

## **PART 1:**

# **INTRODUCTION: SURVEY OF ECONOMIC AND SOCIAL CHALLENGES IN SOUTH EAST EUROPE**

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## **Labour Markets and Employment Development in South East Europe**

### **Introduction**

In contrast to the Central European transition countries, the economies of South East Europe (SEE) have been facing complex and interrelated political and economic problems. The dissolution of Yugoslavia combined with market losses, war in Bosnia and Herzegovina and Croatia, sanctions finally culminating in the Kosovo conflict were the main causes of political and economic instability in the whole region. Taking into account these factors, output recovery has been much slower in SEE than in the Central European countries. Measured in purchasing power standards, Croatia is the best performer in the region, with its GDP at about 38% of the EU average. Next comes Bulgaria (32%), whereas the respective values for Serbia and Montenegro and Albania range between 15-17%. Looking at the economic performance in the 1990-2002 period, Croatia and Romania reached almost 94% of their pre-transitional level in 2002, followed by Bulgaria and Macedonia (about 88% each). Serbia and Montenegro, the worst-affected, reached only about half of what it was in 1990. The cumulative output decline there was one of the largest among all the Central and East European countries.<sup>2</sup>

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<sup>2</sup> In contrast, Poland had surpassed its pre-transition level by 56% and Slovenia by 35% in 2002.

Despite the resumption of economic growth in most of the countries there was no essential improvement on the labour markets in the South East European countries over the past years. In 2002, only Bulgaria and Croatia showed a slight employment increase. In Bulgaria the turn-around was mainly due to a recovery of some manufacturing branches contributing to net job creation as well as active labour market policy measures and the launching of public works programmes (ECE 2003). New jobs in Croatia were mainly provided in the services and construction sectors, the latter due to motorway construction.

### **Demographic trends**

Population data of the former Yugoslavia have to be taken with caution due to the war in the region and the following waves of refugees, especially for the successor states. During the past decade – apart from the extreme case of Bosnia and Herzegovina – population decreased significantly also in Bulgaria, Romania and to a lesser extent in Croatia, fell slightly in Serbia and Montenegro and remained almost unchanged in Macedonia (See table 1 in Annex).

Albania is the only country reporting a remarkable increase in population over the 1991-2001 period. Between 1989 and 1996 more than half a million people left Bulgaria, which was up to 1993 mainly due to the emigration of Muslims to Turkey. Later on, the poor economic situation caused well-educated (young) people to emigrate either to the USA and Canada or to Western Europe. In Bulgaria these developments have led to a considerable depopulation of large areas of the country, mainly the underdeveloped, border and mountain regions (ETF 2000a). The steady population decline in Romania from 1991 onwards was caused both by the negative natural increase and net outward-migration. Similar to Bulgaria, a remarkable size of educated youth has been leaving the country every year. The brain drain problem is a common feature of all SEE countries. Estimates for Bosnia and Herzegovina in the 1996-1998 period put the number of highly qualified who left the country at 42000, three quarters of which were below 40 years of age. During the first

years of the 1990s about 17000 young qualified people left Macedonia (ETF 2000b). A strong outflow of qualified labour was reported also for Serbia and Montenegro. Triggering a steep increase of legal and illegal emigration mainly to Greece and Italy<sup>3</sup> about 40% of the university professors and researchers have left Albania over the 1990-1999 period. Apart from a sizeable external migration, Albania faced an internal mass migration from rural to urban areas (UNDP 2000, p. 46).

In most countries the share of the working age population (15-64 years) accounts for roughly two thirds of the population. With the exception of Albania all countries report an increasing share of people older than 65, the proportion of which is highest in Bulgaria. Ageing of the population is becoming also a problem in rural areas of Romania where the elderly are the majority of the population. Data on Serbia and Montenegro are not available. In accordance with the rising shares of the productive and post productive age groups, the share of young people up to the age of 14 years has been on the decline. The proportion of the pre-productive age group is highest in Albania (32%) and in Macedonia (25%) and lowest in Bulgaria (16%).

## **Employment**

All countries in South East Europe, except Serbia and Montenegro, have been facing dramatic employment cuts over the last decade, by more than one quarter on average (See Figure 1 in Annex). Apart from Bosnia/Herzegovina, Macedonia and Bulgaria were affected most, suffering job losses by almost one third over the 1989-2002 period; in Romania employment fell by about 30% and in Albania by 26%. In Serbia and Montenegro the number of jobs was by about one fifth lower than in

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<sup>3</sup> The majority of emigrants are males in the age between 20 and 30 years. Emigration is mainly driven by economic reasons. Most of the Albanian emigrants are temporary or seasonally employed. About half of the emigration is illegal nowadays, at the beginning of the 1990s this ratio was almost 90% (UNDP 2000, Telo 1999).

1989, and in Croatia by 16%. However, based on health insurance data the employment decline in Croatia was among the highest in region, down by 28.5%.<sup>4</sup> Roughly speaking about 3.3 million jobs got lost in the 1990-2002 period and a big share of the workforce has exited from the labour market altogether, with a growing number of discouraged workers.

Declining employment is clearly reflected in the steady drop of activity and employment rates over the 1996-2002 period (See figure 2 in Annex). Available LFS data indicate a fall in all SEE countries for both men and women (except Macedonia, where the female employment rate increased). Croatia and Romania are by far hardest hit, with the employment rate down by 9 and 8 percentage points. In all countries economic activity rates (labour force as a percentage of the working age population 15-64 years) were lower than the EU average.

The employment population ratio (employed as a percentage of total population) remained stagnant, but low in most of the countries (See figure 2 in Annex). In Macedonia only 27.5% of the population are employed, followed by Albania, Bulgaria and Croatia (30-35%). Romania reports the highest (but also declining) ratio, at 44.6%<sup>5</sup>, slightly below the EU average of 45.4%.

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<sup>4</sup> LFS results, published since 1996 have to be taken with caution as well, as up to the second half of 1999, parts of the Croatian territory (Krajina and Eastern Slavonia) were not included in the sample frame. This might explain the different employment developments between 1999 and 2000, with the Statistical Office data reporting a 3% employment decline and the LFS data (for the first half of the year each) an increase of 2%.

<sup>5</sup> All these ratios are biased as they do not include employment in the shadow economy.

## 2.1 Employment patterns

Since the beginning of transition SEE countries have been undergoing a rapid de-industrialisation process, while employment in services and agriculture remained high. The latter differs quite substantially from developments observed in the central European transition countries, where everywhere except Poland a rapid urbanisation process is under way (See figure 3 in Annex).

Apart from Albania employing some 70% of the total workforce in agriculture, Romania is the most outstanding example where agricultural employment amounted to 35% of the total in 2002 based on LFS data. Agriculture still accounts for about one quarter of total employment in Bulgaria and about 23% in Macedonia. Also in Croatia, agriculture still plays an important role absorbing about 15% of total employment in 2002. Like Slovenia, registration data reveal a much lower proportion of those employed in agriculture than the labour force survey does. Data on the sectoral composition of employment in Serbia and Montenegro are not available; but based on the information obtained from the labour force surveys, the proportion of agricultural employment may account for an estimated 22% of the total. In general one may conclude that the inflow of laid off labour from the industrial and construction sectors to agriculture was eased through the emergence of numerous small farms after the privatisation of large state owned agricultural enterprises; thus agriculture acts as a buffer or shock absorber against unemployment (UNECE 2000, p. 105).

A common feature of all SEE countries is the sharp contraction of industrial employment (including construction). Apart from Bosnia and Herzegovina the rate of decline is highest in Bulgaria and Romania, where more than half of industrial jobs got lost over the transition period, in Macedonia close to 50% and in Croatia more than 40%. In SEE the proportion of industrial employment is smaller than in the most advanced

transition countries, accounting for less than 30% of total employment.<sup>6</sup> Only in Macedonia does the share of industrial employment exceed that mark with a proportion comparable to Hungary (about one third of the total).

The services sector is underdeveloped by European standards but also in comparison with Central European transition countries. Apart from the extreme value of Albania, where the services sector absorbs only about one fifth of total employment, that sector is most developed in Croatia, absorbing more than half of total employed.<sup>7</sup> Compared to other countries of the region there was a dynamic development in the Croatian services sector (especially in tourism, but also in transport) already in the seventies and eighties percentage points. Services sector employment differs substantially across countries and sectors. Altogether we observe an upward employment trend in 1) wholesale and retail trade in all countries, except Macedonia, 2) real estate, and other business services including legal services, accounting, engineering in all countries except Romania (not explicitly shown for Serbia and Montenegro) and in 3) public administration and defence (except Croatia). In contrast, employment fell in a) transport and communication, b) health, social work and c) education. Developments in other segments of the services sector were rather diverse.

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<sup>6</sup> In Slovenia and the Czech Republic, industry and construction account for almost 40% of total employment.

<sup>7</sup> The services sector employment accounts for about 58% in Hungary (the most 'advanced' country).

## Unemployment

Following the sharp contraction of employment, the number of jobless (and accordingly the unemployment rate) grew strongly in all SEE countries, except Serbia and Montenegro<sup>8</sup> (See figure 3 in Annex). Apart from the extreme case of Macedonia (37%) and Bosnia, where the unemployment rate ranks between 37 and 39%, in the first half of 2003, Serbia and Montenegro reports one third of the labour force being registered as unemployed, Croatia and Bulgaria record a decline in registered unemployment rates to 19% and 14% respectively.<sup>9</sup> Romania is the only exception, posting a rate of about 7%, which suggests that most of the (industrial) restructuring remains to be done.

In all successor states of the former Yugoslavia and to some extent in Romania the registered unemployment rate tends to be higher than the rate obtained from labour force surveys (LFS). The largest discrepancies occurred in Croatia and in Serbia and Montenegro where the registered unemployment rates were by 7 and 12 percentage points higher than the LFS rate, in Romania the difference was about 3 % in 2002. Incentives

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<sup>8</sup> Though reporting high levels of registered unemployment both in relative and absolute terms, over the last decade the number of jobless increased less dramatically in Serbia and Montenegro than in other countries of the region. During the period of UN sanctions against Yugoslavia layoffs were prohibited and paid leave very common. Disguised unemployment has been growing steadily during the past decade and was estimated at some 30-40 % of the employed (Arandarenko 2000). Taking into account that the privatisation process is only at the beginning, unemployment is expected to further increase in the years to come.

<sup>9</sup> Figures for registered unemployment especially in the successor states of the former Yugoslavia may overstate the actual number of unemployed. Results obtained from the LFS conducted in these countries indicate much lower jobless rates. These discrepancies might be explained by the fact that a large number of registered unemployed is in *de facto* self-employed in agriculture or works in the informal economy and/or registered unemployed are often not actively seeking a job to they register in order to be insured (see also UNECE 2003, p. 75).

for registration either for those who are working in the informal sector or who are simply unwilling to work are the possibility to be covered by health insurance or to receive some other social benefits. In 2002 in Croatia, a total of 136000 or 39% of the average registered unemployed in this period did not fulfil the international criteria of unemployment either because they did not seek a job (38%), did not accept a job offered (15%) or they worked unofficially (41%).

Although there are substantial inter-country differences, several common features of unemployment can be identified: 1) long-term unemployment is extremely high, 2) youth unemployment (job seekers without working experience) has been increasing rapidly, for example in Serbia and Montenegro about two thirds of the unemployed are first time job seekers. 3) the lowest skill and educational groups are over-proportionately affected and 4) unemployment levels among ethnic minorities and other socially disadvantaged groups are many times higher than the average rate.

The share of unemployed who have been out of work for more than one year can be seen as a guideline indicator of the extent of structural unemployment. Data available for the countries under review show that the problem of long-term unemployment is even more severe than in the other transition countries. Highest values are reported for Albania (over 90%), Macedonia (85%) and Serbia and Montenegro (75%); in Bulgaria two thirds of total unemployment is long-term, in Croatia and Romania slightly more than half (See figure 4 in Annex). In the latter the incidence of long-term unemployment (among people who had worked before becoming unemployed) is highest for those who had a job in the state owned sector: about half of them have been unemployed for two years or more. People less affected are those who had worked in the private sector and self-employed workers (Bisogno 2000).

In most countries chances of becoming employed after entering the pool of job seekers are limited. In Bulgaria, the probability that the unemployed will find a job within the first twelve months of being unemployed is around 6.2%. The incidence of long-term unemployment there

is highest in rural areas, for women re-entering the labour market, the low-educated and low-skilled and young people who have graduated from secondary and tertiary education (ETF 2000a). In Croatia about one third of the unemployed that have worked before are facing unemployment spells of two years or more. In Romania long-term unemployment is a feature of urban areas.

Unemployment hits young people disproportionately. In most countries of the region the LFS unemployment rate among people younger than 25 years is twice as high as the total unemployment rate, in Romania it is even three times higher. The high rates of 58% and about 50% in Macedonia and Serbia and Montenegro indicate a quite critical situation of young people on the respective labour markets (See figure 5 in Annex). Young people do lack professional experience, options are either to emigrate or enter the shadow economy (poor working terms). Youth unemployment is mainly long-term in Albania and Romania, in Albania young job seekers (below 31 years) account for 59% of total long-term unemployed. In Romania, the problem of long-term unemployment among young people is mainly concentrated in urban areas; the lower incidence in rural areas might be due to the possibility of seasonal work, but also due to the migration of young people to the bigger cities. The latter phenomenon can be observed in most countries of the region – Albania, Bulgaria, Montenegro and Romania. Other vulnerable groups among young people are the young Roma in Romania and Bulgaria, young returnees, refugees, demobilised soldiers, and disabled soldiers in Bosnia and Herzegovina and in Serbia and Montenegro (see also ETF 2000).

The main reason for the high unemployment incidence of young people in most countries are widespread skill mismatches (the qualification obtained does not respond to the requirements on the labour market) and school drop-out rates. The latter is particularly obvious in Albania, where about 40% of the young people complete their studies after compulsory education (ETF2000b)

The youth unemployment rate varies also significantly across EU member states, it is particularly high in Italy and Greece, where 26-27% of young people in the labour force are unemployed, while the respective value for Austria is 7% (European Commission 2003).<sup>10</sup>

Similar as in other transition countries and in the EU there are large regional disparities in unemployment in South East Europe. In general, unemployment tends to be lowest in big cities with a developed services sector and in regions with diversified industrial economy. The low territorial mobility of the labour force is aggravated by the lack of housing and/ or high rents, high transport costs and/or the cut of public transport. As far as data are available, in most countries under review, unemployment is lowest in the capital cities.

The unemployment incidence is very high among ethnic minorities. In Bulgaria the jobless rate among the Roma population reaches about 80%, which is five times higher than the national average; most affected are young people below 30 years of age, about two thirds have never worked (ETF 2000).<sup>11</sup> The unemployment rate of Turks and Pomaks (Bulgarian Muslims) is lower than that of the Roma, but is concentrated in some regions where tobacco and mining companies were closed down in the wake of restructuring. A common feature of ethnic minorities is their low educational, which is even more pronounced among the Roma than among the Turks and Pomaks.

### **Informal economy**

When speaking about the labour market in South East Europe it is unavoidable to refer to the informal economy which plays an important

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<sup>10</sup> In 2002 the youth unemployment rate in the EU and in the membership-hopeful countries was 15% and 32% respectively.

<sup>11</sup> The Roma population in Bulgaria numbers about 540000 persons, Bulgarian Turks and Bulgarian Muslims about 700000 people.

role in the whole region. Generally one may argue that the size of the informal economy in SEE is considerably higher than in the CEE countries. However, the estimated magnitude of this sector can vary strongly depending on the method used for calculation. In most countries the informal economy is concentrated in agriculture, trade and construction. A recent study concludes that in Macedonia the informal activities are on the increase in health care, ministries and government bodies and public enterprises (Jankulovska 2002).

According to Christie and Holzner (2003) Albania and Kosovo had the highest proportion of informal activity in 2001, while Croatia was the country with the lowest share of the grey economy (See figure 4 in Annex).

## **Conclusions**

Over the past decade, about 3.3 million jobs were lost in the SEE countries. A large share of the workforce has exited the labour market altogether, with a growing number of discouraged workers and declining activity rates all over the region. The huge job losses in industry and construction have been absorbed only to a very small extent by the services sector; the latter is still underdeveloped by Western but also Central European standards – Croatia being the only exception. In most countries unemployment increased rapidly and remained at persistently high levels and ‘the intensity is quite unusual by European standards’ (Daianu, 2002). The huge proportion of long-term unemployed workers may lead to the erosion of skills, and it might be expected that many of them will exit the labour market altogether, pointing to a further decline in activity rates. Taking into account that transformation is still at the beginning, the labour market situation will further deteriorate.

Future job creation will first of all depend on sustainable economic growth. In contrast to Western European economies, where a GDP growth of about 2% is sufficient to enable new job creation, the respective value in the transition economies stands at about 4-5%. Another

important factor to increase employment is the development of small and medium-sized private enterprises and the ability of SEE countries to succeed in attracting foreign investment. Furthermore, the upgrading of skills will be one of the major tasks in order to overcome the problem of the skill mismatch. An indispensable precondition, however, for a substantial economic improvement in the region in general and on the labour market in particular is to achieve and maintain political stability.

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