was small and negative in the period 1999-2003. During the economic crisis in Turkey in 1994, GNP fell by 6.1 %, but employment continued to grow (World Bank 2006b, p. 25). In 2001, GNP fell by 9.5 %, while employment shrank by 3.7 % until 2003 (according to EUROSTAT figures). In the years following the 2001 crisis, GDP expanded by a cumulative 25 % in real terms, and yet unemployment could not be reduced below the 10 % level. Apparently, agriculture acted as a safety net indicated by a sharp increase in agricultural employment in 2002. Jobless growth continued in 2003 and 2004, not merely in the aggregate economy, but in its subsectors (see Turkey Household Labour Force Surveys). In FYR Macedonia, the only country in the region with low GDP growth after 1999, employment declined strongly reflected in highly negative elasticity values (Table II.12). No elasticity figures are available for Bosnia&H and Serbia&M. Yet, available data show that in these countries employment declined despite recent economic growth (see Tables II.1 and II.2).

The low employment content of growth in CEE and part of SEE-11 has led analysts to speak of “jobless growth”. World Bank economists attribute this phenomenon to overprotected, rigid labour markets and “excessive” social benefits preventing adjustment of labour (Rutkowski and Scarpetta 2005, p. 172). This explanation, however, is hardly tenable since employment performance did not improve after protection standards were scaled down and new flexible forms of labour introduced in recent years (see details in chapter III). A cross-country study also found no evidence of a statistical link between job intensity of growth and the extent of employment protection legislation (Kapsos 2005, p. 25). It means either that EPL has no adverse impact on employment, or that this legislation is not enforced.

Several factors could account for the lacking correspondence between economic growth and employment where it occurred. They include:

- labour saving productivity increase, e.g. engendered by technological change, the reduction of labour hoarding, or conditioned by privatization and an increase of foreign direct investment;
- adjustment to changing labour demand through the variation of hours of work, instead of the number of employed persons; hence, total labour input may still be responsive to growth;
- growth of the informal economy, implying that economic growth translates into informal employment instead of (statistically recorded) formal employment;
- limited reliability of the recorded employment and unemployment statistics (both registered and LFS-based rates), and distorted statistical data on economic growth;
- the net effect of labour migration: migrant workers do not show up in the national employment statistics of their home country, but may add to national economic growth in that country due to income transfers.

Studies on the relative significance of each of these factors, and their interplay, in SEE are missing. At present, research is difficult to undertake because of the lack of time series of relevant indicators and irregular conduct of labour force surveys. For example, no regular time series are available about working hours, annual change of the size of informal employment and about worker movements between the status of formal employment, informal employment, and unemployment. In the computation of the employment elasticity figures presented above estimates of informal employment were included in the employment data. Values for missing years were imputed.

Still, there are hints that most of the factors above impacted either on GDP growth or employment and unemployment in SEE. In Turkey, for example, per capita GDP grew at an average annual rate of 7.6 % since 2001. However, part of this growth has been due to increased working hours rather than increased factor productivity (World Bank 2006b, p. 15). In some SEE-11 countries, employment and income related to the informal economy has been on the upturn (see CREP reports; Rutkowski and Scarpetta, 2005, p. 93 ff). Because of institutional regulation, official statistical data over- or underestimate the true extent of employment and unemployment. A major reason is that workers employed in the informal economy register as unemployed to obtain or maintain access to sickness and other social benefits. In some countries (e.g. FYR Macedonia) workers on fixed-term contracts also register as unemployed because otherwise they are excluded from health insurance. The institutionally distorted measures of employment and unemployment show up in the discrepancies of registered and household labour force survey (LFS)-based unemployment figures, and of LFS and establishment based data on employment. Workers employed informally or on short-term contracts who apply for social benefits although they are not legally entitled to will be unlikely to say in labour force surveys

that they are employed. Hence, even LFS data which are normally more reliable than data from establishment surveys can be misleading. As long as such biases in the measurement of labour market stocks exist we have no handle to accurately test the jobless growth theory. Also, the distorted employment measures call into question the reliability of other indicators, such as labour productivity which measures output per employed persons. For example, in Moldova, GDP calculated by the international financial institutions was judged way too high (McKinley 2006, p.16).

In some SEE countries, a good part of the disjuncture between economic growth and the employment dynamic may be explained by the net effects of labour migration and the earnings abroad remitted by workers to their home countries. Albania, Bosnia&H, Croatia, FYR Macedonia, Moldova and Serbia&M have received shares of remittances from their expatriate labour forces that are important in relation to GDP. Four of them can be termed *highly remittance dependent countries*. In 2004, transfers by Moldovan workers abroad made for 27,1 % of total GNI, the highest rate worldwide after Tonga. Bosnia and Herzegovina (22,5 %), Serbia and Montenegro (17,2 %) and Albania (11,7 %) follow in 5th, 8th, and 18th position of the list of the globally top ranking countries (Table II.13). As a source of foreign exchange the foreign earned income of Moldovans is equivalent to over 70 % of the country's exports and is over four and a half times the amount of FDI received. In Albania, Bosnia&H, and Serbia&M, remittances received were larger than total merchandise exports (Gosh 2006, p. 54).

Table II.13: Workers' remittances (in US \$, millions)

Country	1998	2000	2003	2005 Estimate	% of GDP 2004
Albania	504	598	889	889	11,7
Bosnia&H.	2048	1595	1745	1824	22,5
Bulgaria	51	58	67	103	0,4
Croatia	625	641	1085	320	3,5
Greece	-	2194	1564	1242	0,6
FYR Macedonia	63	81	171	171	3,3
Moldova	124	179	486	703	27,1
Romania	49	96	124	132	0,2
Serbia&M.	1033	1132	2611	4650	17,2
Slovenia	228	205	255	267	0,8
Turkey	5356	4560	729	804	0,3
Middle Income Countries					1,7
World					0,6

Source : World Bank, Global Economic Prospects 2006, Datasets ; World Bank Country Profiles, April 2006.

Next to the officially recorded remittances that go through national banks, it can be assumed that there are additional sizeable complements of unaccounted transfers. Remittances transferred through informal channels, or hand-carried by travellers, are not captured in official statistics. An estimate for Moldova says that of the total sum of remittances, 53 % were formal and 47 % were informal (World Bank 2006, p. 91).

Table II.13 shows, furthermore, that the *level of remittances* received by Turkey and Greece has decreased between 1998 and 2005. With the integration of second and third-generation migrants in the host countries, the flow of remittances declined. In terms of the total value of remittances,

Turkey ranked number 3 in the world in 1980, number 2 in 1995, and still number 4 in 2000, but fell to 17th place in 2002. From 2003 on, expenditure by migrants during visits to Turkey are entered under the heading of “tourists” in the national balance of payments.

In the majority of SEE countries, however, remittances have been increasing. In some countries, its value has doubled or tripled. If workers abroad add significantly to national income in SEE, and if these income transfers are large relative to GDP and growing over time, this will disconnect the dynamic of employment from that of economic growth. While there may be multiplier effects on employment through consumption and investment of the expatriate income, these effects may be too small to maintain a close link between employment and growth. For Bulgaria it has been reported that financial transfers from remittances were spent mainly on consumption, often of imported goods, so that the salutary effect on the domestic economy was lost (Rangelova and Vladimirova 2004, pp. 7-30).

In sum, there are reasons to caution against the proposition of ‘growth without jobs’, at least for part of the Balkan countries. Due to statistical measurement problems and the impact of labour migration, jobless growth may be a statistical illusion. Unemployment figures do not reflect the true magnitude of unemployment because of institutional distortions. Statistically recorded employment captures employment in the formal domestic economy, while blinding us on the job dynamic in the informal economy. SEE nationals working abroad contribute to national income through remittances. This shows up in GNI figures, and makes GNI exceed GDP, but it is not reflected in national employment accounts. In Moldova, the shadow economy and remittances together make up more than one half of GDP, and about three fourth of GDP if estimated undeclared remittances are added. In Albania and Serbia&M, the proportion contributed to GDP by the formal domestic economy is just over 60 %, and in Bulgaria, Croatia, Macedonia and Romania, it is between 60 % and 75 %.

III. Policies and Institutions

Although due to insufficiencies in the statistical data base we have to be sceptical about the recorded changes in employment and unemployment in SEE, it is undeniable that by international comparison labour force activity and employment rates are low and unemployment is high in most of the region’s countries. Transitional recession in the former planned economy countries and delayed restructuring in the war afflicted Western Balkans in the 1990s can account for only part of the disappointing employment performance. The plight of employment is persistent. The main explanation for it must be sought in the policy framework and in institutional arrangements.

Labour Market Flexibility and Social Protection: Orthodox economists usually attribute poor employment performance to imperfections in capital, commodity, housing and, above all, labour markets. Rigid labour markets, engendered by various types of statutory or contractual labour market regulations and social protection arrangements, would cause labour market distortions, stifle adjustment and lead to institutional sclerosis in the economy as a whole, all of which would impact negatively on employment. Their prescription therefore is to deregulate the labour market as far as possible. The virtues of an unfettered labour market, however, spring more from interested belief than from sound empirical research.

In SEE, excessive strictness of employment protection laws (EPL), lack of wage restraint in the public sector and generosity of social security provisions have been made responsible for lackluster results in the creation of jobs and sticking unemployment. Partly under pressure from

the international financial institutions (IFIs) that made financial and technical support conditional on labour market reforms, governments have scaled down employment protection to gain flexibility for employers. Periods of notice in case of layoff or dismissal were shortened, severance pay reduced, and temporary employment through fixed-term contracts and part-time work introduced or the scope of their use extended (for details, see the CREP reports for Croatia and Serbia). These measures were considered necessary to remove impediments for recruitment and unequal treatment of workers, such as privileging the insiders over the outsiders. Turkey forms a partial exception from the general trend. Next to enlarging the legal scope for subcontracting and temporary contracts, the labour code reform of 2003 provided greater protection of workers against unfair dismissal (World Bank 2006 b, chapter 4).

While it is true that in a number of SEE countries, especially the West Balkans and in Turkey, notice periods and worker compensation for dismissal, notably collective dismissal, were more generous, and rates of employer contributions for financing protection above those in other European countries (see Cazes and Nesporova 2006, p. 9; World Bank 2006, p. 4-64, Ghellab 2006), the reform measures taken have done little so far to improve labour market performance – a result also observed for CEE countries (Cazes and Nesporova 2006, p. 15). Worse, they have aggravated the serious deficits in the overall protection of workers against loss of job and income, and escalated the widespread perception of job insecurity. Feelings of insecurity induces workers to resist job change, leading to a low rate of labour reallocation and hindering finding a good match between the demand and supply of skills.

The negative impact of employment protection implied in standard economic theory tends to be exaggerated, whereas their positive effects are ignored or understated. Barring excessive protection standards, there is no clear empirical evidence from Western countries that less protection leads to more jobs or reduces unemployment (OECD 1999). Similar findings were obtained for CEE countries (Cazes and Nesporova 2006, p. 13). Various components of EPL (see ILO Convention 158 on Termination of Employment) have different impacts. The most elementary components, namely the requirements for the employer to inform employees about their upcoming layoff and providing justification for the action should be seen as part of any civilized labour market. There is no reason to believe that they are harmful to employment. On the contrary, feelings of unwarranted or unfair dismissal engender bad labour relations and do harm to productivity and innovation. On the other hand, long periods of notice and sizeable compensation may pose problems for adjustment if they increase the time and cost of staff adjustment to changing labour demand. They tend to reduce the rate of hiring and, at the same time, diminish rate of staff separations so that the net effect on employment is ambiguous. In the end, whether or not EPL creates barriers to adjustment, and how big these barriers are, depends on the type and functioning of labour markets. Those who stress the flexibility impairing effects of protective provisions usually assume that flexibility is accomplished when workers change their employer, their occupation, their sector or their location (see e.g. Rutkowski and Scarpetta 2005, p. 113). Such worker mobility is viewed as the predominant or exclusive mode of adjustment to changing demand. Yet, in reality, as ample research has shown, a good part of adjustment is achieved through adaptations *within* occupations, firms, industries, and locations. It happens when the firm adopts new products and processes, and the worker acquires new skills and competences to meet new operational requirements on site. This way, the employer keeps the incumbent, experienced work force. This is not to say that all labour reallocation can be realized through such “internal” flexibility in “internal labour markets”, yet this facility for adjustment should not be ignored or underestimated. It has clear advantages that are not without importance in an SEE context. Since the average length of service will tend to be greater under this regime of adjustment, there is more incentive for the employer to invest in training of the work

force simply because the return will be higher than in case of shorter employment spells. This has positive implications for functional flexibility, economic growth and competitiveness. Also, mutual trust between employers and workers increases with the duration of the tenure, a condition that can lubricate the willingness of workers to cooperate in the reorganization of production and work.

It should be mentioned just in passing that the presence or absence of employment security may have other repercussions on the economic and social performance of enterprises, such as the handling of grievances of staff. Fixed-term contracts will normally reduce the employee's propensity and chance of successfully voicing grievances because of the fear of not getting the work contract extended. Such contract vulnerability is a strong deterrent to formal and informal conflict resolution at work sites which in turn may significantly reduce productivity and innovative capacity of enterprises.

Granted that some excessive provisions of employment protection had to be relaxed in some SEE countries, overall worker protection standards in relation to restructuring of employment could have been maintained, and in fact improved, had the liberalization of EPL been compensated by action to raise the level of *income protection* of unemployed workers and to upgrade assistance to their re-employment. The failure to do so led to an overall weakening of safeguards against loss of jobs and income. It made it difficult for trade unions to accept the cut-backs of employment protection standards. Income support provided by unemployment insurance and support for re-employment in SEE are widely and seriously deficient. In terms of eligibility for unemployment benefits, the level of benefits, and the duration of benefit payment, legal provisions fall substantially short of European standards. In none of the Stability Pact countries does wage replacement of benefits reach 40 % of the national wage (Cazes and Nesporova 2006). Moreover, benefits are often not actually provided (partly because employers fail to pay contributions), or are not paid in time so that they cannot fulfill their functions of providing income security and job search efficiency. In Serbia, benefits are provided only after 6 months of unemployment. In several SEE states, only a small fraction of the jobless labour force – generally less than 10 % - is eligible for benefits. In Moldova, for instance, no more than 6 % of the unemployed receive benefits. In Albania, the share of benefit recipients is 6.5 % and the benefit level is low. While it is difficult to see that such poor unemployment compensation creates disincentives to work, as propagated by mainstream economics, they will surely entail undesirable effects: Firstly, meagre wage replacement for jobless workers fails to deliver its macro-economic function of stabilizing aggregate demand; in the absence of adequate income protection, jobless workers are likely to join the ranks of the poor; they will be prone to enter the informal economy to find new sources of income ; or they engage themselves in subsistence agriculture; or – that holds primarily for the young and educated – they leave the country temporarily or permanently to look for employment opportunities elsewhere. Each of these responses tends to be detrimental to countries' development.

In sum, most of the SEE-11 countries would benefit from higher protection standards than available at present, and some of them should consider a shift of worker security arrangements from the “protection of jobs” through EPL to “protection of workers” through strengthened unemployment insurance benefits and more active labour market policies, including enhanced redeployment services. The shift is particularly indicated for Turkey which according to the World Bank has the second highest EPL index and the lowest index of protection in terms of passive and active labour market policies among OECD countries (World Bank 2006c, p. 4/64).

In contrast to unemployment protection, some SEE countries provide good statutory standards of protection to vulnerable workers. For example, the labour law in Bosnia&H and Albania requires employers to grant women during pregnancy and after child birth 12 months of leave for each child. In Europe, this duration of maternity leave is reached only by Norway. FYR Macedonia provides 38 months, Croatia 30 months, and Bulgaria 25 months of maternity leave. In Bosnia&H, not all cantons are actually paying the maternity benefits (World Bank 2005, p. 59). More generally, there is a risk that faced with relatively high benefit provisions employers try to avoid hiring members of the protected groups.

In view of the reduced restrictions on termination of employment, the comparatively poor social security standards, and the relatively low minimum wages, it is unjustified to locate the main reasons for the unfavourable employment record in SEE in labour market regulation and social protection. The root problems must be sought elsewhere. This does not imply, however, that further reforms on labour market and protection policies should not be considered. Improvements of income protection standards are indicated in virtually every SEE country.

Monetary and fiscal policies: It is mainly with appropriate macro-economic policies that a country will be able to raise its employment and lower its unemployment. Their function is to stimulate aggregate demand, the decisive parameter for an economy's level of employment.

In SEE, the overriding policy target has been macro-economic stabilization. While in view of soaring consumer prices and large budget deficits in most SEE countries in the 1990s it was necessary to make efforts to achieve such stabilization, it can be argued that these endeavours have been overdone. They are being continued at a point in time when in the majority of countries consumer price inflation has been brought under control and budget deficits have been greatly reduced or eliminated (see Table III.1). In Turkey where core inflation was relatively high in the beginning of the present decade, price hikes were brought down to 8 % in 2005, with a predicted further decline to 4 % in 2007. Moldova and Romania are the only countries of SEE-11 where inflation rates are still double-digit. The average fiscal deficit in the Stability Pact countries (without Moldova) was estimated at 0.9 % of GDP in 2005, down from the 1.7 % of 2004. In Bosnia&H, a budget surplus was achieved in 2003 and 2004. Moldova ran a budget surplus of 1.6 % already in 2003 (McKinley 2006, p.2). In Serbia, a fiscal surplus is expected for 2006 and 2007. Nevertheless, austerity policy in these countries has not been relaxed. The stress on very tight, if not contractionary, fiscal policy forced governments to either run down public expenditure, or increase debt. In Moldova, for instance, expenditures in the consolidated public budget were drastically reduced by 40 % from 1997 to 2003. In terms of public spending, social welfare has been relatively more important than development (investment in infrastructure and economic services), yet this can be seen as an inevitable consequence of the high unemployment and persistent poverty. Cutting social spending in SEE would make it likely that informal employment and emigration resume, or grow even faster. Investment in the countries' future economic capacity is of the utmost importance, while underinvestment will cause long-term damage to development. Investments in human resources today help to avoid outlays for unemployment benefit payments tomorrow. The underutilization of labour resources that is evident from the data above translates into lower output and lower welfare.

Table III.1 : Macro-Economic Indicators

Country	Current Account		Balance of Transfers % of GDP 2004	Present Value of External Debt % of GNI 2004	Real Interest Rate 2003	Inflation (CPI)			
	Balance % of GDP 2004	2005				1990-2003	2003	2004	2005

Albania	-4.4	-5.0	13.6	17	10.0	19.2	0.5	2.9	2.5
Bosnia&H	-23.5	-23.9	22.2	34	9.6	-	-	0.3	2.8
Bulgaria	-8.5	-14.9	4.6	83	6.6	83.8	2.2	6.1	5.0
Croatia	-4.8	-3.8	4.3	110	8.1	52.8	0.8	2.1	3.3
Greece	-7.2	--	--	--	--	--	7.2	3.6	3.2
Macedonia FYR	-7.8	-0.9	14.7	39	14.0	7.1	1.1	-0.3	0.5
Moldova	-2.7	-5.5	--	75	4.8	17.8	11.7	12.5	11.9
Romania	-7.6	-8.9	3.2	51	--	78.7	15.3	9.5	16.3
Serbia&M	--	-9.0	15.3	77	--	--	--	7.5	2.8
Slovenia	-0.4	-0.9	--	--	5.5	10.3	5.6	3.6	2.5
Turkey	-5.1	-6.2	0.3	69	15.4	72.4	25.3	8.6	8.2

Source, UNDP, Human Development Report, 2005 ; UNECE, Economic Surveys of Europe, No. 2/2005
World Bank, World Development Indicators 2006, Tables 2.1 and 4.17; International Monetary Fund,;
*includes population of Kosovo

Macro-economic policies in SEE have been crafted in line with the simple world of orthodox textbook recipes, namely strict control of the money supply; the installation of currency boards; and exchange rate pegs (The majority of the countries are on fixed exchange rates). Under strong pressure from standby agreements with the International Monetary Fund, SEE governments continue to resort to excessively tight monetary policies and increasingly restrictive fiscal policies, with negative implications for growth and employment, spending on human resources policies, and in the end also equity and social cohesion. Among other things, mandatory reserve requirements for commercial banks have been kept high and have been raised in some countries in order to curb the growth of domestic credit. In addition, in countries like Serbia, the monetary authorities have actively engaged in open market operations to withdraw liquidity from the money market. The tight monetary policy, however, has contributed to a real appreciation of the exchange rate, which in turn impacts negatively on trade and current account balances (UNECE 2005b, p. 19).

Due to restrictive macro-policies, real interest rates in most of SEE have been high and have even increased in recent years, and credit has been low. Central banks constantly fear for the stability of the financial system (Gligorov 2005, p. 14). High real interest rates reduce capital investment which transition countries badly need to advance restructuring. Compared to the dynamic emerging economies in East and South East Asia, fixed capital formation in SEE has been small. Its share in GDP between 1990 and 2003 was less than 15 % in Serbia&M, between 15 % and 20% in Albania, Bulgaria, Croatia, FYR Macedonia, Moldova and Romania, whereas in most CEE countries it reached between 20 % and 30 %, and in the Asian emerging economies it amounted to between 30% and 35 % (Rutkowski and Scarpetta 2005, Fig. 3.6). True, investment picked up in some SEE economies during the last two to three years, but this was almost entirely due to FDI inflows to Bulgaria, Romania and Croatia in anticipation of EU accession. Turkey saw a rise of short-term speculative capital inflows in the wake of capital account liberalization, high real interest rates and an appreciating exchange rate. According to Turkish observers, the appreciated value of the Turkish Lira causes a surge in imports that increases the trade deficit and the current account deficit (which had reached 6.5 % in 2005). What is more, it engenders a contraction of labour intensive export industries that costs jobs in the formal economy and entails more informal employment (Telli et. al. 2006, p. 2). In Albania, Bosnia&H, Moldova and FYR Macedonia, growth came largely from foreign transfers, including high and rising levels of remittances making up between 12 % and 27 % as compared to GDP, and foreign aid amounting to more than 5 % of GDP in these countries (see World Bank

Development Indicators 2005). So, there is little reason to believe that the recent economic growth in these countries is the product of domestic capital accumulation.

A regime of high interest rates, moreover, discourages borrowing at home to finance investment, and encourages firms that seek access to international money markets to borrow abroad. As these domestic firms become more exposed internationally, their vulnerability increases due to growing external debt, which is often underwritten subsequently by the national government. With rising servicing cost of the debt, governments typically tend to get persuaded by the IMF to impose even more restrictive monetary and fiscal policies to compress import, resulting in shrinking growth and employment (Bhaduri 2005, p. 9).

Monetary stabilization in the region has also been excessive. There is no empirical evidence to show that lowering inflation below a moderate level increases growth. What sense does it make to steer the economy to zero-inflation targets and to attain budget surpluses, as is the case now for the most Stability Pact economies, when employment rates are extremely low and unemployment remains rampant, and when for lack of jobs workers quit their countries in large numbers? In Moldova and Albania, up to one half of the working population says in surveys that they consider leaving.

Finally, it is hard to justify persistent fiscal tightness by the alleged need to check an undue rise of real wages and total labour costs. As shown in Table II.9, nominal wages in 2004 and 2005 increased by double-digit rates in Moldova and Romania, but real wage hikes were over-sized only in Moldova. In the other countries for which we have data, real wage changes were small or negative. Thanks to productivity improvements (in the formal economy) – largely due to the reduction in overstaffing – real unit labour costs declined in all countries except Moldova. At least in some SEE countries, as for example in Turkey, the problem causing insufficient demand is rather the collapse of real household incomes as a result of declining real wages, inadequate social safety nets and shrinking employment. There is hardly any middle-income country in the world in which real wage increases fell so much behind productivity increases as in Turkey. In the period 1980-2000, labour productivity rose by 136 %, while real wages increased by a mere 26 % (see UNCTAD data base). More recently, Turkish real wages receded leading to a shrinking share of wages in total national income. Hence, real purchasing power and aggregate demand are depressed. If this combines with increases in working hours and related downsizing of staff, as it happened in Turkey's manufacturing sector in recent years, employment suffers. A higher trend rate of economic growth will be needed in order to reduce the unemployment rate which has reached 13 % in urban areas. In view of the rapid growth of the population and very low participation rates this will remain a major policy concern in the medium and long term. In urban areas, the employment rate fell to 38.4 %. Growing unemployment has been accompanied by a rise in poverty and the expansion of informal economic activities (UNECE 2004, No. 1, pp. 46-47).

In the face of shrinking labour income in a number of SEE countries, workers seek survival in the shadow economy. Since many jobs in that sector are of low productivity and no taxes and contributions are paid, a vicious circle of low income, low tax revenues, very limited public investment, low private domestic investment and weak domestic economic dynamism prevails.

The EU-members Greece and Slovenia represent clear cases of increases in real wages and simultaneous positive trends in employment. Real wages (nominal wages deflated by the consumer prices index) rose by an annual average of 3,4 %, respectively 2,6 % in 2002-06 (Eurostat, July 2006). In the period 2000-05, Slovenia's nominal wages increased 0.1 % less than the combined rise of consumer prices and productivity improvement. In other words, it used up almost exactly the distributional margin given by these two indicators, whereas Greece exceeded that margin by 1,8 % (European Commission 2006a).

Interestingly, countries in the EU-25 that exceeded the distributional margin (e.g. the UK) of price and productivity increases saw a positive development of employment, whereas countries that did not use up the margin (e.g. Germany, Poland and Slovakia) experienced negative employment trends (Schulten 2006, Table 4, p. 369).

It ought to be stressed that Slovenia has practised its balanced wage policy despite, or rather because, of being the only country in the EU-25 that has accomplished a rate of 100 % of coverage of wages by (predominantly branch-type) collective agreements and all agreements being generally applicable to all employers. On the employer side the agreements are negotiated jointly by the employers' associations and the chambers of commerce (see Van Gyes et al. (2006). Contrary to assertions by the international financial institutions, wage control in line with macro-economic developments is better achieved under centralized or coordinated collective bargaining than decentralized negotiations at the enterprise level.

In most part of SEE there is room for less monetary and fiscal restraint and more expansionary macro-policy instead. Demand can be raised and employment levels lifted by reducing interest rates and increasing public sector borrowing. As most SEE economies are saddled with onerous debt burdens (of up to 110 % of GNI), debt relief or debt restructuring is another option that should be applied notably to the region's poorer countries. To contain cost-push inflation, economic expansion has to be complemented by wage and incomes policies and labour market policies. Wages should not exceed rates of productivity increase in the long run, and sufficient worker training should ensure that the supply of skills keeps pace with demand.

Labour market policies: The function of labour market policies is to enhance the employability of the labour force and to promote the matching of supply and demand of labour, both in quantitative and qualitative terms. Supported by the ILO, EU Commission and national agencies of EU countries, progress has been achieved in the SEE Stability Pact countries in recent years to design labour market policies, form national labour market administrations and set up a system of public employment services, including labour market information systems, employer and worker counselling, placement services, targeted training and retraining, and direct job creation (see the CREPS for Albania, Croatia, Moldova, Macedonia and Serbia).

While there is room for further improvement of the functioning of SEE labour markets, and greater fit to national labour market structures, through national labour market policy reform, greater effectiveness of policies and institutions will now have to come primarily from their fuller implementation. As indicated above passive labour market policies geared to income protection of redundant and unemployed workers are widely inadequate. Rates of coverage for unemployment insurance benefits are extremely low, and have further declined recently (Cazes and Nesporova 2006, p. 12). Depending on the specific situation in each country they need to be upgraded, either through broader eligibility for benefits, or higher benefit levels and wage replacement rates, or actual benefit payment or compensation in time. Such upgrading would enhance both individual income support and income and purchasing power stabilization at the macro-level of the economy. It would better shield the working population against the risk of poverty and social exclusion. Active labour market policies, notably those for redeployment, direct job creation, and assistance for vulnerable groups, could be much expanded. With the exception of Bulgaria and Slovenia, the share of expenditure on active measures remains very modest. Implementation of the policies and improvement of public services are often hampered by the budgetary restrictions imposed by tight fiscal policies. Where this is the case fiscal restraint tends to be self-defeating. It impairs economic growth and employment in its wake which in turn constrains public revenues. Future reform should also reconsider the presently high burden of payroll taxes. In line with EU policy directives, the financing of labour market policies may be shifted from employer contributions to a tax-based system of financing.

Trade policy bears heavily on employment. The balance of trade forms an important component of aggregate demand. In almost all SEE countries, imports and exports have been very imbalanced in favour of the former. As shown in Table II.3, trade deficits were double-digit in 2004, ranging between 12.5 % of GDP for Romania and 52.2 % in Bosnia&H. They were over 20 % in Albania, Croatia, Serbia and FYR Macedonia. The exceptions were Turkey and Slovenia where the deficit remained just below 10 %, respectively 5 %. (Table I.3). Turkey has attained a positive balance of total trade in mid-year 2006. Deficits in merchandise trade were even larger, running as high as 60 % in Bosnia&H in 2003 and 34 % in Turkey in 2004. While imports from EU countries to the Western Balkans have increased, exports from the region to the EU have lagged behind. The big trade deficits explain in large part the chronic current accounts deficits. They burden not only the balance of payments, but in the final analysis also growth and employment. They provoke the question, whether in the process of transition commodity markets were opened up too quickly and prematurely. Albania, for example, that joined the WTO in 2000, accepted ambitious tariff cuts during its WTO negotiations, and proceeded to further trade liberalization when several bilateral free trade agreements became effective (CREP Albania, p. 9). Cutting import tariffs deprived the Balkans of an important source of public revenues that were badly needed to strengthen the infrastructure. Opening the economy to international markets usually turns out beneficial only if a country has mature industries and products and solid institutions, including institutions for social protection and the labour market. In their absence, the risks of losing out in trade are very high, particularly for workers and small firms. Many workers in the region lost their jobs in import-competing manufacturing industries, such as textiles, clothing, and footwear. The same may hold for certain agricultural and food products. So, instead of frontloading free trade on the transition agenda, institution building should get higher priority. It may not be by accident that Slovenia that went to open its markets gradually, moved decidedly slowly on the privatization of state owned enterprises, and emphasized domestic investment, shows the best track record of all transitions economies in terms of employment and other economic and social outcomes. A similar approach was taken by the thriving economies in East Asia: They protected their industries temporarily with tariffs before exposing them to foreign competition. Countries like India, China and Malaysia have pursued prudent strategies towards commodity trade and capital account liberalization. They have fared better than countries that opened their markets quickly or prematurely.

Investment and taxation policies. As indicated in Table I.4, FDI inflows to SEE vary greatly by country in absolute size, as a percentage of GDP, and per capita. Bulgaria, Romania, and Croatia have seen comparatively high inflows reflecting at least in part the upcoming membership in the EU. Slovenia and Moldova are also on the high side of FDI recipients, whereas Turkey has been at the low end, at least in relative terms. FDI accounts for approximately one half of total fixed capital formation in Moldova, and between one third and two fifths of total investment in Bulgaria, FYR Macedonia and Serbia&M. These are countries where the share of gross fixed capital formation has averaged less than 15 % of GDP (in Serbia&M), or between 15 % and 18 % the 1990-2003 period (Rutkowski and Scarpetta 2005, p. 116). The figures underline how important FDI is for capital accumulation in the region.

In order to court more foreign direct investment, most SEE countries have lowered statutory corporate taxes, personal income taxes and effective tax rates (i.e. the amount of tax levied after deductions and allowances). In so doing they have followed the tenet of the economic orthodoxy which holds that cutting tax rates would improve growth and employment because high taxes are seen as crowding out private investment and also because the state is regarded as a “bad manager of assets”. A broader view of taxes would ask about the benefits delivered from public revenues

and the value of services supplied by the state. This view is prevalent in the Nordic European countries where we find broad appreciation in society of services from (comparatively high) taxes and, given the top economic and social performance of these countries worldwide, apparently no adverse impact of taxes (on the performance of these countries: see Egger and Sengenberger, eds., 2003).

The figures on taxation for SEE indicate that on average the region tends to be on the low side of fiscal charges (Table III.2). This holds even when the SEE tax rates are adjusted for differences in the 'tax base'. Serbia, Moldova and Romania brought their tax rates down from already low rates. In Moldova, the corporate tax is now 16 %, down from 28 % in 2001. Turkey joined in recently to slice taxes for foreigners hoping that this would boost investor

Table III.2: Personal income tax, corporate tax rates and the index of fiscal burden, 2005

Country	Income tax in %	Corporate tax in %	Fiscal burden Index
Albania	25	25	2.8
Bosnia&H	5	30	2.6
Bulgaria	29	19.5	2.4
Croatia	15-45	20	3.0
Greece	--	32	--
Macedonia	15-18	15	2.0
Moldova	22	20	2.6
Romania	16	16	3.3
Serbia&M	10	14	--
Slovenia	--	--	3.4
Turkey	11	--	--

For comparison :

Czech Republic	3.6
Germany	3.5
Sweden	3.9
UK	4.0
USA	4.0
France	4.3
Italy	4.3
Austria	4.4
Netherlands	4.5

Sources : 2005 Index of Economic Freedoms and various government statistics; Telli et. al. 2006, p. 17.

confidence in the country, attract foreign assets and close the current account deficit. Greece cut its corporate tax rate from 40 % to 32 % during the last five years. Slovenia appears to be the only country that kept its tax level unchanged. By making sweeping tax cuts, the SEE countries joined Central European and the Baltic nations and also a number of the EU-15 countries that undertook tax reforms to improve their international competitiveness and position themselves better with regard to their attractiveness for international investors. From 1995 to 2005, corporate taxes in the EU-15 were reduced from 38.0 % to 29.9 %, and in the EU-8 (new member states) from 30.7 % to 19.9 %. As each country attempts to "beggar-thy-neighbour" by reducing unit costs and thereby gaining a larger share of the international market, the overall macro-economic effect may turn out to be counter-productive in terms of depressing aggregate demand, with negative implications for employment.

In SEE, as elsewhere, there is the risk of tax-competition and tax dumping which in the end may be destructive for Europe as a whole and defeat the goals of the Lisbon strategy designed to make Europe competitive through education, research, innovation and quality products. The SEE countries have been susceptible to such destructive competition because they have been dependent on IFI conditionalities that include tax cutting.

The issue is to what extent competition is actually tax-driven and whether in fact lower taxes do help national economies to attract foreign capital and gain more employment. For FDI, lowering taxes is double-edged. While it reduces the cost of producing in the country, it also reduces government revenues that are required for social redistribution, spending on the improvement of the physical and social infrastructure, and providing a broad array of business services. Instead of reducing taxes better results may be obtained by tax restructuring. For example, a study on Turkey found that a lowering of employment tax rates (including the present 22 % social security contributions paid by employers) by 5 percentage points – the target under the current IMF programme for the country - would let the unemployment rate fall by 2 percentage points over its base-path. However, as a result of foregone tax revenues, the policy shift would result in lower public investment in the order of 2.7 % of GDP, and a decline in the quality of public services. The authors of the study argued in favour of an alternative programme that would produce superior macro-economic outcomes. It would involve expanding direct income taxes to compensate for lower payroll taxes, and expanded public investments together with a lower primary surplus target (compared to the 6.5 % IMF target) for the public sector. With this measure, Turkey would benefit through lower unemployment and modest debt ratios (Telli et. al. 2006, pp.21-22).

Table III.3 : The Investment Climate in SEE, 2005

Country	Percentage of senior managers that hold ...as a major or very severe constraint for investment							
	Policy Uncertainty	Corruption	Legal * Insecurity	Crime	Tax Rates	Finance	Skills	Labour Regulations
Albania	19.1	31.8	43.6	8.6	40.9	19.5	10.4	2.5
Bosnia&H	35.1	24.7	41.6	19.9	15.6	25.8	3.6	3.2
Bulgaria	27.6	19.0	56.7	11.5	20.4	22.0	10.4	7.8
Croatia	17.9	18.5	26.0	3.9	12.0	12.7	7.2	3.0
Greece	9.3	10.0	18.2	5.2	27.5	16.3	8.6	7.7
Macedonia	27.9	34.7	55.4	12.8	21.7	31.6	6.1	9.2
Moldova	31.6	17.6	64.2	10.1	37.8	31.9	12.0	8.2
Romania	33.9	30.1	44.3	15.3	34.1	22.6	14.2	16.4
Serbia&M	61.2	25.5	43.1	13.5	29.5	43.9	10.7	13.4
Slovenia	11.5	3.7	34.4	0.9	12.7	9.5	5.4	4.5
Turkey	31.5	17.0	28.5	14.7	37.8	17.5	9.8	12.2

Source : World Bank Development Indicators, 2006 *Lack of confidence that Courts uphold property rights

With the exception of Greece, Romania and Turkey, the tax burden in SEE is not judged by managers as the most severe obstacle to investment. Rather, government policy insecurity, corruption and legal insecurity are considered primary impediments to locating investment in SEE countries (Table III.3). This finding corresponds well to experience from other regions. In a study of the world's largest 1000 firms, chief executives and financial officers were asked about their views on the best destinations for FDI. For the new member countries of the EU, the impediments and risks for investment were ranked as follows: poor local infrastructure (67 % of respondents), corruption (60 %), erosion of low cost advantage (53 %), macro-economic

instability (41 %), insufficient supply chain (35 %), poor labour skills and education (28 %), and labour market rigidity (27 %). Hence, poor skills and labour rigidity were of sub-ordinate significance (Kearney 2004, Fig. 9, p. 21). It can reasonably be assumed that this ranking of factors applies also to the SEE countries. The findings suggest that in seeking more private foreign capital, governments in SEE should be more concerned with improving the quality of local governance than relying on tax breaks. Moreover, if the quality of infrastructure is the top criterion taken by investors to choose country destinations, governments might seek to broaden the spending capacity by improving tax collection and fighting tax evasion in order to finance improvements in that area.

Yet, even if the SEE countries managed to raise the level of FDI inflows it does not follow that this is automatically and unambiguously positive for employment. FDI is not a ‘magic bullet’ for achieving modernization, development and employment. Net advantages from FDI, such as gaining advanced technology and management techniques, do not come automatically but require pro-active government policies to make the best use of foreign capital, to maximize the benefits and contain the risks. The expectation that cross-border capital flows lead to economic convergence with more advanced or higher-income countries has materialized in some countries (e.g. Ireland, Greece, Portugal and Spain whose income moved closer to the EU average), but has not come true in others (e.g. Mexico).

An empirical study of FDI flows to SEE came to the conclusion that it is not clear whether FDI has been net job creating or job destroying in the SEE countries. Jobs were created in some sectors but destroyed in others, or both created and displaced in the same sector, as a result of intra-firm restructuring. FDI flows to SEE have been primarily directed to privatisation, while with a few exceptions, there has been little investment in green-field operations. Furthermore, as was the case in Central European countries, FDI flows to SEE have been geographically concentrated in and around capital cities and economically advanced areas, whereas the least developed and economically depressed regions tend to be „forgotten” (Inotai 2005, section 4.2.10). Thus, one of the big policy challenges consists in how to orient the engagement of foreign-owned firms towards less developed regions in order to reduce high local unemployment rates and achieve more spatially balanced development.

As the employment impact of FDI is ambiguous, there is a need for strengthening domestic investment. Currently, this is difficult in view of the the regime of tight monetary and fiscal policies in SEE. One possible source of assets to be tapped for investment is the flow of remittances from SEE’s diasporic labour force. It is estimated that the bulk of the funds remitted from abroad go into immediate consumption and welfare (for Turkey, see Koc and Onan 2004). Only a small proportion goes to business investments. Governments could provide financial incentives to step up the use of remittances for productive investment, especially in small and micro enterprises. Since the 1960s, Turkey has tried to channel remittances to investment and employment, e.g. by promoting “village development co-operatives” and “workers’ joint stock companies”, notably in rural areas. The projects were of limited success, inter alia because of lacking entrepreneurial experience of the migrants (Köksal 2006, p. 2006). Nevertheless, the idea is worth pursuing.

In development economics, the growth of the remittances economy has sparked much enthusiasm that these flows are contributing to poverty reduction and economic development beyond the recipient’s individual income and the recipient country’s foreign exchange reserves. In fact, in several SEE countries, remittances have financed the current account deficits caused by deficits in the public budgets and foreign trade balances. But they had also inflationary effects

and have affected the exchange rate. So, one ought to be cautious seeing remittances as a “free lunch” in financial terms because they do not create any future financial obligations for the receiving countries compared to debt financing or FDI. It is also argued that remittances and the positive network effects more than offset the negatives arising from the brain drain. However, experience from various world regions suggests that remittances and other flows associated with a diasporic economy are not an unqualified success from a developmental perspective (Nayyar 2002). Migration can ease pressure on labour markets, and reduce unemployment, poverty and social inequality if surplus labour is exported. Returning migrants can be an important source of skills, expertise and ideas (“brain gain”) from which the national economy can benefit. Such benefits can be increased by adopting measures to facilitate the return of such workers to their home countries (e.g by easing re-entry conditions and tax incentives). However, for the SEE region evidence of brain gain is limited, while serious brain drain from the region is well documented. As indicated above, it is not just unemployed labour forming the main group of migrants. It is the highly skilled and educated that leave temporarily or permanently. This has deprived the countries of the very category of labour that are most needed for development, whereas the loss from the investment in training has been uncompensated.

Sectoral and industrial policy: Looking at the structure of output by economic sector (Table III.3), and the sectoral composition of employment (Table I.2), it is striking that in a number of SEE countries in 2004, the latest year for which data are available, the share of employment in agriculture is much higher than the share that agriculture contributes to total output. The ratio between the two is about 2,5 : 1 in Albania and Turkey, and roughly 2 : 1 in Croatia, Greece, Moldova and Romania. Conversely, the proportion of employment in services is smaller than the share of services in total output in all SEE countries for which information is available. In Albania, the ratio is about 1:2, and in Turkey it is about 1:1,5.

Table III.3: Structure of Output by Economic Sector

Country	Agriculture		Industry		Manufacturing		Services		% of total manufacturing			
	1990	2004	1990	2004	1990	2004	1990	2004	Food, Beverages 1990	2002	Textiles &Clothing 1990	2002
Albania	36	25	48	19	--	11	16	56	24	--	33	--
Bosnia&H	--	12	--	28	--	13	--	61	12	--	15	--
Bulgaria	17	11	49	31	--	19	34	58	22	--	9	--
Croatia	10	8	34	30	28	19	56	62	22	--	15	--
Greece	11	7	28	23	--	12	61	70	22	24	20	21
Macedonia	9	13	45	28	36	16	47	59	20	--	20	--
Moldova	36	21	37	24	--	17	27	55	--	59	--	10
Romania	24	14	50	37	34	31	26	49	19	--	18	--
Serbia&M	--	19	--	36	--	22	--	45	--	36	--	6
Slovenia	6	3	42	37	34	27	52	61	12	10	15	9
Turkey	18	13	30	22	22	18	61	68	16	13	15	23
Middle Income Countries	16	10	39	37	25	18	46	53				
World	6	4	33	28	22	18	61	68				

Source : World Bank, World Development Indicators, 2006, Table 4.2.

The figures point to inefficiencies in the sectoral structure of the countries, and the expediency of reallocating resource inputs to higher value-added activities. In view of the low average productivity level and the concomitant high poverty in large parts of SEE, policy interventions

seem to be called for to remedy the situation. The question is how and why such disproportions have arisen, and what would be the appropriate way to correct them. The excess input of labour to agriculture in relation to the national product could stem from the overall lack of employment opportunities. Hence people, especially those in rural areas, respond to it by staying in, or returning to, agriculture as an employer of last resort, or a way of surviving through food production in subsistence farming and animal breeding. The latter has been observed as a rampant survival strategy in many CIS transition countries, and also in Turkey. To align sectoral employment and productivity structures, labour could be shifted from agriculture to other, more productive sectors. This is the “classic” reflex which the World Bank economists call “strategic restructuring” (see Rutkowski and Scarpetta 2005, p. 139). However, it is debatable whether this strategy is opportune in SEE under the present circumstances. In light of the overall deficient demand and the lack of job openings in other sectors, workers quitting agriculture may not find new jobs elsewhere. Therefore, they may not contribute to higher welfare, but simply swell the ranks of the unemployed and under-employed. The mass displacement in Mexico’s agricultural sector in the wake of the North American Free Trade Agreement (NAFTA) has been one of the factors driving immigration of Mexican workers to the US. An alternative, better solution may be to raise the productivity of employment in agriculture, either by applying better production and commercialization methods, including land improvement, irrigation, drainage systems, fertilizers, local storage facilities, etc (Albania has adopted this approach when it recently escalated agricultural production in greenhouses (UNECE 2005b, p. 17)); or by switching to higher value added or higher quality products. Hungary has chosen this route when it adopted the French system of “appellation contrôlée” for its wine growing. As a result, its wine exports have been thriving.

Moving up-market would seem to be a viable, if not inescapable, strategy for SEE’s manufacturing sector as well. In labour-intensive manufacturing industries cost competition has become extremely intense, partly because of the rise of large Asian producers. While for the moment countries like Bulgaria, Romania and Turkey are benefiting from their low labour costs, this competitive edge may soon be wiped out by newly emerging competitors elsewhere. Turkey, for example, has reached an increasingly positive trade balance for labour-intensive and resource-based products, but has faced an increasingly negative trend in its trade balance of medium-level and high-level skill and technology commodity groupings during the last 30 years (Köse and Öncü 2004). Instead of getting fully immersed in a fierce competition on the basis of labour costs, SEE countries may consider reaching out for higher quality products and higher value added production. This would be essential for narrowing the income and development gap with the EU-25 and other industrialized countries, and avoiding the negative experience of many developing countries during recent decades. Although the latter have increased their shares in total world trade and total FDI flows, they could not manage to narrow the income gap to the rich countries because their economies have been concentrated in low value-added, low income-generating production and services.

Education and Vocational Training: As in other transition countries the level of education in terms of primary, secondary and tertiary schooling in the countries of former Yugoslavia and Moldova was respectable by international comparison. During the transition phase the quality has been declining. Vocational education and training (VET) has deteriorated in many places. Modernization of curricula to respond to new skill demands has been insufficient. As the CREP reports show, there have been government efforts to counter these trends. However, the outcomes have been meagre, because the policies have not been effectively implemented. This failure is in large measure due to insufficient financial resources stemming from fiscal stringency. Another institutional barrier to implementation of human resource policies has been

the absence of the social partners in the design and implementation of education and VET policies.

While there are shortcomings in the supply of skills in SEE, particularly in some occupations, skills provision so far do not appear to pose one of the most serious obstacles to more FDI inflows. This can be seen from the surveys of managers about barriers and risks to investment (Table III.3). They view other obstacles, notably problems of governance and legal insecurity, as more serious impediments. As the present foreign investment flows go in good part into the production or the subcontracting of labour-intensive, low-skill industries, such as textiles, clothing, leather and footwear, and automotive parts (in Turkey), the skill factor tends to be of limited significance. Due to offering somewhat higher wages and salaries, foreign investment companies are in a position to cream off skilled workers from domestic firms. The situation may change in the medium-term future should the rate of foreign investment pick up and the demand for higher level skills grow. In this case, skill shortages may become more severe and needs for skill formation rise.

Social dialogue: Workers' and employers' organization, the (bi-partite) dialogue between them, and the (tri-partite) dialogue between them and the government, influences employment performance in various important ways. When some European countries, including Austria, Denmark, Ireland, and the Netherlands, experienced employment revival in the 1990s near to the point of full employment, representatives of government and the social partners felt that the success could not have been achieved without an employment compact resulting from tripartite consultations (Auer 2000; Auer ed. 2001).

In SEE, social dialogue has yet to unfold its positive effects, or its full potential benefits. So far, it has been hampered by deficiencies in the collective organization of employers and workers and the resulting weaknesses of both bipartite and tripartite social dialogue. Though countries vary in terms of the nature and maturity of their collective labour relations, a better functioning social dialogue between decision makers and those who are affected by the decisions would be essential for improving policy formulation and implementation. It would also be important for changing power relations in the countries in favour of a higher priority of employment on the national policy agendas. The lack of effective participation of the social partners in politics in the region appears to reflect the deeper problem of a rudimentary civil society.

Some of the major shortcomings of workers' and employers' organizations are described in the CREP reports. Rates of collective organization are low in the majority of countries; unions fail to recruit new members in growing employment fields, such as SMEs; the organizations are fragmented, partly along the « old » unions from the pre-transition period and the « new » unions emerging from resistance movements. (In the Stability Pact countries alone, 34 national-level union confederations and 28 employer confederations have been counted, all claiming a degree of representativity); the fragmentation on the union side seems to fuel fragmentation on the employer side and vice versa; disputes have arisen over union property that have exacerbated inter-union splits (for a detailed overview of the organization and structure of workers' and employers' organizations in SEE, see Duric (2002) and Hantke (2005)).

Except in Bosnia&H and in Kosovo, there are statutory requirements for tripartite consultations, but the actual practice falls frequently short of the legal stipulations. In many places, tripartism exists « only on paper ». The governments are said to show little will to enter into genuine dialogue. Often, they merely inform the social partners about new policy measures, without seriously consulting them. In 2004, the government in Bulgaria was charged by the trade unions

PODKREPA and CITUB of negotiating with the World Bank the liberalization of the labour code «behind the back of the social partners ». Sometimes, employers resist real dialogue. A basic problem in SEE seems to be the lacking ability of the workers and employers to develop collective bargaining relations in the private sector. The concerns of trade unions on the company and plant-level are rarely focussed on employment related matters, but – following the pre-transition pattern of union responsibilities – rather on social benefits, such as food allowances, supplying household appliances, and organizing vacation activities for members. Moreover, much of their energies and resources go into resolving wage payment problems, including non-payment or wage arrears, and non-payment or late payment of severance payments. With few exceptions, e.g. Bulgaria, employers and unions do not yet command sufficient cognitive, staff and financial resources to conduct genuine dialogue. International experience tells us that tripartism cannot function properly where there is no self-responsible bipartism in place. In SEE, supra-plant negotiations hardly exist outside the public sector. More generally, there are signs that the principles of a pluralism of interests and the independence of associations which are underlying the pertinent ILO Conventions nos. 87 and 98 on freedom of association and collective bargaining are not yet fully established. In the face of deficits of social dialogue, there is not the unity of purpose and trust that enable employers, workers and the government to cooperate closely in finding better solutions to the countries' employment challenges.

A major reason for the insufficiency of social dialogue in SEE is the large proportion of informal employment. It hampers the collective organization of workers and employers. The 2002 International Labour Conference has recognized this problem and has urged the members of the ILO to strengthen social dialogue and tripartism in the informal economy. Turkey has been selected for a pilot programme aimed at the promotion of employment and addressing unregistered employment through improved social dialogue. A constituent needs analysis in February 2004 formed the basis for a subsequent conclusion of a National Plan of Action (ILO 2005c). The social dialogue is to be enhanced through data and information sharing, awareness raising, workshops and capacity building. Meanwhile, studies were undertaken in three Turkish provinces.

IV. Towards a strategy of more and better employment

The adoption and implementation of policies and the establishment of relevant institutions constitute essential steps for promoting employment. *Employment strategies* help countries to connect the policies in a consistent and coherent manner, attach priorities to them, and get them oriented towards explicit goals and targets.

Considering interaction effects of constituent and companion policies of employment is of the greatest importance for attaining the maximum possible outcomes. For example, it is now widely acknowledged that labour market policies and job creation through macro-economic policy must work in tandem to generate higher growth and more and better jobs. One without the other is likely to produce policy failure. Macro-economic policy will have to generate a level of aggregate demand in the economy sufficient to attain full employment. The function of labour market policy is to reduce mismatch of supply and demand in the labour market by providing public employment services, improving the employability of the labour force, and promoting the employment opportunities of disadvantaged and vulnerable groups. While labour market policy does not generate jobs directly (the exception being public works programmes), it lowers the threshold at which growth translates into additional employment. By doing so it serves to increase the potential scope for expansionary macro- policies producing non-inflationary

economic growth. If workers are asked to make concessions on certain labour standards, such as employment protection, or cooperate with faster labour saving product or process innovation, they will go along with such measures only if they see positive net employment growth after a reasonable period of time. Hence, fiscal and monetary austerity which is a regular feature of the policy prescriptions of the IMF cannot be more than temporary if insufficient employment growth is to be avoided.

Setting multiple employment goals

The choice of a national employment strategy starts with the setting of explicit employment goals. Those countries in SEE that have ratified the main ILO Employment Policy Convention no. 122 (of 1964) – i.e. all countries except Albania and Bulgaria – are bound to direct their policies to the achievement of full, productive and freely chosen employment. In practice, the question arises how this is best achieved. Full employment as indicated by a low rate of unemployment – accounting for some frictional unemployment- can be attained both at a high and a low employment-to-population ratio. The unemployment rate can be kept low if jobless workers who look for work go abroad to find employment opportunities, or move to the informal economy, or withdraw from the labour force. While all this helps to improve the unemployment statistics it reduces the scope for domestic growth because it underutilizes the national labour force. Full employment is thus more than the absence of (statistical) unemployment. Its definition should incorporate the rate of employment, i.e. the ratio of the country's labour force that is actually employed. As said above, in the European Union target employment rates have been fixed to entice governments to seek high levels of labour force utilization. Whether full employment is reached just by low unemployment rates or, in addition, by high levels of employment relative to the size of the population at working age, makes a big difference for a country's development. Low employment rates prevailing in most of the SEE-11 economies mean to forego chances for growth and prosperity. Large informal employment means that efficiency is less than it could be given that labour productivity of informal jobs usually falls short of that formal economy jobs. Moreover, unregistered employment means loss of potential state revenues and, therefore, reduced capacity for providing the public services needed for growth, employment and development. Informal employment is typically associated with low wages, often below the statutory minimum, increased work place hazards, and the lack of social security coverage. Hence, full employment should also be defined as full formal employment.

Equally important as the setting of goals in respect of the quantity of employment would be the targeting of qualitative goals of employment. Both the ILO and the European Commission have attached equal significance to the goal of more jobs and the objective of better jobs. The ILO has been advocating the concept of “decent work”, while the EU has promoted the “quality employment”, and more recently the notion of “decent work” as well. They have done this for good reason. They have learned that there are several mechanisms that link good work standards with higher productivity and innovation capacity. The Lisbon strategy of the EU is built explicitly on the link between high work standards, high quality of labour resource inputs and Europe's competitiveness in the global economy. There is ample empirical evidence to show that investment in improved labour standards pays off in terms of economic, social and political dividends (Sengenberger 2005, chapter 4). Hence, it would seem that embracing the improvement, or the further enhancement, of quality of employment as a goal would be rewarding for the SEE-11 countries. This would be essential in order to attain the EU goal of economic convergence which ought to be accomplished by the sustained higher growth of productivity in the SEE region relative to the older EU member states.

Working towards policy coherence

Achieving greater coherence in national employment policies may be seen as posing the greatest challenge in the SEE context. There are two dimensions to policy coherence. First, there is a need for horizontal integration of all policies that in one way or another impact on the quality and volume of employment, such as education and vocational training, active and passive labour market policies, wage and incomes policy, social security, monetary and fiscal policies, trade policies, gender policies, and migration policies. Secondly, there is the requirement of vertical integration, or coordination, of policies across various organizational levels, including the national, sub-national and international level.

At present, serious shortcomings of integration, both of the horizontal and the vertical type, exist in most SEE countries. The region is not peculiar in this regard, but shares the problem with a large number of countries in other world regions. The integration deficits originate partly in inconsistencies of policy stances on the side of international organizations, such as the IMF, the World Bank, and the ILO, which are carried to the national level in the form of conflicting policy advice. In SEE countries, incoherent employment policy advice has manifested itself in the co-existence and variable policy stances of CREPs jointly undertaken by the ILO and the Council of Europe, Poverty Reduction Strategy Papers (PRSP) or Country Assistance Programmes run by the World Bank, and standby agreements of national governments with the IMF. Policy discrepancies between the IFIs and the ILO and working at cross-purposes are especially poignant with regard to labour market deregulation, worker protection, minimum wage fixing and collective bargaining structures (the IFIs argue against centralized and coordinated bargains and pro individual or enterprise level bargains). The international financial institutions have intervened in nearly all segments of employment and labour market policy even where they do not have a direct mandate. As national governments have been under severe financial pressure up to the point of state bankruptcy, they felt that they had no choice but to succumb to the conditionalities attached to concessional lending and other forms of foreign assistance. In some SEE countries, e.g. Bulgaria and Croatia, trade unions have objected to IFI policy interventions and to the governmental adherence to them and have staged protest action for this purpose.

Dialogue among the advisers of the multilateral system is key to reaching an accord on the upgrading of employment as both national and international development goals. It cannot be taken for granted that employment takes the same degree of priority, or the same centrality of concern, in each international organization. These organizations are not value neutral. They pursue vested interests. As stressed by the World Commission on the Social Dimension of Globalization, they have tended to regard employment as derivative from their main mandates, rather than as an objective in its own right (World Commission 2004, para. 506). The WTO promotes the expansion of trade, and this is seen as the way to create employment. The World Bank has shown a strong penchant for rapid privatization. In the design of the PRSP process there is a lack of emphasis on employment. The IMF that has been a big lender in SEE is keen to see that countries fully repay their debt. While this interest is legitimate it should be questioned whether it is best served by squeezing public budgets to a point where longer-term development is jeopardized due to insufficient investment in the countries' physical and social capital. Macroeconomic stability must be defined widely enough to cover social stability and social cohesion. As these are integral parts of the European social model, the ILO, together with the European institutions, must ensure that employment goals in SEE do not fall victim to short-term fiscal discipline and exaggerated disinflation policy. The ILO stands as an organization for which employment and decent work are central to its mission. Therefore, it must take the initiative to seek a better balance of financial, economic and social concerns among the international

stakeholders. It must strive to reach an upgrading of the employment goals in an encompassing and far-sighted development strategy. This call is in line with the report of the World Commission on the Social Dimension of Globalization, published in 2004, that demanded increased coherence between the IMF, the World Bank, WTO, and the ILO and other relevant organizations in the multilateral system (World Commission 2004, p. 133-135).

There are some prospects that international policy coherence is augmented by intensified dialogue between the pertinent organizations. The World Bank, for example, has made some moves in the direction of policy stances of the ILO. This includes the recent endorsement of ILO's core conventions and support for their adherence from the International Finance Corporation, the Bank's private sector lending arm; recognition of the destructive effects of large social inequality; and recognition of employment as a central factor in national development and poverty alleviation strategies. The Bank's *World Development Report 2006: Equity and Development* appears to present more balanced views on such topics as worker protection and privatization. The ILO which has networked with the World Bank on combating youth unemployment in recent years, has now taken the initiative to sort out policy differences with the Bank. SEE would be a good terrain for probing greater policy convergence between the two organizations. European agencies, notably the EU Commission and the EBRD, will also have to be part of an international consensus on coherent advisory and financial assistance.

Insufficient policy integration and cooperation among the international organizations is mirrored by sectorialism at the national level. In particular, ministries of labour and social affairs, ministries economic affairs and trade, ministries of finance, and national banks do not always coordinate and harmonize their policy lines and actions to come up with a coherent national strategy. In some countries, progress towards harmonization of policies across relevant ministries has been achieved. In fact, it is often the different policy positions within the government, notably between labour and finance ministers, that are transposed into the deliberations of the policy making organs of the multilateral institutions. So, incoherence at the national level and discrepancies at international level reinforce each other.

Strengthening regional cooperation

Technical concertation and cooperation among the countries in SEE can greatly help the region to ameliorate employment strategies and accomplish outcomes superior to those available if each country acted alone. Benefits from cooperation can accrue despite, and even because of, the large degree of national and international diversity of socio-economic conditions and disparate development levels. This can be illustrated with regard to the excellent 'peer reviews' that were undertaken for a number of SEE Stability Pact countries over the last two years*. They were conducted under the aegis of the Council of Europe and the ILO, with financial support from the Belgian government, and directed to provide mutual assessment of labour market policies and public employment services, including the proposal of policy instruments and measures that countries found particularly useful. They generate, in other words, international public goods. For example, national labour market experts from Bulgaria and Romania were instrumental in transferring national experience and competence to Moldova and the West

*Footnote: Peer reviews on employment were first introduced in the EU following the so-called Luxembourg process for the implementation of the EU employment strategy. They formed part of the method of 'open coordination' adopted for reaching commonly agreed employment goals and targets. Next to peer reviews this coordination includes (i) jointly formulating performance measures (statistical indicators) for realizing the targets of the guidelines; (ii) annual reporting of the measures taken and the actual degree of target

achievements in national action plans; (iii) and using 'benchmarking' as a method to compare performance of each member state based on the commonly agreed statistical indicators. The European Commission monitors and evaluates the coordination process and publishes an annual report. The European Council, the European Parliament and the social partners are also involved in the process, by adopting the annual employment guidelines, respectively organizing hearings on the progress made towards the common goals in each member state and the overall goal of convergence of employment performance.

Balkans that had started the transition process later or faced interruptions because of intermittent war periods. The peer review technique is especially helpful where it is based on prior employment policy reviews that deliver a sound diagnosis, including the advancement and interpretation of internationally comparable labour market statistics. The technique could be extended to cover other employment related policy areas. In future reviews it should be made sure that macro-economic policies are more fully incorporated and the ministries of economic affairs and finance are represented at the meetings.

Equally important as the exchange of positive experience for the common good in the region are endeavours of cooperation and coordination to abstain from policies and measures with a negative impact on development. An obvious case in point is tax policy. As pointed out above, one country after another in SEE has jumped on the "tax rivalry bandwagon" in recent years. If countries in trying to attract foreign capital and stimulate exports out-compete each other by offering tax breaks or higher subsidies to foreign investors, a race the bottom may ensue. In the end every country may lose because the presumed competitive advantages cancel out and because of lacking fiscal revenues they will miss the chance to guard investors through appropriate local services, a better educated and trained labour force, a more appealing material infrastructure, and better national institutions. Avoiding such destructive competition that is harmful to employment requires cross-national cooperation. Furthermore, an eroding tax base reduces the opportunity for the government to conduct redistribute policies which, in turn, diminishes domestic economic growth.

Summary

In recent years, nearly all countries in SEE experienced economic growth in excess of average world and EU rates of GDP growth. The former centrally planned economy countries have made significant advancements on the road to market economies. The West Balkans have recovered from war and have succeeded in containing civil strife. Greece has improved its relative income position in the EU. Slovenia has shown the best economic and social performance of the European transition countries. It now even outperforms a number of EU-15 countries.

However, progress has remained less than satisfactory in respect of employment and other dimensions of social development in the Stability Pact countries of SEE and in Turkey. These nations continue to be confronted with comparatively low rates of labour force participation and employment, high aggregate unemployment and large-scale joblessness for youth, large proportions of informal employment and high incidence of poverty. There is still a large gap to bridge to reach full employment, improve the quality and productivity at work and strengthen social cohesion. The four poorest countries in the region have seen temporary or permanent emigration of a significant proportion of their labour forces, among them many young and educated workers. Instead of exporting goods from which countries can derive greater prosperity in the globalized economy, they export workers. The sizeable remittances transferred by the expatriate labour force to the home countries have brought foreign exchange and fuelled economic growth. Yet, they are not a substitute for long-term domestic development. The

transfer of income from abroad and informal employment complicate the relationship between GDP growth and employment and obstruct the calibration of growth elasticity of employment.

A more favourable domestic development, including higher rates of employment, in the poorer SEE nations must mainly come from more expansionary macro-economic policies. Monetary and fiscal policies have been excessively restrictive, with negative implications for domestic investment and public spending on the development of national institutions and infrastructure, including labour market facilities. Large trade deficits stemming from rapid and premature trade liberalization have impacted adversely on the current account balance, economic growth and employment. Increased foreign direct investment in recent years has helped to raise capital accumulation, notably in the countries soon joining the EU. Yet, its impact on employment and spatially balanced economic development has been ambiguous. Partly under the influence of international financial institutions, too much has been expected from labour market deregulation for the improvement of the labour market situation. Employment protection was scaled down without providing compensation in terms of adequate standards of income protection for the unemployed. As long as unemployment benefits and active public support for redeployment remain as deficient as they are, good labour market performance will be hampered by poor job search efficiency; structural change towards will be impaired because of rampant worker insecurity; and aggregate demand will suffer because of insufficient stabilization of consumption power. What is more, low levels of minimum wages in most SEE countries led to the risk of generating higher inequality and poverty. Hence, improving social protection standards and enforcing the standards will have to be a policy priority for development in SEE.

The promotion of employment in SEE would, in addition, greatly benefit from more cooperation among key actors and agencies, national and international ones. Enhancing the system of consultations and collective bargaining between workers's and employers' organizations, and tripartite social dialogue between the social partners and the government, will have to be an essential ingredient to a comprehensive strategy for employment. This strategy ought to be informed by explicit goals that put higher employment rates, lower unemployment and higher quality of employment on an equal footing. The statistical data base on employment and labour markets needs to be improved to facilitate research and the monitoring and assessment of policy outcomes. The various policy fields influencing employment need to be integrated and action taken at the relevant ministries in the national government need to be coordinated. At the same time, greater policy coherence must be achieved between the international organizations that deliver advisory services and financial assistance to the region. Regional cooperation among the SEE countries can be conducive to employment policy formulation as demonstrated lately by peer reviews on employment policy conducted in the Stability Pact countries. Such open policy coordination could be extended to forestall destructive economic and social competition among the countries.

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