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## Labour Market Issues in Bulgaria, Romania, and Turkey

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Arbeiten aus dem



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MÜNCHEN

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**Labour Market Issues  
in Bulgaria, Romania, and Turkey**

Barbara DIETZ, Michael KNOGLER, and Volkhart VINCENTZ

Commissioned by the Federal Ministry of Finance, Berlin



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## Abbreviations

AC-10	10 acceding countries
CBA	Collective bargaining agreement
EPL-index	Employment Protection Legislation Index
GDP	Gross domestic product
LFS	Labour force survey
PPP	Purchasing power parity

national currencies:

BGN	Bulgarian lev
ROL	Romanian lei
TL	Turkish lira

## **Key Messages**

### **in a comparative perspective**

#### *Employment*

**Turkey and Bulgaria** show employment rates much below the EU Lisbon targets. Both countries, in particular Bulgaria, have double-digit unemployment rates. The Turkish data are still heavily influenced by the aftermath of the financial crisis in 2001. Youth as well as long-term unemployment in Bulgaria is large, above the average of the AC-10.

Total as well as youth and long-term unemployment rates in **Romania** are far below the AC-10 average and closer to the EU-15 level. This is less a sign of a functioning labour market than an indication of delayed restructuring, although wage restraint has also helped to stabilise employment.

The issue of urban-rural migration is a case in point. In **Turkey** the shrinking of agricultural employment intensified during the stabilisation programme. Industry, construction and services have to absorb a significant flow of rather unskilled work-force in future. In **Romania** urban-rural migration is still dormant, but might become topical in the near future. Very likely direct and indirect subsidies have helped to restrict the out-flow from agriculture.

Employment policy should clearly distinguish between rural and urban areas. Data about non-agricultural employment are likely to be more useful for international comparisons. Housing and subsistence economy provides a large part of the income and dual labour markets in urban and rural areas exist. Employment policy might therefore set different priorities compared to EU-countries with per capita incomes four times as high. In addition, the poverty extends to the state and its budget, which calls for a probably restrictive selection of affordable policy measures.

#### *Wage-setting*

The wage bargaining process did not assure a stable and foreseeable relation between productivity and wages. In **Turkey** and **Romania** there is a widening gap between productivity and wages since the mid-1990s. In both countries unit labour costs have fallen by 30 - 40% since 1999. With the stabilisation programme in Turkey real wages were disconnected from productivity growth. However, there have been signs for a reversal of this process recently. Nevertheless, the opening gap between wage and productivity might not be a temporary, cyclical phenomenon, but may well have a structural component due to continuing migration from agriculture.

The wage system seems to be rather flexible in **Turkey**. Job turnover as well as sectoral wage differentiation is large. However, the extreme differences between wages in sectors covered by collective bargaining agreements and those that are not as well as the strong influence of the state on wage determination might distort the wage structure.



### *Tax-Benefit System*

The tax burden on labour in **Romania** is one of the highest in the enlarged EU. In **Bulgaria** it is also clearly above the EU-15 level. Payroll taxes show the same order: Romania with 52% on gross earnings at the top and **Turkey** (39,5%) at the end. However, the scope to reduce the tax burden is small given the tight budgets in the countries. Social security expenditures are 14% of GDP in Bulgaria and 10% in Romania. Phasing out early retirement regimes and raising the retirement age (Turkey) can provide some financial freedom.

Compliance with the principle “make work pay” is difficult to assess due to lack of data, the existence of discretionary payments and the low level of incomes and social benefits. The government in **Bulgaria** conjectures that 30 - 35% of the welfare recipients either work in the shadow or refuse to work. A programme designed to transfer people from social assistance to (communal) work tries to address misuse of social assistance. However, missing demand for labour cannot be addressed by this active employment policy. **Romania** also links communal work with social assistance and has reduced the maximum duration of unemployment benefits. In **Turkey** no average figures for social assistance are available, but unemployment benefits are low and still cover only a small part of the unemployed. The level of social payments in **Bulgaria** and **Romania** are also sufficiently low compared to minimum wages. Altogether the benefits do not seem to provide disincentives to work, if they can be targeted to the eligible.

**All three countries** have a large shadow economy (30 – 40% of GDP), which helps to keep labour costs low. However, the existence of a large informal sector has significant short- and medium-term repercussions: unfair competition among enterprises, losses of budget revenues, and the creation of a stock of uninsured people, who will become a burden to the budget in future. To reduce the informal sector a mixture of standard measures can be applied such as: reduce the tax wedge on labour, reduce income tax for low wage earners, administrative measures (e.g. compulsory registration of labour contracts), and enhance the accountability of benefits from the social system.

### *Employment Protection*

If the regulations of the new labour law are implemented, **Turkey** will have a rather flexible protection legislation which can be compared to that of Denmark, Hungary or Czech Republic (measured by the EPL-index of OECD). A large part of the labour market is regulated by law.

**Bulgaria** prefers bilateral negotiations between employers and trade unions rather than more centralised ways to promote flexible forms of employment and low costs of hiring and dismissal.

As in the case of labour costs, the informal sector de facto lowers the standards of employment protection in **all three countries**.

## *Migration*

Judged by German experiences, the migration of labour into the EU seems to be controllable. The effect of temporary restrictions of free movement of labour on the long run magnitude of flows depends obviously on the speed of the catching-up process in the sending countries as well as on the development of unemployment rates in the countries concerned.

Illegal migration from all three countries is a major concern, not least because all these countries border the enlarged EU and are used as transit countries by third state nationals. This poses a problem to the countries themselves, because part of the transit migration will try to settle in the transit country. Support of the countries in controlling illegal immigration and emigration is needed. Readmission agreements among several states were enacted. An agreement between Turkey and the EU is still outstanding.

While labour migration can be controlled, migration in the context of family reunification, and particularly welfare migration might lead to further inflows. If strong asylum flows in the past are an indication, one might expect welfare immigration especially from Romania but also from Bulgaria and parts of Turkey. The composition of migration according to the target countries is rather stable due to the existing migrant networks. In future the receiving countries may however engage in a warding-off competition concerning the welfare systems, so as not to attract too many people.



## **I. EU-requirements as benchmarks**

The countries concerned in this paper are either in the process of negotiations for EU-accession (Bulgaria and Romania) or under a review process for opening such negotiations (Turkey). Therefore we will take the EU-requirements concerning the labour market as a benchmark against which the developments in these countries are assessed.

For different reasons all of the countries registered a recession with at least two years of negative output growth since the mid-1990s. Besides these cyclical component, the transition process in Bulgaria and Romania is still going on. Thus, benchmarking against EU-objectives has to take into account cyclical as well as structural peculiarities of the countries.

GDP per capita in PPP is in all three countries only 25% of the EU average, which makes real convergence the central issue for economic policy. Housing and subsistence economy provide a large part of the income in these countries. In addition, dual labour markets in urban and rural areas exist (Annex A). Employment policy might therefore set different priorities compared to EU-countries with per capita incomes four times as high and rather small shares of agricultural employment. Further, poverty in these countries extends to the state and its budget, which calls for a probably restrictive selection of affordable policy measures.<sup>1</sup>

In the following we use as far as possible data from Labour Force Surveys (LFS), which are more likely to include the work in the shadow economy than data on registered employment (Annex B). Although it cannot be ruled out, that part of the shadow economy and activities in the subsistence economy are not included in these data. The same applies to unemployment data. The description of unemployment trends is based on LFS data which are conducted in line with the internationally comparable unemployment definitions set by the International Labour Organisation (ILO). As in other countries, registered unemployment still diverges from unemployment measured in the LFS, indicating differences in the generosity of unemployment benefits in these countries.

### **1. Employment Policy**

The structure and evolution of labour costs and wages are important features of the labour market. They are closely linked to both firms' labour demand decisions and individuals' labour supply decisions. The Broad Economic Policy Guidelines and Employment Guidelines<sup>2</sup> have accordingly highlighted the following priorities for European

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<sup>1</sup> Cp. European Commission (2004).

<sup>2</sup> European Council (2003), Council recommendation of 26 June on the broad guidelines of the economic policies of the Member States and the Community (for the 2003-2005 period), 2003/555/EC, Official Journal of the European Union, 1.8.2003, L195/1-54; European Council (2003), Council Decision on guidelines for the employment policies of the Member States, Common guidelines, 10567/03, 22.7.2003.

employment policy, which are also likely to become priorities for Bulgaria, Romania, and Turkey once they are members:

- The link between wages and productivity, and their impact on employment creation;
- The role of non-labour costs, mainly taxes and social contributions, for employment performance and social cohesion;
- The need for increased wage flexibility and differentiation and their role for employment performance and labour mobility;
- The role of social partners, industrial relations collective agreements and wage setting mechanisms for quality in work and employment performance.

Against the backdrop of these guidelines and policy recommendations, three features of the labour market can be seen as potential factors of influences on whether wage developments are “employment-friendly” – the overall process of wage formation, the impact of taxation on labour income and the design of income maintenance systems for the unemployed, and the design of employment protection.

The European Council set the following goals for employment rates:

- *total employment rate should reach 67% in 2005 and 70% in 2010*
- *female employment should reach 57% in 2005 and 60% in 2010*
- *the employment rate of the elderly (55 – 65) should be 50% in 2010*

## **2. Wage bargaining**

Wage formation systems are to a large extent systems of collective bargaining, involving individual employers and employees and possibly the government. The design of such systems of collective bargaining vary considerably across countries, both within current EU and between EU member states and accession countries. Main differences concern the degree of centralisation and the co-ordination of bargaining at various levels, including the national, sectoral and company level. There are also differences across countries in the coverage rates of collective bargaining, not least because of differences in extending these agreements to other firms or sectors.<sup>3</sup> The degree of centralisation is left open to national regulations. However, the outcome of the bargaining should provide for an adequate productivity-wage nexus and wage flexibility with respect to regions and skill.

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<sup>3</sup> The discussion of how wage bargaining structures effect wage developments has to a large extent been shaped by the Calmfors and Drifill hypothesis. It predicts an „inverted U“ relationship between unemployment and the degree of centralisation of wage bargaining. Fully centralised and fully decentralised bargaining both favour the employment situation: the former, because it can better take into account the economy wide consequences of wage bargaining; the latter, because it can better reflect the productivity in the firm. Calmfors, L., Drifill, J. (1998)

### **3. Tax-benefit-systems**

The Broad Economic Guidelines 2003 call for action to improve incentives to make work pay, to facilitate job creation, to improve the functioning of the labour market and to tackle the root causes of high unemployment and low labour force participation in the EU. Member states are asked in particular, to ‘improve the combined incentive effects of taxes and benefits, reduce high marginal effective tax rates in order to eliminate unemployment and poverty traps, cut the tax burden on low-paid labour, improve the eligibility criteria for benefits whilst preserving an adequate level of social protection, and ensure the efficiency of job search assistance for benefit recipients’.

### **4. Migration**

Several determinants explaining international migration can be listed. Most migration theories deal with labour migration. Wage differences figure prominently in explaining movements between low wage countries and the EU. However, given the partially high unemployment rates in the EU, the chances of finding a job in the new host country also influences migration decisions. Thus, it is the expected wage differential rather than the statistical wage difference that determines labour migration. In addition to wage differentials, generous provisions of public goods and transfers might induce a significant welfare migration. Another view stresses decisions of households to use migration for capital building and risk insurance, which is not available in their home countries. Migration decisions are interpreted as a portfolio strategy to diversify incomes. In contrast to these explanations, which refer to the supply of labour, the demand of labour in segmented labour markets of the host country might also contribute to migration. The labour demand in the secondary labour markets of the EU, with lower wages and less social security, in many cases can not be filled by native labour and serves therefore as a pull factor for migration. This is particularly true for seasonal work in agriculture and tourism. Finally, migrants built up networks in their host countries, which reduce costs and risk for potential migrants and increase the likelihood of further migration. The greater the number of migrants a person knows in a sending area the greater the probability that this person will also migrate. In addition the political and ethno-national situation in the sending countries causes migration.

#### **4.1. EU immigration policy**

The theoretical scope of migration has to be adjusted according to the restrictions imposed by the host countries to control migration. Labour immigration and immigration out of other motives are regulated differently, which influences the magnitude of the flows as well as the composition of migrants.

In the Treaty of Amsterdam (May 1999) the EU put forward a common immigration and asylum policy<sup>4</sup>. The elements of this common policy specified four goals devoted to justice and home affairs:

- partnership with the countries of origin
- fair treatment of third country nationals
- management of migration flows
- setting up of a common European asylum system.

Concerning legal migration, draft directives were issued on the right to family reunification, on the long-term resident status, conditions of entry and residence of third country nationals for salaried employment and self-employment. To combat illegal migration several initiatives were taken which concerned the readmission and return policy, visa policy, pre-frontier measures and border management. Measures on asylum, illegal immigration and return policy have to be adopted by May 2004.

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<sup>4</sup> Denmark, UK, and Ireland do not participate fully.

## II. BULGARIA

### 1. Employment developments

#### 1.1. Overall trend

Employment showed a dramatic decline at the beginning of the transition period. Total employment between 1990 and 1993 decreased by 875,000 or 21,4%. After a short period of stabilisation between 1993 and 1996 it declined again by a further 345,600 or 10,5% between 1996 and 2001, resulting in a total loss of 1.2 million or an employment decline of 28,2% since 1990. Whereas employment appeared to be highly responsive to output variations in the early 1990s, during the crises of the mid 1990s (between 1995 and 1997) employment decreased by only 2.6%, while GDP dropped by 16.5%. The economic recovery that followed was not sufficient to have a positive impact on employment. Despite a GDP growth of 12,2% between 1998 and 2001, employment continued to decline by a further 5.9%. (*Table A1*) In 2002 employment started to grow again. In 2003 employment was up by 1.5% compared to 2002.

#### 1.2. Employment rates

Among acceding countries, the employment rate in Bulgaria is one of the lowest with 52.5% in 2003, 17.5 percent from the Lisbon target. With 49.0% female employment also falls short of the target, but less than the male employment rate. The employment of the elderly, which was 30% (50% target: 50%), shows the biggest short-fall. (*Table A2*) The composition of Bulgarian employment by sectors is broadly in line with the average of the AC-10. This means the share of agricultural employment with 9.9% is about 2.5 times higher than in EU-15. (*Table A3*) However, due to a high proportion of persons engaged in agricultural activity in addition to another main occupation, the data on agricultural employment underestimate the relevance of this sector.

### 2. Unemployment

#### 2.1. Overall trend

Unemployment in Bulgaria peaked in 1993 when, according to the LFS, 814,000 people were unemployed, resulting in an unemployment rate of 21.4%. The unemployment rate started to decrease afterwards and was down to 14% for the period 1996-98. Since then, the contraction of the labour force has slowed down while unemployment has been on the rise again. The unemployment rate reached almost 20% in 2001. In 2002 it decreased to 18.1%. (*Table A4*) A further significant decrease of unemployment happened in 2003. To capture recent trends data table I.1 provides unemployment data, although they do not coincide completely with the data of the European LFS used in the annex tables.



Table II.1:

**Unemployment rates**

	2000	2001	2002	2003*
total	16.9	19.7	17.8	14.0
female	16.6	18.8	16.9	13.5
youth	25.3	39.5	36.5	28

\* three quarters of 2003

Source: CANSTAT Statistical Bulletin 3/2003

## 2.2. Structural features

Except for the years 1993 and 1995, the female unemployment rate has always been similar to or slightly below the male rate. In 2001 the male unemployment rate increased more sharply than the female rate, mainly because of a strong increase in female participation. In 2002 and 2003, both male and female rate declined but remained substantially higher than the EU average.

With the rise in overall unemployment, long-term unemployment increased to 11.9% in 2002 (2.6 percentage points up from 2000). Almost 62% of the unemployed aged 15-64 had been without work for one or more years. The very long-term unemployed (more than two years) represented more than two-thirds of the long-term unemployed. Long-term unemployment is very high among the young. (*Table A4*)

From a regional perspective, Bulgaria shows sizeable differences in unemployment. In 2001, only the South-West had an unemployment rate well below the national average (14.6%). It was just under or at the average in the South-Central and North-Central regions while the South-East, North-East and in particular the North-West regions had unemployment rates of up to 30%. The regional unemployment gap between the highest and lowest regional unemployment rates widened during the last 10 years from 16 to 23 points. The standard deviation of regional unemployment rates (19.9%) is the highest in Eastern Europe.<sup>5</sup>

Like in other countries youth unemployment is significantly higher than adult's unemployment. In Bulgaria the unemployment rate of the group aged 15-24 has always been about twice as high as the unemployment rate for those between 24-54. The total youth unemployment rate stood at 35.5% in 2002 with rates for young men (39%) above rates for women (31.4). (*Table A5*) Although youth unemployment declined significantly in 2003, the rate is still twice the rate of total unemployment.

<sup>5</sup> EBRD (2003), Table 5.3.

### 3. Issues in employment policy

#### 3.1. Wage bargaining system

##### 3.1.1. Collective bargaining

In its last reports on Bulgaria's progress towards EU accession the European Commission pointed to a number of weaknesses in industrial relations, and specifically to inadequate autonomous bipartite collective bargaining at enterprise, sectoral and regional levels.

Table II.2: **Bulgaria: Tripartite Bodies**

Main tripartite bodies	Date	Institutional/legal basis	Composition	Sub-committees
Tripartite Commission for co-ordinating interests	1991	Agreement	Employers: 4 Trade Unions: 2	Yes
National Council for tripartite Co-operation	1993	Labour Code	Employers: 4 Trade Unions: 2	Yes
National Economic and Social Council	April 2001	Law	Multipartite	

Source: EIRO, Industrial Relations in Europe 2002.

At the national level all candidate countries have promoted social dialogue through tripartite structures, notably by creating tripartite national councils, in which employers' and trade unions' representatives discuss various economic and social issues. A formalised tripartite dialogue was introduced in Bulgaria in 1993.

In Bulgaria, the system of collective bargaining is organised on three levels:

- At branch/sector level, "branch councils for social co-operation", made up of the representative branch/sector employers' and trade union organisations, conduct bargaining;
- At municipal level, "municipal councils for social co-operation" provide the forum for negotiations between unions and representatives of the municipal authorities on activities financed by the budget (education, healthcare, culture and administration);
- At enterprise level, trade union and individual employers participate in negotiations within "joint commissions for social partnership".

In 2002 collective bargaining and the conclusion of collective agreements entered a new stage of development, brought about by amendments and supplements to the labour code which came into force in 2001. The most important changes made to collective bargaining procedures included the following:

- The introduction of a clear definition of the levels of collective bargaining – enterprise, branch, sector and municipality;
- The creation of legislative provisions related to branch and sector collective bargaining. A new procedure provides for the extension of agreements' provisions to all

enterprises in the branch/sector concerned, similar to the practise which exists in many EU Member States (expansion clause);

- The introduction of a new option, whereby the parameters for branch/sector bargaining may be determined by a framework agreement between national trade union and employer organisations;
- A stipulation that collective agreements have a duration of at least one year but no longer than two years.

Collective bargaining has strengthened by the development of bipartite co-operation at sector level, – though the European Commissions still points out various shortcomings and weaknesses in the sectoral social dialogue. From an examination of the sector/branch collective agreements in 2001 - 2003 the following conclusions can be drawn<sup>6</sup>:

First, it appears that the parties to the bargaining process – the representative organisations of employers and trade unions – have managed to maintain collective bargaining in almost all sectors during the transition period. The number of branch/sector collective agreements rose by 12% in 2002/03 compared to 2001/02 – covering an estimated 40% of all employees. The low coverage rate results because the expansion clause is not applied in practice and because of a lack of representative trade unions in some branches.<sup>7</sup>

In over 75% of the cases, the bargaining parties have agreed on the maximum two-year duration for collective agreements permitted by the law, which is seen as corresponding to a tendency towards longer-lasting agreements observed in other countries in Europe.

A second important development in sector/branch social dialogue in 2003 has been the creation of a new bipartite mechanism for mediation and voluntarily arbitration in disputes. The new system was established in April 2003, implementing procedures for the out-of-court settlement of collective disputes. The system creates prerequisites for improving the effectiveness of the sector/branch dialogue and the implementation of collective agreements.

Third, a number of provisions agreed upon by the social partners in collective agreements became more effective in setting common minimum sectoral standards in some of the most important aspects of work and industrial relations.

There are two representative trade unions in Bulgaria with a unionisation rate of about 26% in 2003, down from 39% in 1999.

### *3.1.2. Minimum Wages*

Minimum wages are set by government decisions after consultations with the social partners. Following the agreement with the IMF in 2002, the minimum wage should be

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<sup>6</sup> EIRO, Bulgaria: Sectoral collective bargaining develops, [www.eiro.eurofound.ie/2003/12/feature/bg.0312203f.html](http://www.eiro.eurofound.ie/2003/12/feature/bg.0312203f.html)

<sup>7</sup> Loukanova, Tomev(2003)

corrected with the growth rate of the average salary in the public sector for the last reported six months over the previous six months. The ratio between the minimum and average wage had decreased from 54% in 1991 to 27% in 1997. Since then it increased continuously and was 35% in 2003. From 1.1. 2004 the new minimum wage is fixed at 120 BGN, which is 20 BGN above the old minimum wage. Minimum wages in absolute terms are low compared to EU Member States and Accession countries. (*Table A6 and Chart A1*)

## **3.2. Tax-benefit-systems**

### *3.2.1. Non-wage labour costs and tax rates*

Non-wage labour costs, including employers' actual and imputed social contributions, so-called unfunded employee social benefits and any taxes payable by the employer on the wage and salary bill, are a crucial determinant of labour demand decisions by firms.

Non-wage labour costs are almost 30% in total labour costs. The tax burden on labour and the general tax burden are rather high in most accession countries. The tax wedge – defined as the share of total income tax and employer and employee social security contributions in gross wage earnings – ranges from more than 45% in Belgium, Germany and Sweden to less than 20% in Malta, Cyprus and Ireland for low-income earners. In Bulgaria it is over 40%. (*Chart A2 and A3*)

The tax wedge is high due to high payroll contributions. These are the result of a growing financial burden of social security insurance related to the unfavourable dependency ratio. The erosion of the tax revenue due to the declining employment is aggravated by high levels of tax evasion or non-payment.

The composition and distribution of payroll contributions are given table A7. Overall payroll contributions went up from 35% in 1990 to 47,5% in 1999. Since the end of the 1990s, social contributions are gradually being cut, which should also help addressing the important problem of non-payment of taxes. With the last reduction in 2001 the overall contribution rate decreased to 42,7%. Employers contributed 75% of the total to the unemployment insurance in 2002. This share should decline to 50% till 2007.

### *3.2.2. Income support for the unemployed*

Table A8 gives an overview of the main features of the Bulgarian unemployment benefit system. The coverage of unemployed by unemployment benefits is low and it has decreased from 31% in 1997 to 20% in 2001. There is no clear information on the coverage of unemployed by income support from social assistance. The unemployment benefit system has been modified several times since the early 1990s. Successive reforms have resulted in a tightening of requirements regarding previous employment spells and an increased duration. The long-term unemployed are not eligible for unemployment benefits, nor are young people looking for their first job. Together, they represent approximately half of the registered unemployed

Social assistance in Bulgaria is means-tested and comprises a monthly cash benefit as well as a range of in-kind benefits. Eligibility is determined on the basis of the Guaranteed Minimum Income (40 BGN in 2002) adjusted to the household size and the situation of its members. 1,15 million children are eligible to child allowances of 18 BGN. Only the unemployed who have been registered for six months at the labour office can apply for the general social assistance. In addition, they are obliged to participate in municipal temporary work programmes without payment for at least five days a month. A national programme “From Social Assistance to Employment” provides public work mainly for long-term unemployed receiving welfare.<sup>8</sup> It is hoped that the programme also curtails misuse of welfare, which is believed to be at a rate of 30 – 35%. A significant part of the recent increase of employment can be attributed to this active employment policy.

### 3.3. Employment protection legislation

A comparison of the strictness of employment protection regulation between Bulgaria and other transition countries suggests that in general employment protection legislation is not unduly restrictive.<sup>9</sup> Its positive side includes relatively low monetary costs of dismissals (short advance notice and low mandatory severance pay), and an option to redistribute working hours, which gives employers flexibility in adjusting labour input to fluctuations in product demand. In some areas, however, existing legislation excessively restrains employers' freedom to adjust size and composition of their workforce to changing economic conditions, with possibly negative consequences for firm performance. These areas include:

*Procedural cost of dismissal.* Employers complain that laying-off a worker due to poor performance, lack of skills, misconduct or redundancy is difficult. Part of this reflects employment protection provisions by the Labour Code which does not mention economic or organisational reasons as valid reasons for dismissal, another part reflects a pro-labour bias exhibited by courts.

*Strict limitation on the use of fixed-term employment contracts.* Fixed-term contracts are allowed only for work which is temporary or seasonal in nature, and can be renewed only once. These restrictions especially hurt employment chances of less productive workers, that is, exactly those workers who are most stricken by unemployment.

*Restrictions on the use and high costs of overtime work.* The use of overtime work is in principle prohibited in Bulgaria except in emergency situations and in the case of intensive seasonal work. In addition, the Labour Code imposes a tight yearly limit of 150 overtime hours. The use of overtime is also costly for employers as they have to pay an overtime premium of at least 50 percent of the base wage.

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<sup>8</sup> Cp. [www.pension.bg/labor/en/raboten1.htm](http://www.pension.bg/labor/en/raboten1.htm)

<sup>9</sup> Rutkowski, J. (2003), Annex 2.

*Limitations on wage adjustments.* According to the Labour code employers are obliged to pay the 100% wage rate during a production stoppage, i.e. they cannot adjust wages to changing demand conditions.

In case of labour disputes employer and employee can appeal to the Labour Courts. The court trial is free for employees. As mentioned, some investors feel that the Labour Courts are biased toward the employees.

## 4. Migration

Continuing high unemployment in Bulgaria probably contributed to the ongoing net emigration from Bulgaria. About 22000 Bulgarian citizen settle abroad per year, although the flows are smaller than in the beginnings of the 1990s. In 2000 6100 ethnic Turks came from Bulgaria to Turkey. Other preferred destinations are North America and the EU. Net migration was only positive for elder people (60+). There are about 4 thousand Bulgarian students in Germany.

Table II.3: **Migrant populations in EU member states from Bulgaria**  
(latest available year)

Austria**	4,217	Luxembourg**	113
Belgium*	1,529	Netherlands*	1,074
Denmark*	426	Portugal*	436
Finland*	308	Spain*	12,035
France****	3,360	Sweden*	805
Germany*	38,143	Unit. Kingdom***	2,535
Greece**	35,104		
Italy**	6,758	<b>Total</b>	<b>106,843</b>

Source: Eurostat (\*2002, \*\*2001, \*\*\*2000, \*\*\*\*1999)

The labour migration in the agricultural and service sector also led to substantial Bulgarian migrant population in Spain and Italy. Most Bulgarian emigrants settled in Germany followed by the neighbouring Greece. In the beginning of the 1990s many Bulgarian nationals arrived via the asylum regulation in Germany. These flows were drastically reduced after amendments to the asylum law in 1993. Recently the number of seasonal workers is on the rise. One study projects that, if restrictions on migration would be abandoned, in the long run the population of Bulgarian nationals in Germany would rise to about 235 thousand persons.<sup>10</sup>

Bulgaria is a transit country for most migrants, although many give up their plan to go to Western Europe and try to find work in the transit country.

The prospective membership of Bulgaria in the EU as well as the new borders of the enlarged EU, led Bulgaria to adjust its migration legislation to the *acquis communautaire*.

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<sup>10</sup> Boeri, T. Brückner H. (2000)

In particular the efforts to combat illegal immigration and trafficking were stepped up. Border police has been reorganised and closer technical co-operation with EU-members is planned. The Bulgarian government introduced measures to stop illegal migration of Bulgarian citizens to western countries. Several readmission agreements were signed and a new law, defining forms of legal employment for Bulgarians abroad, was enacted. Germany has a readmission agreement with Bulgaria since 1995. 6600 Bulgarians were readmitted from the EU, United States and Canada in 2002.

Table II.4: **Bulgarian migrants in Germany, in thousand**

	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002
inflows	11.0	17.2	31.3	27.2	10.4	8.0	6.3	6.3	5.2	8.0	10.3	13.3	13.0
asylum seekers	8.3	12.1	31.5	22.5	3.4	1.2	0.9	0.8	0.2	0.1	0.1	0.1	0.8
outflows	1.9	3.5	10.8	34.9	17.8	10.3	7.0	6.3	4.8	5.4	6.6	7.9	8.6
net migration	9.1	13.7	20.6	-7.6	-7.5	-2.3	-0.7	0.1	0.4	2.7	3.7	5.4	5.6
stock of													
population	14.7	32.6	59.1	56.7	44.8	38.8	36	34.5	31.6	32.3	34.4	38.1	42.2
socially insured**	1.6	2.4	8.0	6.1	3.7	3.5	4.5	4.5	4.6	5.0	5.4	7.0	8.0
seasonal worker				0.1	0.0	0.1	0.2	0.2	0.2	0.3	0.8	1.3	1.5
contract worker		0.4	2.0	3.8	2.4	1.9	1.0	1.2	0.7	1.4	1.7	1.9	1.3
guest worker			0.0	0.2	0.3	0.3	0.3	0.3	0.4	0.4	0.7	0.8	0.6

\*\*before 1996: West Germany; June 30 of respective year

*Note:* Net migration and change of stocks of population do not coincide because of natural growth of the migrant population, naturalisation and differences in data collection.

*Source:* Federal Statistical Office of Germany

### III. ROMANIA

#### 1. Employment developments

##### 1.1. Overall trend

Employment started to decline in 1992 and continued to decline throughout the 1990s, showing no response to output variations. After an increase in employment in 2000 (2.5%), employment again decreased by a further 0.8% in 2001 and more sharply by 8.7% in 2002. Employment remained almost constant in 2003. (*Table A1*)

##### 1.2. Employment rates

The employment rate in Romania (57,6%) range in the middle between Poland with 51.2% and the Czech Republic with 65% in 2003. Since 2000 the employment rate sharply decreased by 5.4%, due to a decrease both of male and female employment rates. Romania doesn't reach the Lisbon or Stockholm goal for the overall and female employment rate. Older workers' employment rate is relatively high in Romania, well above the AC-10 average but below the 2010 target. (*Table A2*)

Romania's relatively high employment rate and low unemployment rate respectively seem to mask unresolved structural problems.<sup>11</sup> A sharp decline in urban employment has been compensated more by an increasing rural employment (mainly subsistence economy) than by decreasing participation and growing unemployment respectively. Agriculture's share in total employment rose from 33% in 1992 to 41.4% in 2000 and declined to 32,3% in 2002 – still the highest level among the accession countries. (*Table A3*)

#### 2. Unemployment

After a decline in the early 1990s the unemployment rate stabilised at around 5.5% in the mid-1990s. The rise observed thereafter continued in 2002 when the unemployment rate stood at 7%. However in 2003 unemployment fall again. (*Table A4*) To capture recent trends table III.1 provides unemployment data, although they do not coincide completely with the data of the European LFS used in the annex tables.

Table III.1: Unemployment rates

	2000	2001	2002	2003*
total	7.1	6.6	8.4	7.1
female	6.4	5.9	7.7	6.5
youth	18.6	17.5	21.7	18.0

+ three quarters of 2003

Source: CANSTAT Statistical Bulletin 3/2003

<sup>11</sup> Cp. Dimova (2003)



## 2.1. Structural features

The total unemployment rate in 2003 of 6.6% is below the EU average (8.1%), with both the male unemployment rate and female unemployment rate below EU average.

The unemployment rate of the 15-24 year olds has always been about twice as high as the unemployment rate for the group aged 24-54. In Romania, the youth unemployment rate rose from 15.8% in 1998 to 18.5% in 2002 (more than 3 percentage points above EU average), but fall back to the 2001 level in 2003. There is no marked difference between men and women. As the overall unemployment rate the long-term unemployment rate is with 3.8% only slightly above the EU-15 average. (*Table A5*)

The variation in unemployment at the regional level is not very marked. The standard deviation of regional unemployment rates is the lowest in Eastern Europe. However it increased in the last ten years. The gap between the lowest regional unemployment rate and the highest rose from 3 percentage points in 1991 to 6 percentage points in 2001<sup>12</sup>. Registration data however suggest that the variation in unemployment is much greater between counties within each of the planning regions.

## 3. Issues in employment policy

### 3.1. Wage bargaining system

#### 3.1.1. Collective bargaining

As in the other countries of this report the European Commission pointed to a number of weaknesses in industrial relations, and specifically to inadequate autonomous bipartite collective bargaining at enterprise, sectoral and regional levels.

At the national level, all candidate countries have promoted social dialogue through tripartite structures, notably by creating tripartite national councils, in which employers' and trade unions' representatives are invited in discussions on a number of economic and social issues. A formalised tripartite dialogue was introduced in Romania in 1993.

**Table III.2: Tripartite Bodies**

Main tripartite bodies	Date	Institutional/legal basis	Composition	Sub-committees
Tripartite Secretariat for Social Dialogue	1993-97	Under PHARE project	Employers: 8 Trade Unions: 5	Yes
Economic and Social Council	1997	Law on the ESC No. 109/1997		
Social Dialog Committees within each Ministry	2001	Government Decision No. 314/2001		

Source: EIRO, Industrial Relations in Europe 2002.

<sup>12</sup> EBRD (2003), Table 5.3

In the area of social dialogue the adoption and modification of some important laws in 2003 helped to ensure the “institution-building” which may allow wide-ranging tripartite social dialogue, and also provided harmonisation with EU regulations.<sup>13</sup>

In February 2003, parliament adopted a new law on the organisation and functioning of the tripartite Economic and Social Council (CES). According to this law, the CES examines the economic and social situation of the country and makes recommendations to labour relations and wage policies, restructuring and privatisation, social protection and education, and monetary and fiscal policies.

Under a new Trade Unions Law, adopted in January 2003, trade unions may be set up in order to protect the right regulated by national legislation and by collective agreements. According to the law, unions are independent organisations, comprising at least 15 individuals working in the same field or industry, but not necessarily for the same employer. This last provision was introduced as a response to criticism of the former law restricting trade unions in the emerging private sector, which mainly consists of small and medium-sized enterprises. Other new provisions include trade unions’ right to bring a court action to defend interest of any of their members. Elected trade union representatives cannot be dismissed during their term in office and for a period of two years beyond the end of their term. Employers are obliged to invite trade union representatives to board meetings. Trade unions must be notified of resolutions carried by the board of directors within 48 hours of being passed. Union membership has sharply declined during the 1990s. According to ILO, the Romanian unionisation rate now stands at only 44%, compared with 80% at the beginning of the 1990s.<sup>14</sup>

However, both employers’ organisations and trade unions criticise current social dialogue as being merely formal and wish to gain more bargaining power. The legal framework for industrial relations is not yet completed. A number of framework regulations contained in the new Labour Code (adopted in January 2003) are to be subsequently detailed by special laws, such as a law on collective labour conflicts, or rules on the setting of a “wage guarantee fund” in order to guarantee workers’ pay in the event of employers’ bankruptcy. Importantly, given the increasing presence of multinationals in the domestic market, the Labour Code envisages that special regulation will be issued at European Work Councils.

Recent data on the coverage of collective agreements are not available. Collective framework agreements for each sector are negotiated each year at the national level. In 2001, 19 sectoral agreements were established, covering 35% of the companies with more than 20 employees. At national level, the government has concluded a number of tripartite social pacts. The 2002 social agreement was concluded by the government, seven employers’ organisations and three union confederations, while a separate deal

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<sup>13</sup> EIRO, Important industrial relations law adopted, [www.eiro.eurofund.ie/2004/01/feature/ro0401107f.html](http://www.eiro.eurofund.ie/2004/01/feature/ro0401107f.html)

<sup>14</sup> These findings are based on a survey conducted in December 2001-February 2002. In sectoral terms the highest density rates are found in mining (85%), heavy industry (83%), oil, gas and chemicals (76%), while in trade, tourism, public services the decline of union presence has been quite sharp to below 40%.

was concluded with two other representative union confederations.<sup>15</sup> Negotiations over a 2003 social agreement ended in failure.

End of October 2003, the government launched a plan for a “social stability pact” covering 2004.<sup>16</sup> A schedule would be put in place for the stagnated introduction of a wage guarantee fund. In 2004, wages in the sector covered by the state would increase by 6% in January and by another 6% in October, thus covering forecasted inflation fully. The social contribution tax would be lowered by three percentage points. The changes of the pact that have been agreed on seem to be low, as the trade unions continue to demand higher minimum wages.

In the last three years wages grew much slower than productivity. Real unit labour costs were in 2003 about 60% lower than in 2000.

### *3.1.2. Minimum Wages*

After a doubling in 2000, the minimum wage was further increased by 40% in 2001 and by 25% by the adjustment in March 2002 which set the minimum wage at 1,750,000 ROL, an amount corresponding to 34% of the average gross wage. At the end of 2003, the minimum wage stood at 2.5 million ROL. 28.9% of total employees were paid at the minimum wage rate. From 1 January 2004, the minimum wage was increased to ROL 2.8 million (67€). It will be valid till June 2004 and will be increased again to ROL 3.2 million. (*Table A6*) Minimum wages in absolute terms in Romania are the lowest compared to EU Member States and Accession countries. (*Chart A1*)

## **3.2. Tax-benefit-systems**

### *3.2.1. Non-wage labour costs and tax rates*

Non-wage labour costs are rather high in Romania. Expressed as a share of total labour costs, non-wage labour costs exceed 30% of total labour costs. (*Chart A2*) The tax burden on labour and the general tax burden are rather high in most accession countries. The tax wedge – defined as the share of total income tax and employer and employee social security contributions in gross wage earnings – ranges from more than 45% in Belgium, Germany and Sweden to less than 20% in Malta, Cyprus and Ireland for low-income earners. The tax wedge in Romania is over 40%. (*Chart A3*)

Partly in response to the financial difficulties of the pension system, the rate of social contributions increased substantially since the mid-1990s from 35% in 1997 to 43% in 1998 and nearly 60% in 2000. The payroll contributions were reduced in the following years. Contributions to various special funds, which are decided on an ad-hoc basis, were abolished. The new Fiscal Code, which came into force from 1 January 2004, fore-

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<sup>15</sup> See for an overview EIRO, The development and current situation of trade unions, [www.eiro.eurowfund.eu.int/2003/07/feature/ro0307101f.html](http://www.eiro.eurowfund.eu.int/2003/07/feature/ro0307101f.html);

<sup>16</sup> EIRO, Minimum wage issue threatens ‘social stability pact’ prospects. [www.eiro.eurowfund.eu.int/feature/ro0401104f.html](http://www.eiro.eurowfund.eu.int/feature/ro0401104f.html).

sees a reduction of social security contributions payable by employers by 2.5 percentage points. The standard contribution is thus 22%. (Table A7)

### 3.2.2. Income support for the unemployed

The coverage of registered unemployed by unemployment benefits remains high even if it is no longer as high as at the end of the 1990s. (77%). There is no clear information on the coverage of unemployed by income support from social assistance. The unemployment benefit system has been changed several times since the beginning of the transition period. The last reform from March 2002 reduced the maximum duration of unemployment benefits from 27 months to 12 months. It reintroduces the minimum wage as the reference for the calculation of unemployment benefits, which had been suppressed in 1997. The last reform of the unemployment benefit set the conditions for benefit recipients as specified in table A8. Both the amount and the shorter duration of the basic unemployment benefit are expected to provide higher incentives to take-up work.

Social assistance is based on the minimum guaranteed income (MGI), which is reviewed annually on the basis of consumer prices. The beneficiaries of the MGI without job must be registered at the agency for employment and are obliged to work 72 hours a month in community work programmes.

## 3.3. Employment protection legislation

After lengthy debates and consultation between the social partners a new Labour Code was adopted by parliament on 24 January 2003. The new Code provides a considerable degree of harmonisation of the Romanian employment law with the *aquis communautaire*. With regard to labour market regulation the main changes are as follows:<sup>17</sup>

*Working time.* The normal working time is set at 40 hours and weekly working time should not exceed 40 hours on average. Overtime can be remunerated by time off or a pay supplement, which cannot be below 75% of basic pay. Employees are entitled to a minimum of 20 days annual paid leave, in addition to the seven days of statutory holidays.

*Fixed-term employment contracts.* For the first time, special types of employment contracts are regulated by the new Labour Code, including temporary agency work, part-time employment, employment on fixed-term contracts and home-based work, while employment performed under a 'civil contract' (as a way of avoiding social security contributions) has been abolished. The Labour Code forbids employment on probation for a period of more than six months.

*Limitations on wage adjustments.* In the event of temporary periodical cessations of a company's activity, employees are entitled to at least 75% of their basic wage.

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<sup>17</sup> EIRO, Important industrial relations law adopted, [www.eiro.eurowfund.ie/2004/01/feature/ro0401107f.html](http://www.eiro.eurowfund.ie/2004/01/feature/ro0401107f.html)

*Mass redundancy.* Collective redundancies may be made only after previous consultations with trade unions or employees' representatives. The employer is required to give notice of the workforce reduction at least 45 days in advance and employees may propose measures to avoid or reduce the redundancies within a period of 20 days after notification.

*Employees' consultations rights.* Employees' information and consultation rights have been greatly increased. Thus the trade unions or elected employees' representatives are to be consulted whenever work quotas are to be established or modified and employers should periodically inform their employees about the company's economic and financial position.

The new Labour Law defines the methods to settle labour disputes. No special Labour Courts exist as yet, however the employer organization wants them to establish. The Law on the Solution of Labour Disputes seems to be working, with more than 50% of disputes solved through conciliation.

## 4. Migration

Romania has the highest migrant population in EU member states after Poland. About half of the Romanian emigrants settled in Europe. The ethno-national situation of the Roma explains much of the migration. The outflow from Romania decreased in the nineties. According to Romanian statistics 9900 Romanians emigrated in 2001.<sup>18</sup> These data must refer to net migration because 20,3 thousand Romanian citizens already came to Germany in this year. The Romanian migration is to a large extent circular with 11,000 citizens returning annually.

Table III.3: **Migrant populations in EU member states from Romania**  
(latest available year)

Austria**	17,470	Luxembourg**	355
Belgium*	3198	Netherlands*	2,094
Denmark*	1,176	Portugal*	512
Finland*	546	Spain*	31,641
France****	10,510	Sweden*	2,495
Germany*	88,102	Unit. Kingdom***	4,011
Greece**	21,994		
Italy**	62,262	<b>Total</b>	<b>246,366</b>

Source: Eurostat (\*2002, \*\*2001, \*\*\*2000, \*\*\*\*1999)

Within the EU most of the migrants settled in Germany. The presence of the migration from Romania to Greece, Italy and Spain is fairly new. This has to be attributed first of all to labour migration in the agricultural and service sector. In addition, asylum mi-

<sup>18</sup> OECD (2003)

gration of Roma from Romania, in particular to Germany, France, Italy and Spain, played a role.

Table III.4: **Romanian migrants in Germany, in thousand**

	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002
inflows	78.2	61.4	109.8	81.6	31.4	24.8	17.1	14.2	17	18.8	24.2	20.3	23.8
ethnic Germans	111.2	32.2	16.1	5.8	6.6	6.5	4.3	1.8	1.0	0.7	0.5	0.4	0.3
asylum seeker	35.3	40.5	103.8	73.7	9.6	3.5	1.4	0.8	0.3	0.2	0.2	0.2	0.1
outflows	15.8	30.2	51.9	101.9	44	25.2	16.6	13.6	13.5	14.7	16.8	18.6	17.4
net migration	62.4	31.2	58.0	-20.3	-12.6	-0.3	0.4	0.7	3.5	4.2	7.4	1.7	6.4
stock of													
population	60.3	92.1	167.3	162.6	125.9	109.3	100.7	95.2	89.8	87.5	90.1	88.1	88.7
socially insured**	8.9	13.8	23.4	27.5	25.5	24.9	24.7	23.6	23.4	23.3	19.4	21.1	21.7
seasonal worker			2.9	3.9	2.3	3.9	5.0	5.0	5.9	7.5	11.8	18.0	22.2
contract worker		1.8	7.8	13.5	2.2	0.3	0.0	1.0	1.6	3.9	5.2	3.7	3.3
guest worker			0.2	0.6	0.5	0.5	0.5	0.4	0.4	0.5	1.5	0.5	0.5

\*\*before 1996: West Germany; June 30 of respective year

Note: Net migration and change of stocks of population do not coincide because of natural growth of the migrant population, naturalisation and differences in data collection.

Source: Federal Statistical Office of Germany

Taking the migration to Germany as an example, some changes over time can be observed. After the sharp increase of citizens coming from Romania since the end of the eighties, the numbers of Romanian nationals reached their peak in 1992/3 and declined thereafter. This development has first of all to be attributed to the increase of asylum seekers between 1990 and 1993, most of whom left Germany again because their admission failed. In the case of Romania, migration networks have also been built up for decades in the context of ethnic German migration. As in many other transnational migrations, networks foster further movements. In the 1990s the amount of seasonal workers from Romania was steadily increasing.

There are different projections about the future potential immigration from Romania to Germany under the assumptions of free movement of labour and EU-membership of Romania. The highest projection<sup>19</sup>, taking 1997 as a start value, estimates that after 15 years the Romanian population in Germany would be 1.2 million persons, which amounts to a cumulative inflow of about 1 million Romanian nationals. Another estimate<sup>20</sup> finds a long term population of 714 thousand, which translates to an inflow of 605 thousand compared to the start value of 109 thousand in 1995.

A more recent study<sup>21</sup> gives only projections for the migration from Bulgaria and Romania together. By these estimates about 520,000 Bulgarians and Romanians will

<sup>19</sup> Sinn et al. (2001)

<sup>20</sup> Boeri, Brücker (2000)

<sup>21</sup> Alvarez-Plata, Brücker, Siliverstovs (2003)

settle in Germany in the long run. This much lower estimate takes as a starting value the population of 2001, which was 121,000 nationals of both countries.

In addition the study conjectures that temporary restrictions on the free movement of labour will delay the immigration, but have only a small impact on the total inflows in the long run. According to the study, postponing free movement of labour from 2004 to 2014 reduces the migration flows from Bulgaria and Romania in the first year after opening only from 47,000 to 44,000, leaving the long-term migrant population of these countries in Germany almost unaffected.

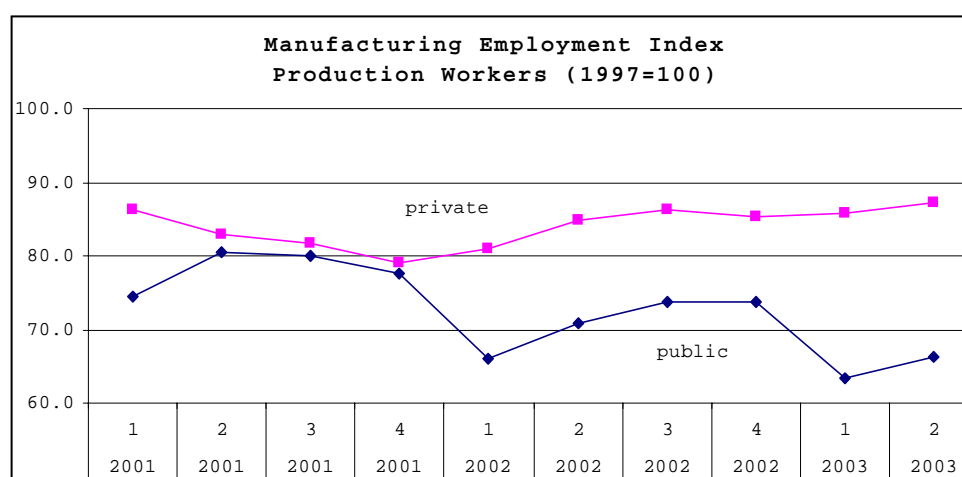
## IV. TURKEY

### 1. Employment developments

#### 1.1. Overall trend

The employment figures of the last years are influenced by the financial crisis in 2001. While output growth was resumed in 2002, employment only stabilised in 2003. However the aggregated figures conceal different developments. While manufacturing employment in the private sector was adjusted downwards in 2001, the public sector, which employs about 10% of the labour force, only reacted to the crisis in the beginning of 2002, when the private sector already started to expand employment again. (Chart IV.1)

Chart IV.1: **Manufacturing Employment Index, Production Workers**  
(1997=100)



Source: H.Ercan, Quarterly Labour Market Report, October 2003

#### 1.2. Employment rates

Data in table A1 use the general applied definition for labour force and able-bodied population aged between 15 – 64 years. The Turkish statistic (table IV.1) provides more recent data for the first three quarters of 2003 but only for people older than 15 years.

Turkey is far from reaching the goals for the employment rate. The average employment rate of 44.4% in 2003 is much lower than the rates in the acceding and candidate countries. (Table A2) Turkey misses the target by a large margin because of the extremely low employment rate of women. The male-female distribution of the Turkish labour force is approximately 72% and 28%. About 60% of the employed women work in the agricultural sector, 80% hereof in the form of unpaid family labour.



The share of agricultural labour force in Turkey is with 35% close to the level of Romania but higher than in the new member states. (*Table A3*) The declining long-term trend in agricultural employment provides a continuous supply of labour which had to be absorbed by manufacturing and services. While female participation in these sectors increased, the female participation rate in the agricultural sector declined, which is reflected in a fall of the share of unpaid family workers in total employment. The process of urbanisation will continue, not least because agricultural subsidies are likely to be reduced further in the coming years. Thus, in order to absorb excess supply from the agricultural sector, the women participation rate in urban areas has to increase.

Table IV.1: **Employment indicators (15+)**

	2001	2002	2003*
Population (000)	67296	68393	69342
Population (15+) (000)	47158	48041	48803
Labour force (15+) (000)	23491	23818	23981
Employment (000)	21524	21354	21450
Unemployment (000)	1967	2464	2530
Employment rate - total	45.6	44.4	44.0
Employment rate - female	25.1	25.3	24.9
Employment rate - male	66.5	63.9	63.3
Unemployment rate - total	8.4	10.3	10.6
Unemployment rate - female	7.5	9.4	10.3
Unemployment rate - male	8.7	10.7	10.7
unemployment rate – youth	16.2	19.2	20.5
Unemployment rate – educated youth	25.5	29.1	28.4
<i>in percent of total employment</i>			
Employed in agriculture	37.6	34.9	35.3
Regular or casual employees	47.2	49.8	49.6
Self-employed and employer	30.2	29.4	30.1
Unpaid family worker	22.6	20.9	20.3

\* three quarters of 2003

Source: SIS (2003)

### 1.3. Non standard employment

In the 3rd quarter of 2003 8.5% of total employed were casual employees and 24.7% were self-employed. Based on the figures of employees unregistered with the social security institutions the informal employment can be calculated. (see table IV.3) In the non-agricultural sector about 39% are classified as working in the informal sector. Taking a broader definition and counting all unregistered employees as informal, more than half of the employed work in the shadow.

## **2. Unemployment**

Following the financial crisis and the stabilisation programme, unemployment rates increased considerably to about 11% in 2003. The increase of unemployment mainly hit the industrialised areas of Turkey. Within 2003 the unemployment rate started to decline from 12.3% in the 1st quarter to 9.4% in the 3rd quarter (according to Turkish statistics).

The developments in male and female unemployment were quite similar with female unemployment rates only slightly below the male ones. (*Table A4*) Female youth unemployment, however, was about 2 – 3 percentage points lower than the male youth unemployment rate in the last years. Youth unemployment in total remained almost twice as high as the adult unemployment rate and reached 19.6% in 2002. (*Table A5*) The unemployment rate of educated youths (15 – 25 years with at least a high school degree), which hovered around 28 – 29% in the last two years, was even higher

## **3. Issues in employment policy**

### **3.1. Wage bargaining system**

#### *3.1.1. Collective bargaining*

Only about 15% of the paid workforce are covered by collective bargaining agreements. The unionisation rate is given by the International Confederation of Free Trade Unions as 14.6%. In January 2002 there were 2.6 million union members in the largest three unions namely Turk-Is, Hak-Is and DISK. Almost all civil servants and employees of state-owned economic enterprises are represented by unions, but law forbids them from to go on strike.

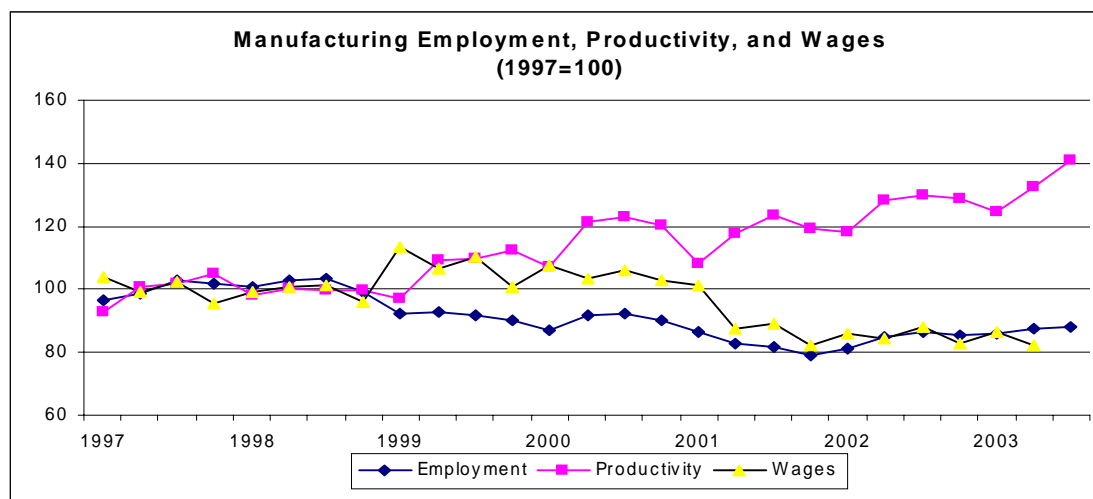
The tripartite bargaining structure at the national level in the Economic and Social Council is still not very effective. The new labour code established a “Tripartite Commission for Consultation” for consultations. The bipartite social dialog is limited to collective bargaining at the enterprise level. The unions claim unduly restrictive regulations for collective bargaining. To be authorised for collective bargaining the union must represent half of the employees in the enterprise and 10% in the sector.<sup>22</sup> There is no social dialog in most of the private enterprises. The EU demanded further progress in establishing full trade union rights.

The formal and informal influence of the government on wage setting is believed to be strong. Wages-setting agreements with the public sector enterprises and civil servant salary adjustments give signals to the wage bargaining negotiations in the private sector.

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<sup>22</sup> ICFTU (2003)

Chart IV.2: **Manufacturing Employment, Productivity, and Wages**  
(1997=100)



Source: H. Ercan, Quarterly Labor Market Report, January 2004

Since the outbreak of the financial crisis the development of labour productivity and wages diverged widely. While productivity increased by 12% in real terms, real wages in the manufacturing sector decreased by 25,2% in the 3rd quarter of 2003 against the 1st. quarter of 2001. Real wages reached the lowest level since 7 years. In spite of these trends employment gains have been modest

### 3.1.2. Minimum wage

Minimum wage legislation was implemented nation-wide in 1974. Minimum wages are adjusted twice a year. Measured in \$ the minimum wage peaked in 1999 with about 200 \$ per month. In the wake of the financial crisis minimum wages in \$ declined. From 1.1. 2004 the new minimum wage, which will be effective for 6 month, increased from 306 million TL to 423 million TL (235 €) for employees older than 16 years. (Table A6) The new gross minimum wage translate to a net minimum wage of 303 million TL For employees less than 16 years old the gross minimum wage increased from 256 million TL to 360 million TL (200 €). The IMF expressed concern about this hefty nominal increase of minimum wages by almost 40% in domestic currency. Consumer inflation in 2003 was 18.4% and is expected to reach 12% in 2004.

### 3.1.3. Wage dispersion

The wage levels in Turkey show a clear hierarchy. Workers covered by collective bargaining agreements (CBAs) have about twice the wages of workers not covered by CBAs, while workers in the private sector covered by CBAs earned about 20% more than workers in the public sector. The wage level of civil servants is the lowest.

In the period 1980 – 2000 Turkey showed inter-industry wage differentials higher than the US, Greece, Spain or Hungary and Poland. Despite some reduction of the wage differentials in the 1990s the data point to a quite flexible labour market. The job turnover rate provides the same indication. In the last decade the portion of jobs created and destroyed in a year was 22,3% of all jobs. With 52,1% the rate was highest in small private firms and lowest in the public sector with 11,7%. An econometric analysis by Taymaz and Ölzer also found that the manufacturing industry, which is the most regulated and unionised sector, is quite flexible.

## 3.2. Tax-benefit-systems

### 3.2.1. Non-wage labour costs and tax rates

Payroll tax is between 33,5 and 44% of insurable earnings. It includes pension contributions, health and unemployment insurance. The employer contributes 23,5%. Employees pay as much as 16%. Details are given in table A7. Below an income floor a minimum tax applies. There is also a ceiling above which earnings are not insurable. Public servants pay 15% and the state 20% payroll tax.<sup>23</sup>

Average social security contributions of the employee were 12% (employer 18%) of labour costs in 2002.<sup>24</sup> The tax burden of 42% on labour costs<sup>25</sup> is on the lower end of the rates in the acceding countries and slightly above the EU-15 level. (cp. Chart A3) However total annual labour costs in PPP (17400 \$) are higher in Turkey than in most acceding countries, because \$-wages are higher.

The average income tax in 2002 was 12% of the labour costs. The tax burden in terms of annual income is given in the table IV.2.

Table IV.2: **Income Tax brackets, 2003 and 2004\***

Marginal tax rate (percent)	2003 schedule (billion TL)		2004 schedule (billion TL)		Maximum average tax rate (percent)
	min	max	min	max	
15	0.0	5	0.0	6	15
20	5	12	6	14	18
25	12	24	14	28	21.5
30	24	60	28	70	26.6
35	60	120	70	140	30.8
40	120		140		---> 40

\* Average exchange rate was in 2003 1€ = 1,695,300 TL

Source: [www.de-kant.com/vergi\\_dosyalar/vergi002.htm](http://www.de-kant.com/vergi_dosyalar/vergi002.htm)

<sup>23</sup> Tunali et al. (2003).

<sup>24</sup> OECD, Taxing Wages, 2002.

<sup>25</sup> for a single individual without children.

### 3.2.2. *Income support for unemployed*

The unemployment insurance system was established in August 1999. Collection of premiums commenced on June 1, 2000. Since the law requires the payment of at least 600 days of premiums in a 3 year period before receiving unemployment benefits, the first payments began in March 2002. The system applies to workers who are registered in the Social Insurance Institution (SSK) and does not cover civil servants or the self employed.

The system is designed as a group insurance policy for workers who lose their jobs involuntarily and are not at fault. Premium contributions are calculated as a fraction of the worker's gross wage and equal 2 percent for the worker, 3 percent for the employer, plus an additional 2 percent that comes from the State. The characteristics of the unemployment benefit system are given in table A8. In addition to these payments, health insurance coverage, job search help, vocational training, vocational development and retraining services are provided to the unemployed.

The insurance fund is managed by a board consisting of employee, employer and Treasury representatives, and is headed by the Director General of İŞKUR, the Turkish Employment Organisation, which was established in July 2003.

Of the total 2.3 million unemployed in 2002 only about 550 thousand were registered with İŞKUR in October 2002. Of these only 40 thousand were collecting unemployment benefits. This figure has certainly increased significantly in the last year, but the coverage of unemployment insurance is still low.

In Turkey there are three major social security institutions. The Social Insurance Institution (SSK), the Pension Fund for civil servants and Bag-Kur, which is a fund for self-employed. However 54,4% of employed persons were not registered in any social security institution in Turkey (table IV.3). Of these 68% were residing in rural areas and 86,6% were employed in the agricultural sector. This low coverage of the pension system is likely to exert pressure later, when these unregistered people become needy.

Table IV.3: **Percentage of employed persons unregistered in social insurance institutions, 3rd quarter 2003**

	total	agriculture
Total	54.4	91.4
Regular employee	18.5	39.8
Casual employee	92.2	97.4
Employer	17.9	68.0
Self-employed	65.9	81.3
unpaid family worker	97.9	99.5

Source: SIS (2003)

Recently the social insurance system of the private sector (SSK and Bag-Kur) faces increasing non-payments of contributions. The arrears of contributions amounted to almost 6% of GNP. In autumn 2003, the government opened a payment facility to restructure the existing arrears. On demand of the IMF the partial "amnesty" for non-payments will not be repeated.

The pension system was reformed in 1999 but the new provisions could only be implemented in May 2002. For new entrants the minimum age of retirement will be 58 for women and 60 for men. Formerly the earliest retirement age was 38 (providing 20 years of employment) for women and 43 (25 years employment) for men.

Two major institutions provide *social assistance* for people below the poverty line, mostly elderly or disabled people and children. A large part of these benefits comes in kind (food, clothes, meals etc.). The eligibility to the benefits varies and is set at the regional or municipal level.

### 3.3. Employment protection legislation

Turkey has started to change its laws and regulations in accordance with the *acquis*. On May 22, 2003 a new labour law was enacted by parliament and became effective on June 10, 2003. The decrees related to the new Labour Law are expected in the first quarter of 2004. Thus, one has to wait to judge the implementation of the new regulations. The new law complies much more with the EU directives than the former law. Important changes concerned the *working time*. In the old labour law the weekly working time was set at 45 hours. The new law defines a normal average weekly working time, for which the worker is paid the “normal” wage rate, as 45 hours. The limit for overtime work is set at 270 hours. Thus, a worker fully using the limit of overtime work can have a maximum working time of 50.4 hours per week, if she works 50 weeks a year. These regulations do not comply with the EU directive, which calls for a maximum average weekly working time of 48 hours.

The new law does not comply with the requirement of a “paid annual leave of at least four weeks”. Workers, that are employed 1 – 5 years are only given 14 days annual leave in the Turkish law.

Other changes include mandatory written labour contracts, a probation period of 2 months (1 month in the old law) with social insurance from the first day of employment. The new legislation improved the regulations concerning part-time and fixed term work, collective redundancies, protection in case of insolvency and the protection of young people at work.

High severance payments in the old labour law had been criticised to hinder job creation and promote working in the shadow economy. With the start of the unemployment insurance severance payments became somewhat redundant. The new labour law abolished these payments and in addition reduced the unfair dismissal compensation. As in the case of temporary employment, the protection of regular labour was significantly reduced.

For a detailed overview see table IV.4, which compares the old and the new law to the Council Directives on employment. A positive mark (+) for the labour law shows that they are in conformity with the EC directive. A negative sign (-) represents non-conformity or that the issue is not addressed in the law. A question mark (?) means the issue is not addressed in a well-defined way, or there are some differences between the law and the directives.

Table IV.4: EC directives and the Turkish Labour Law

Directive Date of issue [Enter into force]	Issues/Regulations	Labor Law Law 1475 [Relevant articles]	New Labor Law Law 4857 [Relevant articles]
93/104 Organization of working time 23 November 1993 [23 November 1996]	? normal weekly work ? max weekly working time ? min period of daily rest ? min period of weekly rest ? min period of annual leave ? shift work ? night work (info / health) ? patterns of work	? + ? - ? + ? + ? - ? + ? - (excl. men) ? - [A. 41, 43, 49, 61-65, 73]	? + (45 hours) ? - ? + ? + ? - ? + ? + ? - [A. 41, 46, 53-70]
99/70 Framework agreement on fixed-term work (UNICE/CEEP/ETUC) 28 June 1999 [10 July 1999]	? definition of fixed-term work ? definition of "comparable permanent worker" ? abuse arising from the use of successive fixed-term contracts ? rights of fixed-term workers ? information / training	No specific clause on fixed-term work   [A.8 defines only temporary and permanent work]	? + ? ? ? ? (no limit) ? + ? ? / - [A. 11-12]
97/81 Framework agreement on part-time work (UNICE/CEEP/ETUC) 15 December 1997 [20 January 2000]	? definition of fixed-term work ? definition of "comparable full-time worker" ? no shift from full-time to part-time work without consent ? rights of part-time workers ? information / training	No specific clause on part-time work   [A.8 defines only temporary and permanent work]	? + ? ? ? + ? + ? ? / - [A. 13]
98/59 Collective redundancies 20 July 1998 [1 September 1998]	? definition of collective redundancy ? information and consultation ? procedure	? - / + (changed by Law 4773) ? - / + (changed by Law 4773) ? - / + (changed by Law 4773) [A. 24]	? + ? + (exc. A 2.3.b.v and vi) ? + [A. 29]
2001/23 Employees' rights in the event of transfers 12 March 2001 [12 April 2001]	? employees' rights ? employers' liabilities ? info and consultation	? + ? + ? - [A. 14, 53, Law 2822 A. 8]	? + ? + ? - [A. 6]
80/987 Protection of employees in the event of insolvency [Amended by 2002/74] 20 Oct 1980/23 Sept 2002 [28 Oct 1983 / 8 Oct 2002]	? claims ? guarantees (guarantee institution) ? coverage	No specific clause [Law 2004 on bankruptcy, A 206 workers' claims have priority in the event of insolvency]	? + ? + ? + [A. 33]
94/33 Protection of young people at work 22 June 1994 [22 June 1996]	? definition of "young" ? employers' obligations ? restrictions	? - ? - ? - [A. 67. Also regulated by the Law on Apprenticeship and Vocational Training, No. 3308]	? + ? + ? [to be regulated by the MESS] [A. 71 -73, 85, 87]
91/533 Information for employees 14 October 1991 [30 June 1993]	? information content ? time limits ? enforcement	? +? ? - ? + [A. 9 and 11]	? +? ? + ? + [A. 8]
2002/14 Consultation and employee representation 11 March 2002 [23 March 2005/2007]	? information content ? coverage ? procedures / enforcement	? - ? - ? -	? - ? - ? -

Source: E. Taymaz, S. Özler, (2003), Table 3.

The OECD undertook a major effort to compare employment protection across countries. The employment protection legislation index (EPL index) covers regular employment, temporary employment and collective dismissals and ranks the legislation between 0 and 5 (most restrictive). Based on the old labour law Turkey had the second strictest employment protection legislation after Portugal with an EPL index of 3.6. This was almost completely due to the strict protection of temporary contracts and high severance payments. The new Labour law improved much on both issues. The EPL-index based on the provisions of the new law would give a value of about 1.5. Thus, if the new law is effectively implemented, Turkey would belong to the countries with rather a flexible protection legislation like Denmark, Hungary or the Czech Republic.

Specialised Labour Courts deal with individual as well as collective labour disputes. The High Council of Arbitration is involved in settlement, conciliation, and arbitration of collective disputes.

#### **4. Migration**

In 2000 about 3.6 million Turks resided abroad, most of them, about 3.2 million, in Europe. By far the most important host country is Germany with about 2 million Turkish nationals. It is estimated that about one third of the Turkish population abroad emigrated for reasons of employment. This would amount to 5.1% of the Turkish labour force. In the last years about 1000 highly qualified professional workers migrated annually to jobs abroad in IT, finance or managing. In addition, about a quarter of students abroad do not consider returning to Turkey.

The emigration flows from Turkey declined over time. While in the nineties about 100 thousand emigrated annually the figure was down to 60 thousand in 2000. This is also reflected in the data of Turkish emigration to Germany. (Table IV.5) After the mid-eighties the net-immigration to Germany was drastically reduced and became less volatile. A further drop of inflows occurred in the mid-1990s when asylum migration receded. This was clearly the result of changed German laws regulating immigration. In the seventies more than half of the Turkish population in Germany belonged to the labour force. In the last decades growth of the Turkish population in Germany continued, while the employment of Turkish nationals remained almost unchanged during this time. The Turkish population in Germany grew because of the natural growth of the foreign population and as a result of asylum and family reunion. Asylum flows from Turkey, these mostly being Kurds, declined from 20,000 in the mid-nineties to 10,000 in recent years. Since 1991 the migration between the two countries is regulated by bilateral agreements.

The Turkish nationals in Germany amounted to 2.8% of the Turkish population in 2002. According to one estimate this share would increase to about 4% in the long run if Turkey stays outside the EU and no free movement of labour applies. With unrestricted



labour mobility and membership in the EU the share of Turkish population in Germany would increase to 8%.<sup>26</sup>

Table IV.5: **Turkish migrants in Germany**, in thousands

	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002
inflow	83.6	81.9	80.6	67.8	63.9	73.6	73.2	56.0	48.0	47.1	49.1	54.6	58.6
asylum seeker	22.1	23.9	28.3	19.1	19.1	25.5	23.8	16.8	11.8	9.1	9.0	10.9	9.6
outflows	35.1	36.1	40.3	46.3	46.4	43.2	43.5	46.0	45.1	40.9	39.0	35.9	36.7
net migration	48.5	45.8	40.3	21.5	17.6	30.4	29.7	10.0	2.8	6.2	10.1	18.7	21.9
stock of													
population	1694.6	1779.6	1855	1918	1965	2014	2049	2107	2110	2053	1999	1947	1912
labour								1039		1008	1290	1004	
socially insured*	594.6	632.3	652.1	631.8	605.1	600.4	578.2	559.8	564.4	565.9	551.7	548.7	529.1

\* West Germany; June 30 of respective year.

*Note:* Net migration and change of stocks of population do not coincide because of natural growth of the migrant population, naturalisation and differences in data collection.

*Source:* Federal Statistical Office of Germany

Transit migration and the flows of illegal migrants, often smugglers and traffickers, declined recently. In 2002, 82,000 illegal migrants were apprehended, 10,000 less than the year before. Despite the progress, further co-ordination and co-operation with the EU in the area of illegal migration is needed. (Joint Action Programme on Illegal Migration) Visa policy as well as the migration and asylum strategy were further aligned with the *acquis*. With several countries readmission agreements were negotiated or signed in 2003. However, such readmission agreement between the EU and Turkey does not exist as yet.

<sup>26</sup> Sinn et al. (2001) Compared to other studies this study provides estimates at the higher end for migration from Eastern Europe to Germany. Thus, the projection of Turkish migration, which is not included in the other studies, is probably also rather high.

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## Statistical Appendix

Table A1: **Growth of GDP, employment, and productivity**

	1995	1996	1997	1998	1999	2000	2001	2002	2003	cumul. change 02/94	cumul. change 02/99
<b>Bulgaria</b>											
GDP	2.9	-9.4	-5.4	3.9	2.3	5.4	4.1	4.8	4.9	7.8%	15.0%
employment	1.3	0.1	-3.9	-0.2	-2.1	-3.5	-0.4	1.5	1,5	-2.9%	-2.4%
labour productivity	1.6	-9.5	-1.5	4.1	4.5	9.2	4.5	3.2	3,4	26.2%	17.8%
<b>Romania</b>											
GDP	7.1	3.9	-6.1	-4.8	-1.2	2.1	5.7	4.9	4.9	11.3%	13.2%
employment	-5.2	-1.2	-3.8	-2.3	-4.5	2.5	-0.8	-8.7	-0,2	7.8%	-7.2%
labour productivity	13	5.2	-2.3	-2.5	3.5	-0.3	6.6	14.8	5,1	43.0%	22.0%
<b>Turkey</b>											
GDP	7.2	7	7.5	3.1	-4.7	7.4	-7.5	7.8	5,8	29.7%	7.1%
employment	3.7	2.1	-2.5	2.8	2.1	-0.4	-1	0.2	1,5	7.1%	-1.2%
labour productivity	3.4	4.8	10.3	0.3	-6.7	7.8	-6.5	7.6	4,3	21.3%	8.5%

Source: European Commission (2003) Employment in Europe 2003; for 2003:EuroStat.

Table A2: **Employment rates: Progress towards the Lisbon and Stockholm targets**

	Total employment rate			Female employment rate			Older workers employment rate		
	2002	Gap below 2010	Change 2000-2003	2002	Gap below 2010	Change 2000-2003	2003	Gap below 2010	Change 2000-2003
<b>BG</b>	52,5	17,5	2,1	49,0	11.0	2.7	30.0	20.0	9.2
<b>RO</b>	57.6	12.4	-5.4	51.5	8.5	-6.0	38.1	11.9	-11.4
<b>Turkey</b>	44.4	25.6	-1.6	25.3	34.7	+0.4	35.3	14.7	-1.1
<b>AC-10</b>	55.9*	14.1	-1.6*	50.2*	9.8	-1.2*	30.5*	19.5	1.0*
<b>EU-15</b>	64.3	5.7	0.9	56.0	4.0	1.9	41.7	8.3	3.9
<b>2010 Target</b>	70%			More than 60%			50%		

\* 2002.

Source: European Commission (2003) Employment in Europe 2003; Eurostat.

Table A3: **Employment structure in % of total employment (15 – 64)**

	Agriculture	Industry	Services
Bulgaria	9.9	33.0	57.1
Romania	32.3	32.2	35.5
Turkey*	34.9	23.0	42.1
EU-15	3.7	28.4	67.9

\* according to Turkish statistics 15+

Source: European Commission (2003), Employment in Europe 2003; SIS (2003).

Table A4: **Unemployment rate by gender, % of labour force 15+**

	Total		Men		Women	
	2003	Change 2000-2003	2003	Change 2000-2003	2003	Change 2000-2003
BG	13.6	-2.8	13.9	-2.8	13.2	-3.0
RO	6.6	-0.4	6.9	-0.3	6.2	-0.1
Turkey	10.5	4.0	10.7	4.1	10.1	3.8
AC-10	14.3	0.7	13.7	0.9	15.1	0.3
EU 15	8.1	0.3	7.4	0.7	9.0	-0.2

Source: European Commission (2003), Employment in Europe 2003; Eurostat, SIS (2003)

Table A5: **Youth unemployment rate and long-term unemployment rate 2002**  
(% of labour force 15-24; % of labour force)

	Youth unemployment rate			Long-term unemployment rate		
	Total	Men	Women	Total	Men	Women
BG	35.5	39.0	31.4	11.9	12.3	11.5
RO	18.5	18.6	18.5	3.8	3.8	3.7
Turkey	19.6			3.7		
AC-10	31.9	31.4	32.7	8.1	7.4	8.9
EU-15	15.1	14.8	15.5	3.0	2.6	3.9

Source: : European Commission (2003), Employment in Europe 2003, OECD

Table A6: **Minimum wages (1.1.2004)**

	in national currency	in €	exchange rate against €
Bulgaria	120 BGN	61	1.96
Romania	2,8 million ROL	67	42,026
Turkey gross	423 million TL	235	1,796,000
Turkey net	303 million TL	169	1,796,000

Table A7: **Payroll contributions, in % of gross wage**

	Bulgaria	Romania	Turkey
Social security contributions	24.7% (employer) 8% (employee)	33% (two third paid by the employer, one third paid by the employee)	11% (employer) 9% employee
Unemployment fund contributions	3% (employer) 1% (employee)	3% (employer) 1% (employee)	3% (employer) 2% (employee)
Health care contributions	4.5% (employer) 1.5% (employee)	7% (employer) 7% (employee)	6% (employer) 5% (employee)
Others			3,5% (employer)
<i>Total</i>	<i>42.7%</i>	<i>52%</i>	<i>39,5%</i>

Source. JAP, Taymaz and Özler (2003)

**Table A8: Attributes of unemployment benefit systems**

	<b>Bulgaria</b>	<b>Romania</b>	<b>Turkey</b>
Qualifying conditions	Employed for 9 months in last 15 months, for seasonal work for 6 months in last 12 months  Willingness to accept a job or training offered by PES	Employed for 12 months in last 24 months  Monthly visit and willingness to accept a job or training offered by PES	Employed for 600 days in last 3 years
Duration of payment	4-12 months depending on previous employment record. Maximum duration of 12 months corresponds to 25 years of service.	6, 9 or 12 months depending on previous employment record (up to 5 years, between 5 and 10 years, 10 years and over): Minimum request: 1 year of contributions.	6, 8 or 10 month depending on previous employment record (600 days, 900 days or 1080 days)
Monthly unemployment benefit	60% of gross wage during the last 9 months, subject to a minimum (70% of minimum wage) and maximum (130% of minimum wage)	Flat amount of 75% of gross minimum wage	50% of net wage in last 4 month  Maximum: net minimum wage
Taxation	Tax-free	Tax-free	Tax-free

Source: JAP, Taymaz and Ölzer (2003)

Chart A1: **Minimum Wages in the EU and the Accession Countries**

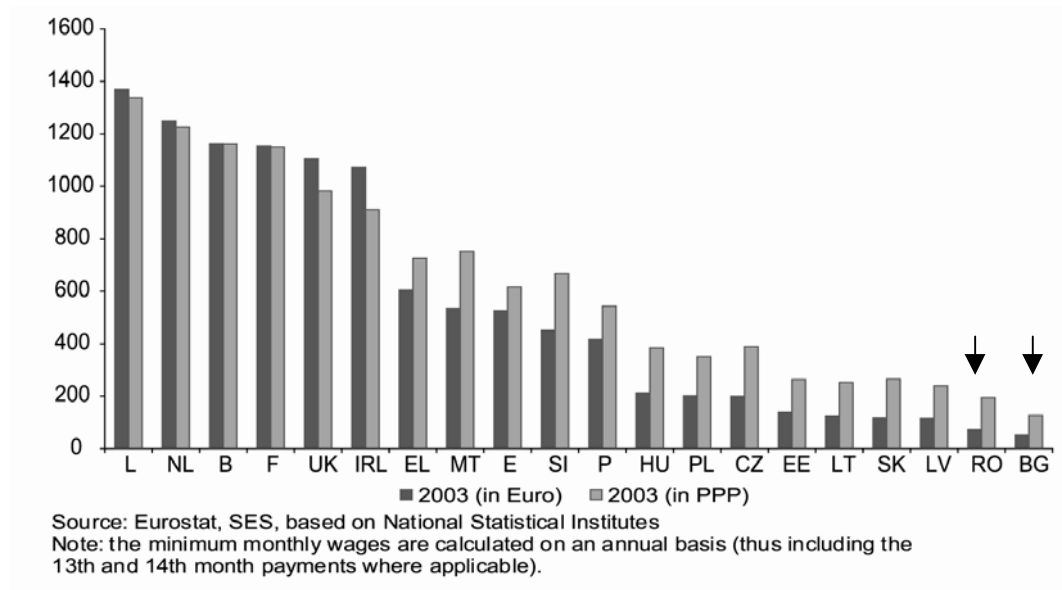
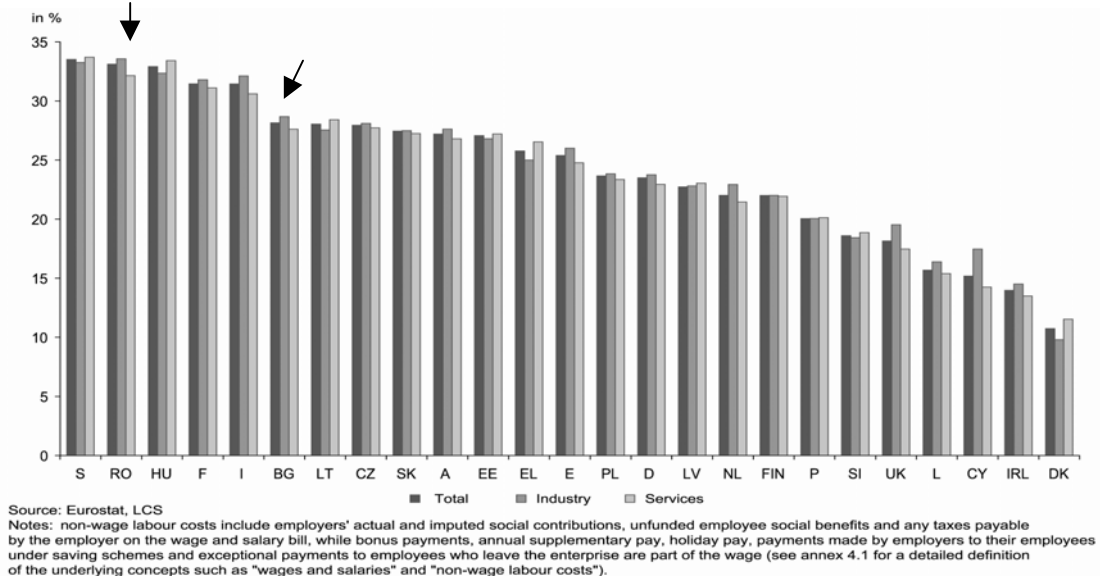
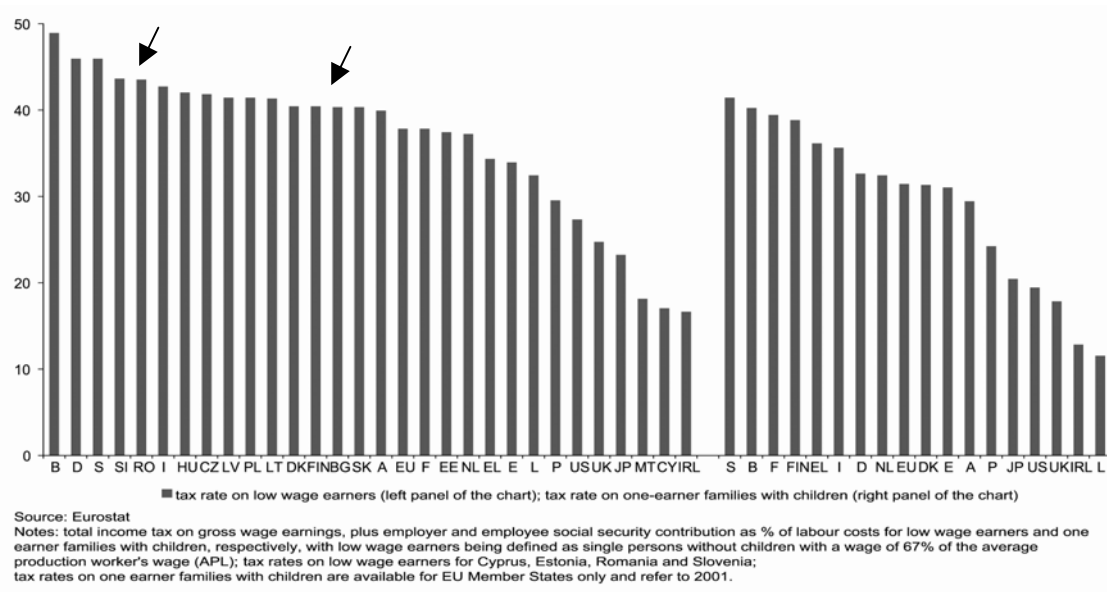


Chart A2: **Share of non-wage labour costs in industry and services, 2000**



**Chart A3: Tax burden on labour in the EU and the Accession Countries, 2002**





## Annex A: Social sustainability

Per capita income in PPP in the countries is about a quarter of the EU-15 level. Poverty as measured by the World Bank (table A9) is significantly higher in Bulgaria and Romania than in the poorest acceding countries. Poverty in Turkey was in 2000 close (but still somewhat higher) to the level in Latvia in 1998. Minimum wages in purchasing power standards were around 200 € in Bulgaria and Romania and twice as high in Turkey. High unemployment in Bulgaria and Turkey with low unemployment benefits and a small base of eligible people (in Turkey) are also part of the poverty in the countries. Social transfers in the three countries are low and have only a small impact on the poverty rates.<sup>27</sup> The level of pensions was in the mid-nineties about 35% of per capita income in Bulgaria and Romania and 56% in Turkey. Average monthly pensions in Bulgaria and Romania in 2002 were slightly above 150 € measured in purchasing power parities.

Table A9: **Poverty**

	Survey year	Population below	
		\$ 1 a day %	\$ 2 a day %
Bulgaria	2001	4.7	23.7
Romania	2000	2.1	20.5
Turkey	2000	< 2	10.3

Source: WDI 2003

All of the countries have a high share of agricultural employment. In Bulgaria a large part of labour force works in agriculture but has also a non-agricultural occupation. Therefore, the measured employment share in agriculture differs considerably depending on the classification of the main employment.<sup>28</sup> In economic terms however, the share of agricultural labour in Bulgaria is comparable to that in Romania and Turkey. Poverty and a high share of agricultural employment are central issues of development problems, which might demand specific policy to overcome misallocation and market rigidities.

A large part of the rural population receives its main income from subsistence economy and housing (i.e. imputed rents). In addition, much of the agricultural work is done along traditional lines within extended family units. Income sharing is likely the domi-

<sup>27</sup> Social transfers reduce the poverty rate in Bulgaria by 3, in Romania by 5 and in Turkey by 4 percentage points, while in the EU-15 poverty is reduced by 9 and in the AC by 12 percentage points through social transfers. The poverty rate is measured by the share of persons below the threshold of 60% of national disposable income. See: Structural indicators (social cohesion) for the Spring Report to Lisbon Strategy (2004).

<sup>28</sup> Employment in agriculture classified by main occupation according NACE are only 8 – 9% of total employment. However, if total work in agriculture is considered the share is close to 30%. (see: country fiche „Bulgaria“ ECFIN/29/04-EN)

nant form of payment among the family members. Thus, incomes are determined by average rather than marginal productivity. This might also apply to other forms of work as family-run petty retail trading etc. The existence of a sector based on income sharing as well as other sectors, whose activity is dominated by profit maximisation, are a sign of dualism in the economy.

The countries concerned show quite different rural-urban migration flows. In the last years agricultural employment declined and urban labour supply increased in Turkey. The reduction of agricultural subsidies as part of the Turkish stabilisation programme was one of the determinant of these migration flows. In contrast, a flow from urban to rural areas is observed in Romania. At least partially this is explained by social need and insufficient possibilities for earnings in the urban areas. Continuing direct or indirect subsidisation of agriculture might also play a role. The Bulgarian situation is unclear due to data issues mentioned above, but the share of agricultural employment does not seem to decline. In any case, if familiar employment and labour market policies are considered, the appropriate subject should be the non-agricultural labour force. Average figures that include agricultural labour would distort the picture and the validity of the analysis.

In the medium term, if a catch-up process should realise, a shrinking of the agricultural sector in all countries is likely to be necessary. This process might need policy support to achieve an efficient allocation of labour but avoid oversupply and the creation of large informal sectors in the urban areas. Wages in urban sectors might be too high and will not support an equilibrium for several reasons:

- i) The unionisation in urban areas is higher and wages are more flexible in rural areas
- ii) As said, payment in agriculture might be governed by income sharing rather than marginal productivity
- iii) The formal urban sector is often a showcase for government policy with minimum wages, pension schemes, and unemployment benefits. Thus, workers compensation is higher than in agricultural work without these benefits
- iv) Efficiency wages might be used more often in urban work to elicit effort for work which is difficult to monitor.

If such rural- urban wage differences exist, the oversupply of labour leads to a widening informal urban sector. Migration and the extent of informal work are at least partially interlinked, which might create a trade-off between efficient allocation of rural-urban labour and the retrenchment of the informal economy (the base of a socially unprotected population). The existence of a large stock of socially uninsured people in agriculture as well as in the informal sector will put a large burden on future state budgets and leads to far-reaching social problems with possibly political implications.

## Annex B: Shadow economy

Estimates of the shadow economy of Bulgaria and Romania by F. Schneider show significantly higher values for these countries than for the acceding countries regardless of the method used for the estimation. (Table A10)

According to the labour force survey (4th quarter of 2003)<sup>29</sup>, 33% of the urban employed persons in Turkey were not registered with the social insurance institutions. If one considers only the regular employed the rate of unregistered person is 19%. This figure can be taken as a lower bound of the shadow economy. Almost all casual employed and unpaid family workers are not registered. In agriculture, where almost all labour force is either self-employed or unpaid family worker more than 90% are unregistered. At least a part of the casual employment as well as the agricultural employment has probably also to be counted to the informal sector, because of underreporting of incomes.

Table A10: **The Size of the Shadow Economy in Transition Countries**

	Size of the Shadow Economy (in % of GDP)				Shadow Economy Labor Force in % of (Working Age) Population 1998/99
	Physical Input (Electricity) Method Using Values from Johnson et. al. (1997)		DYMIMIC Method		
	Average 1990-93	Average 1994-95	Average 1990-93	Average 2000/01	
Bulgaria	26.3	32.7	27.1	36.4	30.4
Romania	26.0	28.3	27.3	33.4	24.3
<i>Unweighted Average: Central Eastern European Countries</i>	<i>22.4</i>	<i>25.1</i>	<i>23.4</i>	<i>29.2</i>	<i>23.3</i>

1) Working age population means population between the age of 16 and 65.

Sources: Own calculations using the DYMIMIC method and values using the Physical input method are from Johnson, Kaufmann, and Shleifer (1997, table 1, p. 182-183), Johnson, Kaufmann, and Zoida-Lobatón (1998a, p. 351).

Source: Friedrich Schneider (2002), The Size and Development of the Shadow Economies of 22 Transition and 21 OECD Countries *University of Linz and IZA Bonn Discussion Paper No. 514*, June

Quite different approaches are used to estimate the shadow economy. The electricity-method takes electricity consumption as a proxy for of total production. The difference between the official GDP and the via electricity consumption approximated GDP is counted as shadow production. DYMIMIC stands for dynamic multiple indicators multiple causes approach. By statistical methods causes of the informal sector as tax burden are related to indicators of the shadow economy as the velocity of cash money or the participation rate. From the estimation parameters the size of the unobserved shadow economy can be deduced.

<sup>29</sup> State Institute of Statistics (SIS) ([www.die.gov.tr/english/SONIST/ISGUCU/09030413.gif](http://www.die.gov.tr/english/SONIST/ISGUCU/09030413.gif))