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Transition and the labour market in Uzbekistan

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Preface

This paper is one of a series of three chapters chosen from the volume prepared for the ILO/UNDP multidisciplinary mission on *Social Policy Review* which was requested by the Government of Uzbekistan, and which took place over the period of 21 March to 21 April 1995, with Professor Keith Griffin as its Chief.

The volume provides a systematic and critical review of the macroeconomic and social policies in Uzbekistan. To our knowledge, this is the first attempt to provide a coherent policy framework which combines the objectives of social policy as an integral part of macroeconomic reform. *The main message of the report is that Uzbekistan should speed up its pace towards economic reform, and at one and the same time ensure that the social dimensions of reform are taken into account.* Thus, the thrust of the argument is that sound social policy is a prerequisite for the success of economic reform. It should form an integral part of the overall development strategy, and not simply react to whatever negative consequences macroeconomic policies may create. Social development policies must therefore be carefully designed to ensure that during the transition to a more market-oriented economy, average living standards are not allowed to deteriorate, thus threatening the whole process of reform and the prospects for long-run growth.

To implement this strategy, a number of *policy reforms, institutional changes and investment programmes* were recommended. The main objective of the *programme of action* is to identify a limited number of areas of intervention that would help to translate the major recommendations of this report into reality. The list is not exhaustive, but contains the critical elements of a social development strategy designed to support the process of reform. Four major programmes are proposed: (a) the creation of a social development fund; (b) launching a social assistance programme; (c) initiating a programme for national capacity building; and (d) improving the database for social development.

An important question relates to the *finance strategy of these recommendations*. Despite the serious difficulties encountered during the transition from a centrally planned to a more market-oriented economy, Uzbekistan finds itself in a relatively good financial position and thus has some room for manoeuvre in launching a more expansionist development strategy.

This report provides an excellent example of the way in which social policy could be integrated in a systematic manner into the framework of macroeconomic policies. It also demonstrates the possibility of striking a balance between the requirements of rapid economic reform and social cohesion. We are confident that the relevance of this report goes beyond Uzbekistan, especially to other Central Asian republics.

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Contents

1. Introduction

As a former republic of the Soviet Union, Uzbekistan has had to face major economic shocks since the collapse of the centrally planned economies. First, with the political dismantlement of the Soviet Union, it became an independent State in 1991. Economically, this meant that Uzbekistan was to lose the large aid transfers — almost 20 per cent of its GDP — it used to benefit from Moscow prior to the collapse. Second, with the disruption of the trade system among the former Soviet bloc, Uzbekistan simultaneously faced a large deterioration of its terms of trade and a sharp reduction in its traditional export markets. The trade effects were all the more devastating since the former Soviet Union was characterized by an extreme integration of production and a related very high specialization of each republic. This was reflected in the structure of foreign trade: the Uzbek exports represented, in 1990, 40 per cent of the GDP, among which 85 per cent were inter-republic trade. Third, with the general recognition that market economies would achieve better economic outcomes than central planning, Uzbekistan embarked upon a transition towards a more market-oriented system. A programme of economic reforms, including economic liberalization, privatization and restructuring, was implemented. The disruption of the internal production network was, however, limited as the Government chose to implement transition reforms at a slow pace. Particularly, large enterprises remained under the ownership of the State and were still highly subsidized, either through direct public transfers or through an access to credit at negative interest rates.

Those shocks resulted in a large decrease of the production, with GDP falling in real terms between 1991 and 1994. The cumulated decrease amounted to almost 20 per cent. The release of state controls over price settings in a context of expansionary monetary policy — mainly through easy credit to state enterprises — together with the strong inflation imported from the rubble zone resulted in hyperinflation. Under the double pressure of the economic recession and rapid price increases, real incomes fell sharply. In addition to the reduction in real wages, Uzbekistan households faced a wide erosion of social benefits. The level of employment has been maintained so far, as firms have been allowed, through the maintenance of a soft budget constraint, to continue operating with large redundancies.

This will not be the case in the future. In order to re-establish a more stable macroeconomic environment, the Government will have to implement a stabilization policy aiming to reduce inflation. To accelerate the development of the private sector, further structural reforms will have to be implemented. In the short term, both macroeconomic policies and structural reforms will accelerate labour shedding from presently overstaffed enterprises and affect real wages. Like in other countries which embarked upon transition earlier, the transition from a centrally planned to a market-oriented economy will be difficult, especially in terms of sharply increasing unemployment and falling average incomes.

Therefore, labour market policies will be crucial in the transition period. Their main function will be to improve the functioning of the labour market, as a large reallocation of labour will have to take place from public to private activities as well as from old/unproductive to new/competitive sectors. Employment restructuring could be eased through job-search assistance, retraining, incentives to increase workers' mobility. In addition, an appropriate industrial policy and some state support to the development of the service sector could accelerate both economic restructuring and employment creation.

But, more fundamentally, employment and wage policies could play, if properly designed, a key role in the resumption of employment, incomes and growth. [1] Actually, and contrary to a widespread belief, it is very unlikely that price stabilization, privatization and market reforms will by themselves ensure a rapid renewal of growth. By re-establishing the correct price signals and the appropriate institutional setting they will enforce the supply side of the economy and allow it to respond adequately to the evolution of the demand. But without an adequate level of households' income, consumption will remain depressed and investment rates insufficient. It is therefore very important that both real wages and employment remain kept at a level that prevents the demand from falling dramatically.

In that context, this article proposes an appropriate set of employment, wage and public investment policies which, if designed altogether in a consistent way and implemented simultaneously, could play a central role in the success of the transition towards a market economy. The first section describes the recent trends in the labour force, employment, unemployment and wages, in order to evaluate the extent of the present potential disequilibria that characterize the Uzbek labour market. Labour market policies are proposed and discussed in the next section, with particular emphasis on measures to enhance private employment development and direct job-creation schemes. The third section discusses wage policy. A synthesis of the preceding discussions is drawn in the conclusion, which presents the main components of a consistent employment and wage policy.

[1] The labour market policies recommended here have been designed in the broader context of macroeconomic policies and structural reforms from which they are indissociable. In fact, they represent a central pillar of an overall strategy aiming at: (i) stabilizing the economy; (ii) implementing the appropriate market mechanisms and institutions; and (iii) generating a renewal of growth. Labour market and public investment policies are particularly important to achieve the third goal. For further details, see "Social policy and economic transformation in Uzbekistan", ILO/UNDP, 1995.

2. The present situation: Large potential imbalances in the labour market

2.1. The labour force

Uzbekistan is characterized by a very young and rapidly growing population. Among the 22 million people recorded in 1994, 50 per cent were of working age and 43 per cent were below working age. [1] Those over working age accounted only for 7 per cent of the population (see table 1). The population growth, despite a slight decline during the last decade, remains rapid, at 2.3 per cent a year between 1990 and 1994, primarily because of a very high fertility rate. The growth of the labour force therefore is certain to be very dynamic during the coming years, with an exceptionally high replacement ratio. In the near future every person leaving the working age group will be replaced by 2.6 young potential workers entering the labour force. This means that, assuming labour force participation rates remain constant, the labour supply will increase dramatically.

Table 1. Breakdown of the population by three age-groups
(percentage of the total population)

	1985	1990	1994
Working age	49.2	49.2	49.2
Over working age	8.1	7.9	7.7
Under working age	42.6	42.9	43.1

Source: Draft "Human Development Report on Uzbekistan" and GKPS.

Because of the particularities of the labour concepts used during the Soviet period, the labour force data used in Uzbekistan are not totally comparable to those used in Western countries. Hence, some caution is needed when discussing labour force participation. Nevertheless, a good approximation of the overall labour force participation rate in Uzbekistan is the ratio of the so-called "economically active population", including both the employed population of working age and the unemployed willing to work, to the working-age population. This ratio declined from 87 in 1989 to 81.8 per cent in 1994 (see table 2). This is rather low by former Soviet standards (compared to 95 per cent in Russia in 1989) but high by Western standards (70 per cent in the OECD countries and 66 per cent in the European OECD countries in 1991).

Two interpretations of this relatively low labour force participation rate as compared to other socialist countries can be offered. The first is that, already under the previous system, Uzbekistan could be regarded as a "labour surplus" area. [2] Indeed, 13 per cent of the working-age population was not working, which is high compared, for example, to Russia

[1] According to the national definition, people of working age include women between 16 and 54 years old and men between 16 and 59.

[2] As described in World Bank, 1994.

where this figure was only 5 per cent. To what extent this reflects the inability of the previous system to provide every citizen with a job is difficult to judge. Given the rapid increase in the supply of labour in Uzbekistan, it is plausible that even under the Soviet system of guaranteed employment for every able-bodied person, the demand for labour was already lower than the supply and that some of those classified as "economically inactive" were actually willing to work. If this was the case, it could be assumed that the conflict between an abundant supply of labour and the obligation of the State to ensure full employment resulted in extensive overstaffing throughout the economy. Although open unemployment was non-existent, hidden unemployment can be assumed to have been high in the pre-transition period.

While this explanation is very plausible, the very young age structure of the population and the high fertility rates are probably more important in explaining the relatively low labour force participation rate. Half of those "economically inactive" were students of working age, most of the rest being women on maternity leave (the interruption for maternity is a maximum of three years). The low labour force participation rate may therefore be a reflection of an unusually high proportion of young people in university and of women with small children in the total working-age population. In that case, the future evolution of labour supply will depend in large part on the evolution of the labour force participation rate among females.

Compared to Western countries, the labour force participation rate in Uzbekistan before independence was very high. This is true for all former centrally planned economies and is related to the special status of employment in the Soviet system: apart from the fact that the State had an obligation to provide work for every citizen, employment was simultaneously the principal means of social integration and the channel through which the population received social benefits. In fact, social benefits were not provided by the State but instead were provided directly by state enterprises to their workers. There were therefore very strong incentives to become and remain economically active, especially for women and also for elderly workers.

Table 2. Working-age population, labour force, employment and unemployment
(thousands)

	1993	1994	1995 (forecast)
Able-bodied working-age population	10 600	10 860	11 213.1
Economically active population of which:	8 722.1	8 883.2	9 256
Population employed in the economy	8 259	8 335	8 610
Other categories of employed	138.1	145.2	150.8
Unemployed	325	403	495.2
Economically inactive population of which:	1 877.9	1 976.8	1 957.1
Full-time students	924	920	928
Others	953.9	1 056.8	1 029.1
Labour force participation (%)	82.3	81.8	82.5
Unemployment rate (%)	3.1	3.7	4.4
Proportion of students in the economically active population	49.2	46.5	47.4

Source: Ministry of Labour.

Given the small size of the elderly population in Uzbekistan the labour force participation rates among the elderly cannot account for the generally high labour force participation rate. The major explanation has to do with large women's participation in the labour market. The transition towards a more market-oriented economy could to a large extent modify this situation. In all countries which have experienced such a transition the female labour force participation rate has decreased when state enterprises ceased to provide social benefits. On the other hand, the reduction in child allowances and other related benefits could put pressure on women to remain in the labour market. The question of whether a large reduction in female labour force participation is desirable, as reflecting the aspirations of Uzbek women, or should be discouraged as a form of repression of women, will not be addressed here. [1] The key point is that while a decline in female labour force participation rates could ease the pressure on the supply of labour, it is unlikely to be enough to prevent the labour force from rising very rapidly. The overall population dynamics are too strong. This points to the imperative need for extensive job creation.

[1] For an extensive discussion of the status of women in Uzbekistan, see "Social and economic reform in Uzbekistan", 1995, Ch. 7.

2.2. Employment and unemployment

The pre-transition situation was characterized by full employment. However, this full employment was not the result of a perfect match between the demand and the supply of labour in an economy achieving an adequate level of output. There were massive shortages in the supply of consumer goods as well as in certain types of capital goods. These shortages were inherent to the functioning of the previous system. [1] Full employment was achieved through the artificial support of unproductive state firms, which resulted in a very low productivity per worker. In almost all other former centrally planned economies, the transition process has resulted in large job losses. This erosion of employment has been the result, in part, of a move by state enterprises towards rationalization and labour shedding. In addition, job losses have been generated by, on the one hand, the huge demand shock involved in stabilization policies and, on the other hand, the supply shock that has been occasioned by the disruption of the former production and foreign trade systems.

Full employment has been maintained so far. This can be explained mainly by the maintenance of a soft budget constraint on enterprises which have been provided with easy credit, state subsidies, or other forms of financial support through the state budget or the banking system. They have been allowed to continue paying the inflated payrolls of their excessive number of employees. Therefore, although the process of structural reforms is already quite advanced in some areas, firms have not yet begun the large-scale restructuring of their production processes that will be required if they adopt rational market-oriented behaviour. On the contrary, most large enterprises have continued to be overstaffed just as they were in the Soviet period.

Enterprises have even been able to cope with the large "transitional" decrease in their production without shedding labour. Although the growth of employment has somewhat decelerated since the transition began and employment is increasing at slightly lower rates than the growth of the labour force, causing some open unemployment to emerge, there has been a considerable contradiction between the evolution of employment and production. Since 1990 output has decreased by 16.5 per cent, while employment has increased by 5 per cent. As a result, there has been a decrease of more than 20 per cent in the productivity of labour. This reveals the magnitude of labour hoarding during the first years of the transition. This lag in the reaction of employment to changes in output has obviously contributed to an increase in overstaffing.

Open unemployment remains almost non-existent. In March 1995, the total number of officially unemployed was 36,200, or 0.4 per cent of the active population. Among the unemployed, only 28,000 were officially recorded as unemployed, the others remaining mainly on severance pay. Since about 34,000 job vacancies were recorded at that time, open unemployment can be regarded as frictional in nature. (Note that the unemployment figures in this paragraph are much lower than the unofficial figures reported in table 2.)

In the absence of labour force surveys, the estimation of effective unemployment rates is difficult. However, a number of indicators give an idea of the magnitude of "hidden" unemployment.

The first indication is the increase in rural employment (see table 3), which, given the considerable decline in agricultural output (almost 10 per cent between 1990 and 1994), surely cannot be regarded as reflecting an increase in the demand for rural labour. Rather,

[1] See Janos Kornai, "The economy of shortage", 1980.

it can be understood as a flow of urban workers who, out of work or facing deteriorating conditions of living in the towns, move into private farming activities.

Table 3. Shift in the structure of employment (percentages)

	1990	1993
Urban	46.6	44.8
Rural	53.4	55.2
Agriculture	40.4	44.6

Source: GKPS.

The second indicator is the number of workers in part-time activities or on unpaid leave. The total number of employees having part-time jobs at the end of 1994 was 31,700, among whom 17,800 had part-time jobs explicitly because of a reduction in production. For the same reason, 41,300 workers were given unpaid or partially paid leave. Altogether, part-time jobs and involuntary leave represent around 2 per cent of total employment in state and private enterprises. This figure continues to be quite low and points to the lack of economic restructuring so far.

2.3. Key features of the labour market

The sectoral distribution of employment reflects the highly distorted structure of the economy, with oversized agricultural and service sectors combined and only a very small industrial sector. Agricultural employment accounts for 45 per cent of total employment, employment in construction and services for 40 per cent and industrial employment for only 15 per cent (see table 4). Within the service sector, 60 per cent of the employed are involved in public services mainly related to transfer payments and social services. The remaining workers are employed in trade, transport and communications. The fact that a very small proportion (only 0.3 per cent of total employment) is involved in the banking and insurance systems points to an inadequacy of the modern service sector with respect to the requirements of a market economy. Industrial activity remains linked mainly to agricultural production, with the main industries being food and textile processing, agricultural machinery and fertilizers.

The large regional disparities in demographic trends and economic activities are a key feature of the Uzbek labour market, and they result in a large dispersion in regional employment. First, large disparities are recorded among the regions in population density (i.e., population per square km) and therefore in labour supply. The highly populated regions — Andijan, Fergana, Namangan — have traditionally been considered "surplus labour" areas while others — Djizak or Surkhandarya — are "labour shortage" areas. The main explanation for the disparities is the comparatively lower economic potential in sparsely populated areas that have low soil fertility and are in need of expensive irrigation systems.

Table 4. The distribution of employment in 1993 (percentages)

Agriculture	44.6
Industry	14.1
Construction	6.8
Services	34.5
of which:	
Non-commercial	24.4
Trade, transport and communications	9.7
Banking	0.3
Other	0.1

Source: GKPS.

Large disparities also exist in the sectoral distribution of activities and employment (see table 5). While agricultural employment accounts for more than 50 per cent of total employment in Andijan, Kashkadarya, Samarkand, Surkhandarya and Korhezm, the share of industrial employment is highest in Tashkent Oblast, Navoi and Samarkand. The labour "shortage" areas, Djizak, Surkhandarya and Kashkadarya, also have very low industrial employment.

Given this regional disparity, the Government has tried, with relatively little success so far, to offer incentives for families to emigrate from labour surplus to labour shortage areas. Homes, personal plots and cattle were freely given to migrating workers. But strong family ties and the traditional reliance on "clan" mechanisms of social protection contribute to the immobility of labour, an immobility which so far persists despite such incentives. The low potential of destinations, and the large inequalities in access to housing and infrastructure, are probably also important factors behind the reluctance of the population to move between regions. The system of residence permits, or the "propiska" system, may also have restricted labour mobility. Whatever the causes underlying this phenomenon, low labour mobility will become an even more serious problem if job losses hit some regions more than others. In particular, dramatic outcomes could occur in so-called "company towns" in the event of mass lay-offs, because migration might well be the only way of getting another job for the displaced workers.

Table 5. Population density and employment by regions and sectors, 1993

	Agriculture	Industry	Construction and services	Total	Population density
Uzbekistan	44.6	14.1	14.3	100	49.6
Karakalpakstan	44.1	9.7	46.2	100	8.3
Andijhan	49.0	15.4	35.6	100	464.6
Bukhara	45.4	12.0	42.6	100	32.7
Djizak	44.4	10.2	45.4	100	41.6
Kashkadarya	53.7	7.9	38.4	100	65.8
Navoi	32.3	21.5	46.2	100	6.6
Namangan	42.5	14.9	42.6	100	215.1
Samarkand	52.8	11.1	36.1	100	145.0
Surkhandarya	56.3	7.1	36.6	100	71.6
Syrdarya	48.3	9.5	42.2	100	121.0
Tashkent Oblast	34.5	21.4	44.1	100	148.0
Fergana	45.7	17.9	36.4	100	337.7
Khorezm	50.1	9.3	40.6	100	185.6
Tashkent city	33.5	18.5	48.0	100	6 382.4

Source: GKPS.

The effect of privatization on employment patterns remains unclear. The privatization process so far has affected only a limited number of sectors, noticeably retail sales, services and light industry. Mostly small-scale enterprises have been privatized, but the majority of large enterprises remains the property of the State. Therefore, over 50 per cent of employment is still concentrated in the state sector. Private ownership (private farms, individual enterprises and personal plots) only accounts for 20 per cent of employment while the other 30 per cent are employed in kolkhoz (20 per cent) and other forms of collective enterprises (see table 6).

The dynamics of employment during the transition process will be determined by the relative paths of the decline of the state sector and the rise of the private sector, with their asymmetric evolution determining the level of unemployment. It is difficult to assess to what extent the new private sector has contributed to net employment creation so far. The proportion of those employed in the private sector has increased, but it is difficult to establish to what extent this is only a result of the transformation of ownership of former state activities or of the dynamics of emerging new private activities. If privatization is the main source of employment growth in the private sector, there may have been no net creation of new employment. Indeed, there might actually have been a net reduction in employment associated with some restructuring of the privatized firms. But the privatization of medium and large-sized enterprises has usually been accompanied by an explicit restriction on the new owners, that prohibits mass lay-offs during a certain period after privatization. This period can last as long as three years. It is reasonable to assume, therefore, that there has been little reduction in the employment in the newly privatized firms. Therefore, although it is difficult to tell how many new activities have really emerged in the private sector, it is unlikely that they have contributed to dynamic employment creation so far.

Table 6. Structure of employment by type of ownership, 1993 (percentages)

State sector and consumer cooperatives	53.6
Joint stock, leased, private and joint venture enterprises	4.8
Kolkhoz	19.4
Social funds	2.9
Individual enterprises	19.3
Total	100.0

Source: GKPS.

2.4. Wages

Under central planning, the structure and evolution of wages were entirely regulated by the State. A minimum wage was set and other wages were calculated as a multiple of the minimum wage to reflect differences in skills and sometimes in state priorities in favour of specific economic sectors. Until now, this system has been explicitly retained for the state sector. It is not entirely clear to what extent the privatized enterprises, as well as those state enterprises whose payroll is not paid from the state budget, are still regulated in this way. It is evident, however, that these firms still have to pay their workers at least the minimum wage, and that thresholds have been set for the different categories of workers. Implicitly, the old system appears to remain in place. It would therefore be correct to say that since the beginning of the transition process both the level and structure of wages have remained under strong state control.

Wage policy has so far been designed to achieve two contradictory objectives: on the one hand it is to prevent real wages from falling too sharply in order to ensure a minimum standard of living for workers, while, on the other, to ensure that real wages move in line with productivity in order to limit inflationary pressures. Since productivity has been falling, this second objective suggests that real wages should decline. A third objective, which is implicit in the policy pursued, is to limit increasing wage dispersion by preserving a strict wage scale in the private as well as in the public sectors.

The first objective has been pursued by the regular indexation of the minimum wage, which, through the coefficient (or multiplier) system, has had repercussions on the entire wage scale. Using official estimates of the price index, it would appear that real wages have not fallen sharply. However this could be misleading because there is considerable uncertainty about the accuracy of measurements of changes in the cost of living. There is no consumer price index so far that is based on a properly constituted basket of consumer goods and the consumption deflators used in calculating GDP have sometimes been revised very drastically.

The second objective has been explicitly expressed in the obligation for firms, since the middle of 1994, to keep wage increases in line with output increases. The control is to be effected through banks, which will not allow total wage payments to grow faster than 70 per cent of the growth rate of a firm's output gross value. In the absence of hard budget constraint, this device is used in an attempt to regulate wage increases in firms that lie outside the state budget. It can be argued that even in small enterprises facing a real budget constraint, this policy is useful. In the absence of an efficient labour market in which wages are determined by the relative pressure of demand and supply for labour there is a danger that even small enterprises will pass on wage increases in the form of higher prices.

In summary, the labour market in Uzbekistan is characterized by a large excess of labour supply over demand. This was acute even under the previous system and the situation has become worse during the transition period. So far, this excess supply of labour has not resulted in large-scale open unemployment because the overstaffing in state enterprises has been maintained and agriculture has absorbed much of the growth of the labour force. This path will not be sustainable in a more market-oriented economy in which firms simultaneously face competition and financial constraints arising from the removal of state subsidies and selective access to credit. Hence there is an urgent need for active policies directed towards the creation of employment to support the structural reforms recommended at the macroeconomic level.

3. Labour market policies: Avoiding unemployment?

With the strengthening of the budget constraint on state as well as private enterprises, redundancies are likely to occur rather quickly, through either the restructuring of firms or bankruptcy of the most unproductive enterprises, especially those engaged in activities with negative value added. At the same time, implementing the reforms on the macroeconomic level will accelerate the development of the competitive private sector. Liberalizing trade and access to foreign currencies, enlarging access to credit for small and medium-sized enterprises in the private sector, improving the quality of banking services, eliminating procurement prices on cotton and grain: [1] all these measures aim at creating an appropriate economic and legal environment for the emerging private sector.

In the long run, the growth of private employment will compensate for the decline in employment in presently overstaffed enterprises. But during the transition period, job destruction is likely to exceed job creation. That is, there is likely to be a temporary deficiency in labour demand because the reallocation of resources to the private sector will take time. In the absence of deliberate action from the Government, there will almost certainly be growing unemployment. This has occurred in almost all transition economies so far, and it is likely to occur in Uzbekistan as well, with the added factor of a very rapid increase in population.

There is therefore an urgent need for an appropriate policy oriented toward easing the imbalances that are likely to emerge on the labour market. Two directions will be examined here. The first is the design of policies to enhance job creation in the private sector. Implementing an adequate legal framework and a favourable macroeconomic environment are obviously the prerequisite to private employment growth. In addition, active labour market policies should be used to improve the functioning of the labour market at least at two levels. Employment services will have to be designed and implemented in order to improve the matching process between vacancies and jobseekers; an appropriate training policy will be required to upgrade and adapt the skills of the labour force. The second direction is concerned with direct public job creation. Here, an extreme scheme will be considered: assuming the Government wants to avoid high and lasting unemployment, it is interesting to discuss the possibility and desirability of implementing a guaranteed employment scheme to address the residual imbalance between the supply and the demand for labour during the transition period.

3.1. Enhancing private sector employment

Employment policy should first concentrate on establishing a favourable environment for the development of private firms. It is important that administrative obstacles — licences, regulations and discriminatory taxes — are removed. In addition, there may also be a need for positive interventions. While market signals should theoretically ensure an efficient allocation of human capital among firms, sectors and regions, this process takes time, and huge market failures are likely to occur during the transitional period. Some intervention by

[1] These economic reforms, recommended at the macroeconomic level in the general report (see ILO/UNDP, 1995, Ch. II) define the broader policy context for the design of labour market policies.

the State in initiating development in particular branches or areas might therefore be necessary.

Given the already oversized agricultural sector relative to the economy as a whole, there are few possibilities for raising employment in that sector. The main line of the employment policy should be to develop industrial activities in rural areas. Food and textile processing are the most promising light industries as they rely on nationally produced inputs, are labour intensive and enjoy good market prospects at home and abroad. In developing new industries, caution is needed when choosing the technology. Excessively mechanized methods of production should be avoided because the comparative advantages of the country are based on a large, well-educated labour force and low labour costs whereas capital is scarce and costly. When alternative techniques of production exist, public as well as private decision-makers should be aware of the relative costs of labour and capital and allocate them in accordance with profit-maximizing criteria.

The experience in other transition economies is that, at the early stage of the transition, the growth in private sector employment has been concentrated in services, which were underdeveloped in the former centrally planned economies. Trade, communications, information, banking, accounting and insurance are sectors where private employment should increase quickly. Therefore the Government should support the development of this sector.

Policies should also be concerned with removing obstacles to the mobility of labour. Apart from eliminating the "propiska" system of residence permits and other barriers to internal mobility, some priority might be given to reducing inequalities among regions in terms of access to good housing and infrastructure. This could be an important part of the public works programme described below.

In the context of the transition, training appears to be an important element of an employment policy aiming to provide positive assistance to job creation. But designing the appropriate training policies may be far from simple. Basically, the restructuring of the economy implies that new activities are to be developed, for which workers coming from old activities might lack the appropriate skills, which in turn could hamper the development of new sectors. Particularly, there seems to be a lack of service-oriented skills — accounting, banking, management — for which training is definitely needed.

But to the extent that the transition period is presently characterized by a slack in aggregate demand, it is very important to be aware of the fact that training is not likely to create jobs *directly*. Therefore, caution is needed when designing training policies, in order to avoid displacement effects. In other words, training should not simply displace one worker for another. Therefore, it might be required to target the training programmes towards certain groups, for example those who have already started a business, in order to help them stay in business and develop, which is in turn likely to generate additional employment. But large-scale retraining of laid-off or redundant workers could prove very expensive and yield low returns, especially as long as the path of new job creation has not clearly emerged and that the new required skills are not properly defined.

3.2. Implementing a guaranteed employment scheme

Regardless of how rapidly the private sector expands, it is unlikely that it will create new jobs fast enough to offset the elimination of old jobs and to absorb the first-time entrants into the labour market. Hence there is bound to be an employment problem for the foreseeable future. One option is to let unemployment increase and implement a system of unemployment benefits to provide the unemployed with a reasonable standard of living. This has been the policy in many other transition economies and it has proved to be rather expensive. Consequently, benefits have frequently had to be cut dramatically when the number of unemployed persons grew and as the base for unemployment contributions, namely, the earnings of the employed, declined. Moreover, unemployment has proved not to be necessary for the reallocation of labour from public to private employment. Often, private jobs have been filled by direct flows from the public sector and the majority of those entering unemployment remained without jobs indefinitely. The problem of long-term unemployment has widely emerged in transition economies, with all the related persistence problems that have long been observed in Western Europe. Thus, unemployment has proven to be an obstacle to restructuring rather than a means of reallocating labour. In many countries, high unemployment has in fact affected the overall reform process, slowing restructuring and discrediting reform governments. Moreover, the experience of large and persistent unemployment in Western Europe has shown how difficult it might be to get unemployment down once it has been allowed to rise and, conversely, that there is a large pay off to preventing unemployment from rising in the first place.[1] It is against that background that we will examine the means to *avoid unemployment* in Uzbekistan.

The means that will be discussed here is the implementation of a guaranteed employment scheme,[2] provided by the Government through a large public works programme. Basically, this programme would act as a residual source of employment for those who could not find a job in private activities; it would thus place a safety net under those who would otherwise be unemployed. The general idea is to substitute an "employment benefit" for unemployment benefits. The former would be superior in that it would utilize otherwise unemployed, and hence unproductive, human resources to create useful income-generating assets. The scheme should of course concentrate on the construction of productive assets, including investments in infrastructure projects, that can be expected to contribute in future to sustained higher levels of output and income. Given the poor quality of the infrastructure, the inadequacy of communication services, the large inequalities in housing between regions, the need to improve the environment, and the urgent need to restore some of the historic national monuments, there are a number of opportunities to use labour productively to remedy clear cases of public underinvestment. The public works programmes should be designed so that they can address both chronic unemployment and the seasonal unemployment common in rural areas.

Public works schemes of the type recommended above face two sorts of criticism. The first is a general criticism of public works, namely, that they are likely to displace resources, either capital or labour from the private sector, or to act as a substitute to private activities that cannot compete with public programmes functioning on public subsidies or lower wages. The second criticism is concerned more directly with the concept of a guaranteed employment programme, namely, that it interferes with the operation of the labour market. The argument is that if the State guarantees employment so that the demand for labour automatically matches its supply, the labour market may not be able to achieve two of its basic functions, namely, to allocate labour among competing activities and to determine the level of wages through the forces of demand and supply.

[1] This is a conclusion drawn by C. Bean in his extensive survey of European unemployment (1994).

[2] This idea has been developed by Keith Griffin and Terry McKinley, 1994.

These criticisms might be relevant if labour employed in public works were treated in exactly the same way as workers in other segments of the labour market. Employment in public works, however, differs from employment in other sectors of the economy in one crucial respect: the wage rate is deliberately set at a level designed not to attract workers from other jobs. The purpose of the scheme is to provide work only to those who cannot find other sources of employment. The wage rate, therefore, should be set below the wage offered in the private economy for the same category of work. This would discourage workers from seeking employment in public works projects if work is available elsewhere and thus ensure that the public works scheme does not create a shortage of labour for the private sector. Experience in other transition economies, especially in Poland, suggests that the participation in public works declines as the demand for labour in the overall economy recovers, thus supporting the view that these programmes do not crowd out other forms of employment.

If the wages paid to workers employed in public works projects are fractionally lower than wages paid in the rest of the economy, as we recommend, then the wage in the guaranteed employment programme will play the same role as unemployment benefits in economies which tolerate open unemployment. The only difference is that under our proposal labour resources are utilized rather than allowed to remain idle. Under our proposal there would be a competitive labour market, where demand and supply would determine the evolution of real wages. In addition, in the public works programme, workers would still have an incentive to enter into "competitive" employment just as if they were unemployed. The pool of workers engaged in public works would have similar effects on the "competitive" labour market as would a pool of unemployed workers: their presence would put pressure on real wages because they would remain in competition with those who have a regular job.

Another criticism directed towards public works schemes is that such public activities displace private activities as they benefit from state subsidies, lower labour costs, and guaranteed markets. This perverse effect is all the more undesirable in a transition economy since the principal aim of the structural and economic reforms — and to a certain extent the principal means of the transition process — are precisely the privatization of formerly public activities and the emergence of new private firms. In order to avoid such displacement effects, it will be necessary to impose a principle of additionality [1] on public works programmes: they should be designed of such a character that they would not otherwise have been undertaken. For example, they should be limited to areas in which there has been a clear underinvestment from the State. Hence there is no danger that the public works programme would simply act as a substitute for activities and jobs that would otherwise be created by private enterprises.

The public works programme we recommend has broad similarities to the Swedish labour market policies that existed until the late 1980s. In Sweden, after a short period of unemployment, the unemployed were automatically reintegrated into various state programmes. They were either directly given public jobs, or integrated in relief work programmes or in training programmes. Recruitment subsidies were also used on a large scale. There is little evidence that this accentuated inflation or crowded out private sector employment. [2] It is often claimed that guaranteed employment programmes are expensive and can be sustained only as long as the pool of workers seeking employment is not too large.

[1] For a broader discussion of public works programmes, see L. Calmfors: "Active labour market policy and unemployment — A framework for the analysis of crucial design features", OECD *Economic Studies*, spring 1994.

[2] For a detailed study of the Swedish active labour market policies, see L. Calmfors: "Lessons from the macroeconomic experience of Sweden", *European Journal of Political Economy*, 9, 1993.

Actually, a detailed study of labour market expenditures among different countries shows that such programmes are in practice virtually self-financing in terms of the unemployment benefits saved. [1]

In Uzbekistan, moreover, such a scheme would be less costly, in terms of economic efficiency, than the "disguised unemployment compensation" that exists at present. Hence the cost of the public works programmes should not be too much higher than an unemployment benefit scheme. The level of benefits would be the same, the duration of the programmes would be similar, and the other additional costs could be kept at a low level. The projects should be designed in such a way that labour costs account for a large proportion of total costs. In an intertemporal macroeconomic sense, in fact, the programme should be self-financing, since if investment projects are selected carefully, they should generate a stream of future benefits that exceeds the initial costs. Nevertheless, in the short run, the scheme involves net outlays from the state budget. It will therefore have to be financed out of general government revenues.

Here is one crucial difference between the guaranteed employment scheme and an unemployment benefit scheme. While in the majority of countries the latter is financed through an insurance system, with the workers insuring themselves against the risk of being unemployed, the public works programme functions like a welfare programme, financed out of the general budget. In this case, a lack of employment opportunities is regarded not as a particular risk faced by certain members of the population, but as a national problem that involves the whole society and requires national solidarity. The same issue is present in Western countries, where there is now a debate on the best way to finance unemployment benefits: should they be financed from social contributions or from income taxes? The answer depends in part on whether one regards unemployment as an individual or a collective problem. Given the high probability that unemployment will increase suddenly and massively in Uzbekistan if the reform process accelerates, the concept of unemployment as a "national catastrophe" would appear to be appropriate.

Furthermore, to replace a system of unemployment benefits by a guaranteed employment scheme is potentially attractive in Uzbekistan in part because open unemployment has not become a major problem. Hence, during the early stages, the costs of implementing a public works scheme will not be high. The difficulty of financing a guaranteed employment scheme through the state budget is primarily a question of priorities and should not be exaggerated. If the provision of employment is regarded as sufficiently important, both for the individuals concerned and for the contribution employment can make to faster growth, it should be possible to raise additional public revenues or to reallocate public expenditures from lower priority activities.

The projects included in the public works programme should be carefully selected. The main criteria should be: (i) that they are labour intensive, since a primary purpose of the scheme is to act as a residual source of employment for those who otherwise would be unemployed; (ii) that they concentrate on activities where there has been an obvious underinvestment by the State; and (iii) that priority is given to investments that result in the creation of permanent assets which can raise future output and income. If these basic guidelines are followed, the guaranteed employment scheme should be cost effective compared to a passive unemployment benefit scheme.

[1] For example, Bean (1994) argues that "the overall cost of unemployment including benefits was virtually the same in Sweden as in the United Kingdom at 2.6 per cent of GDP".

Other criteria are also relevant. For example, those regions that are presently poorly provided with infrastructure or housing might be especially targeted. This could be part of an overall policy aiming to increase labour mobility and easing population pressure in some regions. When possible, projects should be designed to create skills or to provide some training so that they improve the workers' chances of finding a job in the competitive sector. A frequent criticism of public works is that they do not provide effective ways of reintegrating the unemployed into the economic mainstream. Improving not only the stock of physical capital through public investment but also the human capital utilized on public works projects would increase future income and output. One should not ask the guaranteed employment scheme to do too much however, or raise expectations too high. If it ensures that everyone has a job, that output is increased and that everyone has a sense of participation in worthwhile economic activities, that will be a considerable achievement.

4. Wage policy

The type of wage policy that should be implemented during a period of transition from a centrally planned to a market economy raises several issues. First, there is the micro-economic logic of the labour market, according to which the allocation of labour should be determined by the free movement of relative wages. Second, there is the macroeconomic outcome associated with the employment-wages trade-off when there is an excess supply of labour. Third, there is the economic policy issue of controlling inflation originating from a price-wage spiral. We shall comment briefly on these three issues.

4.1. The structure and level of wages

The essential function of the labour market in a market economy is to allocate labour resources optimally. This is achieved through the movements of relative wages and the emergence of a wage structure that reflects the marginal productivities of different types of workers. This has two consequences, first on the structure of wages and second on their evolution.

First, large inequalities in compensation among different types of workers may be required on efficiency grounds: if the marginal productivity of an engineer is much higher than the marginal productivity of a low-skilled worker, then the salary of the former will be much higher than the salary of the latter. This wage structure will provide incentives to become an engineer. Without such an incentive, the supply of engineers could fall short of the demand. Hence an unfavourable effect of an egalitarian wage structure could be a shortage of high-skilled, high-productivity workers. This is the textbook case. The reality of the labour market is of course much more complex. For example, the behaviour of the worker is certain to be influenced by other factors, such as the intrinsic interest of the work, general working conditions, etc., in addition to the wage. In practice, there is no clear relationship between the extent of wage differentials and efficiency in resource allocation.

Second, the evolution of real wages will be influenced by the evolution of the demand for labour, assuming the supply is relatively inelastic. A decline in the demand for labour will therefore result in a decline in real wages while maintaining full employment. In that case, high unemployment should not occur in the long run. In practice, however, a number of market economies have experienced high and lasting unemployment. Two elements can be identified to explain this phenomenon.

Initially, some downward real wage rigidity has been registered. Various factors have been said to account for this rigidity, among which the most popular and most emphasized is the role played by labour market institutions. However, recent studies have shown that those have actually had only a small and sometimes ambiguous impact on wage evolutions and employment creation. [1] A more satisfactory explanation is given by the efficiency wage theory. It is claimed that there exists a wage level, the "efficiency wage", below which it is not in the interest of the firm to pay its workers. Firms are assumed to have imperfect

[1] See *World Employment Report 1995*, ILO, for an international analysis of the relationships between labour market regulations and employment.

information about individual employee's productivities [1] and are thus unable to make their wage offer contingent on their employees' performance. Consequently, firms may have an incentive to keep the wage above the level that would be necessary to ensure full employment. In other words, since it is assumed that the firm is unable to control the effort of its workers on the job, setting too low a wage would result only in lower incentives for the worker, less effort and lower productivity. It thus can be shown that it is cost effective for the firm to pay at least the efficiency wage even if excess supply in the labour market would allow the firm to pay lower wages.

The second factor explaining poor labour market outcomes lies in the poor macroeconomic environment that has characterized market economies since the first oil shock. In fact, wages are not the only determinant of employment creation. In their decision to hire or fire workers, firms are primarily concerned by the future evolution of their production, and only secondarily by the relative cost of labour. Therefore, a lasting insufficiency in job creation is to be explained mainly by the low production expectations that are associated with an insufficient level of aggregate demand, and only marginally by too high a level of wages.

The micro-economic view of the labour market has two implications for economies in transition. First, the labour market should be allowed to function freely and to determine a new, and much less egalitarian, wage structure. This requires high labour mobility and the removal of all administrative controls on the wage scale. Second, although employment decisions are highly influenced by factors other than labour costs, it is nevertheless true that in situations like the present when the productivity of labour is so much lower than the cost of labour, real wages should be allowed to fall to a low level too. But how low? This is the question we address in the next section.

4.2. Is there a trade-off between employment and wages?

Emphasis has often been put on the trade-off between wage rates and employment levels. It is sometimes argued that the level of employment can be maintained if real wages fall to the level of the marginal productivity of labour. While this is theoretically true at the firm level for a profit-maximizing behaviour, on the macroeconomic level the links between employment, labour productivity and wages are more complex.

Actually, in the former socialist economies, large transfers through subsidies allowed the maintenance of a total wage bill that was not in line with the gross output of state-owned industrial enterprises. In effect, workers were highly subsidized by the State, and the subsidies were usually financed by squeezing agriculture through low procurement prices. State enterprises were characterized by serious overstaffing that resulted in low apparent productivity per worker. Although real earnings were quite low, real wages were not kept in line with labour productivity. It appears therefore that both employment and real wages will have to fall during the transition process.

In effect, when enterprises are ultimately forced to face a hard budget constraint, the total compensation of employees will have to fall for two reasons: (i) to adjust to the removal

[1] This criticism addresses a crucial assumption underlying the micro-economic theory of labour market: firms are assumed to set employment at such a level that the marginal productivity of labour equalizes the real wage. As marginal productivity is decreasing when employment increases, setting a lower real wage results in more employment. But in reality, it is extremely difficult for a firm to determine the exact level of its workers' marginal productivity and the relationship between real wages and marginal productivity might well be very weak.

of explicit and hidden subsidies from the State; and (ii) to adjust to the fall in output that almost always accompanies the transition. In theory, this adjustment could be achieved in two ways. If real wages were to be maintained at their former levels, large lay-offs would have to occur, raising the productivity of labour until it is compatible with the level of real wages. Alternatively, a high level of employment could be maintained, but only at the cost of low labour productivity and low real wages.

This logic, however, does not reflect the reality of the production process. The main problem is that labour productivity is not totally endogenous to hiring and firing decisions but is also influenced by characteristics of the techniques of production and by the exogenous pace of technical progress. Given a certain technique of production, the firm must allocate a certain number of workers to its machines. This number is neither totally fixed, nor totally flexible, and investment by the firm can of course lead to changes in the labour intensity of production, especially in case of large variations in the relative cost of labour to capital. But this change in labour intensity only occurs on the fraction of capital that is renewed through investment. Therefore, the degree of labour intensity in the economy changes rather slowly. Of course, the rate of turnover of the capital stock increases with the level of gross investment, and therefore the employment-wage trade-off depends very much on the level of investment. In the long run, neither relative prices nor the characteristics of the technology at a given moment in time are as important as the pace and composition of capital accumulation which is mainly determined by economic growth and by the evolution of technical progress.

It follows that it is largely an illusion to believe that massive job losses in overmanned state enterprises can be avoided by a large decrease in real wages. Rationally behaving firms will first re-establish the level of employment that is required by the existing techniques of production and compatible with the level of output, and will in the longer term change the techniques of production in order to catch up with Western standards of productivity. It is conceivable that for a relatively short period a consensus could be reached among firms, workers and the Government to favour employment at the expense of real earnings. But given the required decrease in the wage bill, it is very unlikely that this kind of "consensual job-sharing" would be acceptable to the parties concerned, or enable the economy to make the required adjustments.

This has an important implication for wages. The objective of the Government should not be to use a reduction in real wages to sustain employment in firms where the workers are presently employed. Instead, firms should be allowed to set wages as they see fit, presumably at a level that reflects the productivity of labour in the enterprise and conditions in the labour market. This does not mean that all administrative controls should be removed, but they should not be used to attempt to influence the trade-off between employment and wages. Indeed, it can be argued that wage policy should be used solely as a tool to regulate inflation. This is the subject to which we now turn.

4.3. The control of inflation

In a market economy, wages have a central role to play in controlling inflation. If an enterprise is a "price maker", it will set its prices by applying a more or less fixed margin to unit costs of production, of which labour costs are the most important. Hence, every increase in unit labour costs will result in a price increase. To keep unit labour costs unchanged, real wages will have to increase at the same rate as labour productivity. Every increase in real wages that outstrips the increase in productivity will be inflationary. This is how the so-called "price-wage spiral" functions. In this framework, the regulation of real wage increases is fundamental. In a market economy, this function occurs through the relative pressure of the supply and demand of labour: if the supply exceeds the demand, e.g., if there is unemployment, workers will be in a weak position to defend their wages, and real wage increases will be moderated. The only desirable effect of unemployment in a market economy is to keep real wage increases in line with productivity gains and thereby prevent inflation from rising.

Given the very rapid inflation Uzbekistan faces, wages and prices are likely to continue chasing each other indefinitely unless a regulatory mechanism is introduced. In the absence of a hard budget constraint, firms can increase wages as much as claimed by their labour force, and workers in the absence of unemployment have very strong bargaining power.

There are only two ways to stop high inflation, namely, by reducing real wages or by reducing profits. Each method contains the price-wage spiral. While a reduction in real wages prevents unit labour costs from increasing, a reduction in profits (by a strict control on prices but not on wages) is likely to result in widespread bankruptcies and, in the end, lower incomes for workers and rising unemployment. That is why, given the terms of the debate, wage moderation is crucial. Hence the present policy of the Government of controlling strictly the overall increase in real wages can be justified, especially since wages are not allowed to be regulated by varying the level of unemployment. However, a policy of wage controls is certain to fail unless it is supported by a tight budget constraint on enterprises. Otherwise firms will take advantage of the situation to increase their prices and their profit margins.

In a context of "normal" inflation, that is an inflation rate which is compatible with a proper evolution of relative prices, the evolution of the general level of prices still has a great importance because it is the main determinant of the external competitiveness of the economy. Therefore, inflationary pressures should always remain under control and carefully regulated. In that regard, the characteristics of the wage-setting institutions are crucial.

4.4. Wage-setting institutions

Unemployment, as an indicator of the tensions occurring in the labour market, is a key variable in the regulation of inflation. But the institutions also matter, particularly the characteristics of the wage bargaining process between workers and employers. This bargaining process can be pursued in a centralized manner: wages are determined on a national basis and extended automatically to all branches of the economy. This requires tripartite agreements between employers, workers and sometimes the Government. On the opposite, wages can be determined in a totally decentralized manner, e.g. directly between the employer and its employees at the firm level. The "middle way" is to set wages at the level of branches or sectors. The evidence on the superiority of any of these systems, superiority in the sense that one system would ensure the best control over inflationary pressures, is far from clear cut, despite that there have been some theoretical and empirical findings that totally centralized and totally decentralized systems were to achieve better outcomes than more "mixed" systems.

Beyond the debate over the optimal degree of centralization or coordination of the bargaining process, the discussion on the opportunity to create, to keep, or to strengthen trade unions and tripartism in general involve other key issues. In the particular period of transition, tripartite consultations, involving workers, employers and government, could help create a social consensus, mobilize support for the political and economic changes under way and promote acceptance of the social costs involved; "strong workers' unions could be conducive to organizing mass protests by those who suffer from transition; they would provide information flows to governments about programme failures and pressure them to bring about potentially valuable changes in the direction of programmes". [1] If all parties were associated in the taking of decisions, the outcomes of the process would indeed stand a better chance to be perceived as equitable by all concerned and to be effectively implemented.

For all those reasons, tripartism and a centralized wage bargaining process would probably be the most appropriate institution in the context of the transition. Nevertheless, the present situation does not allow such tripartite consultation to be undertaken. Given the legacy of the former system, there is still a unique official trade union that represents over 96 per cent of all workers and only weak and non-experienced employers' trade unions. In this particular context, tripartite agreements are very unlikely to result in appropriate wage settings.

Decentralized wage bargaining will not be desirable as long as there is no tension in the labour market, in the form of open unemployment, to regulate wage increases. Therefore, as long as this situation remains unchanged, an administrative control over wage setting will still be required.

In conclusion, what can be said on the optimal wage policy in the particular case of Uzbekistan? First, the micro-economic theory of the labour market implies that the wage structure and level should establish freely according to the demand and the supply of labour. This should lead to the creation of much larger inequalities in the compensation of the different types of workers than it is the case nowadays. The maintenance of a relative egalitarian distribution of income might be a sensible political choice, but labour market theory shows that inequalities should not be addressed through wage equalities. Rather should such inequalities be reduced through public transfers. [2]

According to the micro-economic rationality, there should be no state intervention at all in wage setting. But this comes in strong contradiction with macroeconomic outcomes, as wages are a crucial element in the inflationary process and cannot, in the particular case of Uzbekistan, be regulated by the market through unemployment, nor in a centralized bargaining process that would be aware of including explicit inflationary targets in the wage negotiations.

Therefore, there seems to be definitely a need for state control over real wages evolutions. But only the overall increase in real wages should be regulated. The structure of wages should be left for the market to determine. How should this control be implemented? The strengthening of the budget constraint on firms will not be sufficient. Of course, with the removal of state subsidies, firms will have very strong incentives to reduce wage costs, but it is not clear that they will be able to resist to the pressure of workers. They will still have the possibility to pass excessive wage increases on to price increases, feeding the price-wage dynamics. Presently, Uzbekistan imposes a penalty tax, at the firm level, for the portion of

[1] Freeman, R., 1993.

[2] This has been realized, for example, in Sweden, where the dispersion of wages, measured through Gini coefficients, is not larger than in other OECD countries but where the dispersion of disposable incomes is much lower due to a vast transfer system.

wage increases that exceeds output growth. The unwanted side-effect of this sort of policy is that it might impede the development of private firms, as there often exist long delays between a hiring decision and the time when the final product is sold. Therefore, especially in the emerging private sector, a policy relying on tax-based incentives appears more suitable.

5. Conclusion

This paper has surveyed labour market issues in the context of a policy of subsequent macroeconomic stabilization and accelerated transition towards a more market-oriented economy. The salient point is that the present situation of full employment will not be sustainable in the future, at least in the form that has been known during the period of central planning. Large labour market imbalances will develop with the implementation of a strict anti-inflationary policy and the acceleration in the pace of structural reforms. Particularly, an important decline in employment is to be expected when firms, be they private or public, will face a hard budget constraint. Indeed, the removal of the currently extensive state subsidies, which is required for both anti-inflationary and economic restructuring purposes, will inevitably convey to the closure of the most inefficient firms and the dismissal of a large number of presently redundant workers. Moreover, in the context of a rapidly growing population it is very unlikely that the expected decline in the labour force participation rates will be sufficient to meet the reduction in employment. Therefore, unemployment on a large scale is to be expected in the near future. At the same time, the fight against hyperinflation and the necessity for firms to bring wages back in line with low labour productivity will translate into rapidly falling real incomes.

Those growing tensions on the labour market will have to be addressed through adequate and courageous labour market policies if Uzbekistan wants to avoid a major social disruption. In return, the maintenance of social cohesion will be a critical factor for the success of the overall transition process. The Government will need broad and continuous support among the population for the implementation of reforms. It might lose this support if the short-term consequences appear too harmful.

The rôle of labour market policies will be twofold. First they will have to accompany and ease the reallocation process of employment from former inefficient to emerging competitive activities. In that regard, both employment services and training schemes will be essential. Extensive and efficient employment services will be required to improve the matching process between a rapidly changing pool of vacancies and a growing pool of unemployed. Particularly important will be the availability and the rapid diffusion of information concerning job opportunities. Appropriate training schemes will also be essential to upgrade the skills and abilities of the labour force in line with the requirements of the new market activities. Second, labour market policies will have to alleviate the tensions that will develop with the reduction in employment against a background of a demographic boom. A first option would be to allow for the emergence of large open unemployment, and elaborate a system of more or less generous unemployment benefits. For many reasons explained in more detail in this paper, we are not convinced that such a passive scheme is the most appropriate solution.

In this paper we have presented and discussed an alternative possibility: the implementation of direct public job creation on a large scale. Not only theoretically, but also practically, this solution seems feasible, desirable and best suited to the current situation in Uzbekistan. At the macroeconomic level, this policy would be the essential pillar of a strategy aiming at the renewal of growth, providing simultaneously a guaranteed level of earnings to sustain private consumption and a direct boost to capital accumulation through public investment. On the labour market, it would keep workers in the mainstream of the working life, avoid the deskilling effects that usually accompany long periods of unemployment and hence prevent the development of persistence effects that have proved so harmful in Western

European economies. In a social perspective, the scheme would provide every worker with at least a satisfactory level of income. The side-effects usually associated with public jobs creation could largely be avoided with an appropriate design of the public works projects: the wage rate paid on these schemes should be set at a level ensuring that public activities do not crowd out labour resources from the private sector, and one of the criteria in selecting the projects should be that they would not have otherwise been realized by the private sector. Finally, it is necessary to complement the employment strategy with an adequate wage policy to ensure that the structure and level of wages reflect simultaneously the conditions of production and the real degree of tension in the labour market, and that inflation remains under control.

If properly implemented, the guaranteed employment scheme could play a crucial role in the success of the transition from a centrally planned to a market-oriented economy. Its essential contribution would be to avoid large-scale and prolonged unemployment, a problem which has been a major obstacle to implementing structural reforms elsewhere. This is especially true in countries where, given the legacy of state-provided full employment in public enterprises and collective farms, unemployment is seen as both a major failure of state policy and as a dramatic retrogression in the living conditions and the social status of the worker. The guaranteed employment scheme should also be regarded as a major vehicle for producing income-generating assets, through the improvement of physical as well as human capital, and thus it should become a major component of the overall development policy of Uzbekistan.

Abstract

This paper identifies the nature and magnitude of the disequilibria that will arise on the Uzbek labour market if a policy of subsequent macroeconomic stabilization and accelerated transition towards a more market-oriented economy is to be implemented. The salient point is that the present situation of full employment will not be sustainable. An important decline in employment is to be expected when firms face a hard budget constraint. In a context of a demographic boom, this reduction in employment will lead to large open unemployment. At the same time, the fight against hyperinflation and the necessity for firms to bring wages back in line with poor labour productivity records will translate into rapidly falling real incomes. These features are potentially explosive from a social point of view and might well hamper the whole transition process. In this context, the paper then discusses a set of labour market policies designed to address those growing imbalances while preserving the process of economic stabilization and restructuring. In addition to policies that will ease the reallocation of employment from former/inefficient to new/competitive activities, e.g. the development of employment services and training schemes, particular emphasis is put on direct public job-creation schemes. The strengths and weaknesses of such schemes are presented. The paper comes to the conclusion that if they are properly designed, such schemes implemented on a large scale could play a central role in the transition process while their unintended side-effects could be largely circumvented. Particularly, a guaranteed employment scheme would avoid the large-scale and prolonged unemployment which has been a major obstacle to implementing structural reforms elsewhere. It would definitely buy strong support for the transition process among the population, and at the same time contribute to the improvement of physical as well as human capital. It should thus become a major component of the overall transition and development strategy in Uzbekistan.

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