

Peer-reviewed academic journal

**Innovative Issues and Approaches in
Social Sciences**

IIASS – VOL. 7, NO. 2, MAY 2014

Innovative Issues and Approaches in Social Sciences

IIASS is a double blind peer review academic journal published 3 times yearly (January, May, September) covering different social sciences: political science, sociology, economy, public administration, law, management, communication science, psychology and education.

12

IIASS has started as a Sldip – Slovenian Association for Innovative Political Science journal and is now being published in the name of CEOs d.o.o. by Založba Vega (publishing house).

Typeset

This journal was typeset in 11 pt. Arial, Italic, Bold, and Bold Italic; the headlines were typeset in 14 pt. Arial, Bold

Abstracting and Indexing services

COBISS, International Political Science Abstracts, CSA Worldwide Political Science Abstracts, CSA Sociological Abstracts, PAIS International, DOAJ.

Publication Data:

CEOs d.o.o.

Innovative issues and approaches in social sciences, 2014,
vol. 7, no. 2

ISSN 1855-0541

Additional information: www.iiass.com

ADJUSTMENT DURING THE CRISIS: INSTITUTIONAL BUFFERS ON THE EASTERN EUROPEAN LABOUR MARKETS

Pavol Babos¹

Abstract

The economic crisis had profound effects on labour markets of the EU member states in terms of a decline in employment and a rise in unemployment. This paper investigates how the states limited the impact of the change in economic output on the employment and the unemployment. The analysis suggests that there are different labour market institutions influencing the impact of the fall in GDP on the employment decline and unemployment increase. The first part of the paper explores and compares the extent to which the labour market institutions cushioned the impact of the economic crisis on the EU countries. The second part of this paper provides an in-depth comparative analysis of the labour market institutions and the adjustment mechanisms in Central Eastern European countries: Latvia, Slovenia and Slovakia. In the end this paper suggests that the specific institutional setting of a country, according to the Varieties of Capitalism, might shape the form of the government response to the crisis and the effect of particular institutions on the adjustment channels. The study shows that adjustment in Slovenia took place mostly within the firms, while in Latvia the most efficient adjustment channels actuated outside the firms, mostly within the government sponsored training programmes and international migration. In Slovakia, government sponsored adjustment, which focused on maintaining the existing positions, prevailed together with the promotion of self-employment.

Keywords: Crisis Adjustment, Labour Market Institutions, Unemployment

DOI: <http://dx.doi.org/10.12959/issn.1855-0541.IIASS-2014-no2-art02>

¹ Pavol Babos, PhD is a Junior Analyst at the Institute for Forecasting, Slovak Academy of Sciences. Contact address: pavol.babos(at)savba.sk

Introduction

By the beginning of 2011, almost the entire European Union has begun to recover from the global economic crisis. There is a general agreement in the literature that the EU economy experienced the hardest hit in mid-2008 (Spiegel & Rose 2009, Rosenberg & Purfield 2010). The extent of both the drop in economic output and the fall in the employment and the rise in the unemployment varied significantly among the EU member countries. However, after a closer look at the development in the individual states, one finds examples of simultaneous GDP falling and employment rising, as well as states' drop of output and decrease in unemployment.

This paper investigates the relation between the change in the economic output and the change in the employment and the unemployment in the EU member states. The research was inspired by the similar study by Leschke & Watt (2010) and expands the timeframe of the research and shifts the focus towards Central Eastern Europe. In their original study, Leschke & Watt sought to explain how the labour market institutions influenced the sensitivity of the employment and the unemployment on the economic crisis. Studying four of the Western European countries within a one year time frame, they found that several labour market institutions (hereafter LMI; such as short-time working schemes or employment protection legislation) had considerable influence on softening the effects of the economic shock. This was especially true for countries such as Germany and Denmark, which used the short-time working schemes before the crisis; they were able to either avoid or delay the consequences. Leschke and Watt also found that disability measures and early retirements did not play a significant role in the four countries.

This paper attempts to add value to this line of research by shifting the focus on Central Eastern European countries and widening the timeframe. Including the EU New Member States in the research of adjustment during the crisis is important for several reasons. Firstly, these countries experienced a much faster economic growth before the crisis and a considerably larger contraction of production during the crisis. Also, the productivity growth was faster in the CEE countries due to the catching up process (e.g. Égert, Drine, Lommatzsch and Rault 2003). These reasons provide a strong rationale to investigate the labour market institutions in the CEE countries. We use the term "buffers" as coined by Leschke & Watt (2010).'

Reviewing briefly the development of the labour markets in the EU27, this paper first explores the variation in the change of un/employment in

relation to the change in output. Subsequently, the study focuses on the detailed comparison of the three Central Eastern European countries: Latvia, Slovakia and Slovenia.

After the introduction, the paper continues with a more general section analysing the labour market development in the EU27 with a special focus on the selected countries. This section also draws the conceptual linkages between the core fields of interest – economic output in terms of GDP, employment and unemployment. The sequent third section presents the in-depth analysis of the labour markets development and the role of institutions in their performances in the sample countries. The concluding section discusses the potential influence that the varieties of capitalism have on the form of the adjustment, particularly in the selected countries, as well as generally.

Theoretical Background

Conceptual Linkages between Labour Markets Performance and Institutions

According to the economic theory (the production function), the economic output of a firm depends on the input of labour and capital, e.g. land and technology. In the case of an economic shock, a firm adjusts the input factors according to the demand for its products or services. This paper assumes that adjusting the input of capital is difficult or impossible in the short-term. Therefore, in the case of a sudden fall in demand it is the labour input that is adjusted. Consequently, assuming the capital input is constant; the economic growth might be decomposed as the multiplication of the labour input growth and the hourly labour productivity growth.

In the perfect market environment the labour adjustment usually means laying off workers. This is the easiest solution for firms, and in a perfectly fluid labour market there are no limits to such a measure. Firms can rely on flexible hiring once the demand for the product increases again. However, this is not the case for the EU countries with the developed employment protection legislation and institutions regulating hiring and firing. Thus, firms use the distinct measures to adjust the labour input, for example, quickly re-assigning some of their staff from production to other unproductive activities such as trainings, seminars or maintenance activities. Consequently, the hourly labour productivity decreases and helps to keep the input of labour relatively higher.

The elasticity of the economic output and labour input is to a considerable extent dependent on the changes in labour productivity. This article argues that the labour market institutions facilitating the re-assigning of workers (e.g. benefits for within-firm training) constitute the first institutional buffer. This softens the transfer of the loss in the output into the rise in the unemployment. It does so by lowering the labour productivity.

Change in the labour productivity, however, is not the only option available. The year 2008 saw a considerable rise in using different tools for working time adjustments. Many governments introduced incentives to stimulate firms to use a variety of work-sharing schemes or flexible time accounts. These measures allowed firms facing economic hardships to adjust the working time of their employees and still keep the headcount employment at a constant level. Such measures are considered the second institutional buffer that prevents employment from shrinking despite the fall in the economic output.

Workers, who lose their position, although temporarily, are considered to be out of employment and are not reflected in employment statistics. However, they are not automatically registered as unemployed either. States developed a variety of policies to keep people away from the official unemployment status. Different training schemes and educational programmes for people to ensure they can find a job more easily in the future are a few such programs falling under these policies. On the other hand, there are also early-retirement options and other types of “voluntary” inactivity that translates into a lower level of unemployment. These policies create the third institutional buffer, influencing the pace of such a translation of the loss of employment into unemployment. To answer the questions raised in the study it is necessary to include the international migration of workers within this third institutional buffer.

This study takes the development of GDP as a given fact during the recession period. We investigate the performance of the labour market institutions in cushioning the effect of the output decline into the rise of unemployment. Put simply, this study assumes the static relationship between the variables in short-term. However, it is probable that the labour market institutions have some effect on the output development in long-term, by maintaining higher employment levels and thus preventing the demand from a deeper decline.

As explained by Leschke & Watt (2010), Luxembourg should be excluded from the intra-EU comparison for methodological reasons. More than half of its GDP is accounted for by non-residents, mostly

French and German citizens. Therefore there is a strong assumption that transmission mechanisms between the economic output and employment and unemployment described below would be outweighed by migration and therefore render the regression analysis biased. This argument led the authors to leave Luxembourg out of the analysis. However, for the sake of simplicity, we refer to the EU or EU27 as a whole.

Labour Markets and Varieties of Capitalism

Various adjustment mechanisms were not used across the EU to the same extent. Similarly, member states did not introduce, or strengthen, exactly the same labour market policies fighting the crisis. Answering why it is so could also help us to understand why different institutional buffers were more successful in some states and less in others.

Generally, it is primarily a firm's decision how to adjust the labour input in times of a drastic output decline. However, firms operate in a certain institutional setting, which provides incentives for certain types of decisions and discourages other ones. Additionally, firms in most EU member states are required to coordinate, or at least consult the large-scale measure with trade unions or employees' council, public employment service, or other state agencies (World Bank, 2010). The form of relationships firms have with other relevant actors in the economy therefore influences the form of adjustment within firms and indirectly influences the policies states might need to adopt. The 'Varieties of Capitalism' theory (hereafter VoC; Hall and Soskice, 2001) reflects this actor-centred approach more thoroughly, including the coordination strategies of firms.

In the VoC approach firms interact with other actors on a daily basis and many choices they make depend on how they solve the problem related to the coordination of behaviour of all market actors (Hall & Soskice 2001). Solving these coordination problems depends on the institutional settings of the particular political economies in which firms operate, defined as "*systems of rules that structure the courses of actions that a set of actors may choose*" (Scharpf 1997: 38). Usually the choices influence wages, workers' skills, employment and other labour market related outcomes. In times of economic crisis the type of coordination firms evolved to use may impact the adjustment mechanism they will apply.

Two ideal types emerged in the Hall & Soskice's analysis (2001). In the Liberal Market Economies (LME) hiring and firing costs are rather low,

the labour force is generally skilled, trade unions are weak and the coordination between the actors is to a large extent driven by market forces. Some authors also relate the LME model to a weak or underdeveloped welfare system (Bohle & Greskovits 2007). On the other hand, Coordinated Market Economies CME are known for strategic coordination among actors, informal relations, rich networks and associations. This results in rather rigid hire & fire practices and longer redundancy notices.

Varieties of Capitalism approach has been extensively applied to the CEE region recently (Feldman 2006, Bohle & Greskovits 2007, Knell & Srholec 2007, Babos 2010). Although there is still an on-going debate on the classification of the CEE countries, a basic consensus is as follows. Slovenia is the closest example of a strategically coordinated economy; the Baltic States resemble liberal market-coordinated economies, while the Czech Republic, Poland, Hungary and Slovakia have relatively mixed institutions.

Selection of the countries for comparative analysis is based on the VoC classification. Similarly to Leschke and Watt (2010), we included one country from each group, i.e. Latvia, Slovakia and Slovenia. This allows us to investigate the functioning of labour market institutions across different production regimes and to compare the effect of these institutions. In the selected country sample, Latvia represents the liberal market economy, Slovenia represents the coordinated market economy and Slovakia represents the group of countries with a mixed institutional setting.

Empirical Analysis

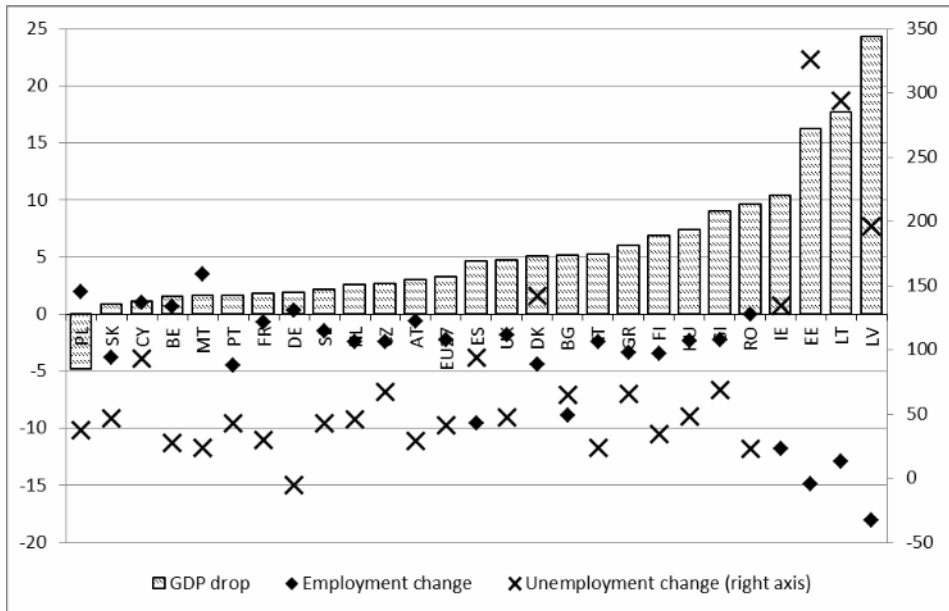
In order to explore the influence of the labour market institutions, this section starts with a brief review of economic development in the EU. We use data from the European Commission databases (Eurostat, Ameco, Labdev)¹. The time span of the analysis runs from the second quarter of 2008 to the same period in 2010.²

1 The total working hours were calculated as a product of total headcount employment and actual average-worked hours per person. Constructing the indicator this way, it is reliable enough to show broad trends in the EU27.

2 Selection of the time span for the study is based on the following reasons. Firstly, the same quarters of a year must be compared due to the unavailability of seasonally adjusted data. Since there is a broad consensus that the crisis hit most of the EU economies in mid-2008, the second quarter of this year was chosen as a starting point. Secondly, almost the whole EU27 was recovering by the end of 2010

Figure 1 shows the development of the main indicators. The Baltics was the highest hit region in the EU, with more than a 15% fall in GDP over two years. Other than that, there are no clear geographical patterns within the distribution of countries. The Central Eastern European countries are evenly distributed across the figure. Although the Slovene GDP declined sharper than the Slovak one, Slovenia's employment dropped less than Slovakia's.

Figure 1: Fall of GDP, Change in Employment (headcount) and Unemployment (shown on right y-axis), 2008Q2 to 2010Q2, in %



Source: European Commission, National Accounts

It is reasonable to assume that a sharper drop in economic output leads to a bigger loss in employment, measured as total-hours worked. Again, the three worst hit countries were the Baltic Republics with the loss of employment more than 12 percentage points. Slovakia and Slovenia were around the EU average (Figure 1). Baltic countries are also those with the highest increase of unemployed people. In Latvia, the number of people out of job has tripled, in Estonia this number was more than four times higher in 2010 Q2 comparing to 2008 Q2. Although the position of the Baltic States in this comparison is expected due to the fall in GDP, there is still an interesting difference regarding the previously discussed developments. While Latvia was the most severely hit by the fall in GDP and employment, it has experienced a considerably slower rise in the

unemployment, compared to its Baltic neighbours. This will be discussed in a more detail in the second part of this paper.

Output, Employment and Unemployment: Regression Analysis

Regression analysis proved that there is a significant relationship among the abovementioned concepts.¹ While predicted values from the regression are a reflection of the EU average, we use residuals for individual countries to compare the elasticity of the adjustment, e.g. the extent to which a change in one variable is accompanied by a change in another variable. Residual values thus express the deviation of the individual case from the line of the best fit, which is the average. Hypothetically, if there were no variation in elasticity, the predicted values would equal the observed values for all countries. While it is important to interpret the elasticity in question cautiously, this serves to highlight deviations of individual countries from the EU average.

Table 1 below presents the ranking of countries according to their residual values, showing the top three, bottom three countries and the countries of interest. Higher ranking of a country means it has a more effective adjustment mechanism². The differences between how the individual economies transpose the output shock into the loss of employment might be explained by the change in working hours (flexible time accounts, work-sharing schemes, short-time work, etc.). The standardized coefficient of 0.985 between the change in headcount employment and total hours employment indicates that an adjustment in working hours slowed down the loss of headcount employment. Romania, Latvia and Slovenia experienced the strongest effect of such an adjustment. On the other hand, Slovakia, Spain and Poland were among the least effective EU countries in this regard.

¹ The absolute values of the beta coefficients are in the Appendix 1.

² The full table with all residual values for all the countries is in the Appendix 2

Table 1: Ranking of Countries Based on Residual Values from Regression Analysis

| Rank | Output vs. Employment (headcount) | Output vs. Working Hours | Output vs. Unemployment | Employment vs. Unemployment |
|------|-----------------------------------|--------------------------|-------------------------|-----------------------------|
| 1st | Romania | Romania | Latvia | Cyprus |
| 2nd | Latvia | Latvia | Romania | Malta |
| 3rd | Slovenia | Lithuania | Slovenia | Poland |
| . | . | Slovenia (4th) | . | Slovenia (8th) |
| . | Slovakia (24th) | . | Slovakia (23rd) | Slovakia (21st) |
| 25th | Poland | Slovakia | Denmark | Ireland |
| 26th | Bulgaria | Spain | Cyprus | Bulgaria |
| 27th | Spain | Poland | Poland | Latvia |

Source: Eurostat, Author's own calculation

Regarding the relationship between the development of the economic output and unemployment, Latvia suffered a much smaller unemployment rise while experiencing a relatively greater output shock than its Baltic neighbours. Together with Romania and Slovenia (Table 1, third column) there seems to be LMI cushioning the unemployment increase most effectively. On the other hand, Slovakia, Denmark and Poland seem to have relatively poorer labour market performance. However, not all differences between individual countries can be easily interpreted by LMI. There are more factors that come into consideration, especially international workers' migration with respect to post-communist countries. This will be discussed further in the next section. Loss in the headcount employment is almost never translated into the rise of the unemployment to the same extent. Different mechanisms prevent a certain share of employment loss being classified as unemployed (as discussed above). Within the EU, Pearson's correlation coefficient between the headcount employment and unemployment is 0.812. Regarding the countries of interest, Slovenia ranked relatively high (8th). Both Latvia (27th) and Slovakia (21st) seem to have poorly operating labour market policies to prevent the rise of the unemployment.

The regression analysis indicates that several institutional mechanisms influence the extent of translation of the GDP fall into the employment and the unemployment. Based on the above, it is clear that there are substantial institutional buffers in the EU member states. Having set the

scene, we can proceed to the more comprehensive comparative analysis in the next section.

Labour Market Institutions in Post-Communist Europe: Comparison of Latvia, Slovakia and Slovenia

One of the main findings in the previous section was that the varieties of institutional adjustments in the national states prevented the output shocks from affecting the employment level to the full extent. This section attempts to explain the role that institutions and governments played in this process. Admittedly, this section replicates the structure of the working paper by Leschke & Watt (2010) to a certain extent. The authors examined four Western European countries in a one-year timeframe, while this paper compares the three post-communist countries over two years. The selection of countries was made deliberately so it would enable the comparison of representatives of different “varieties of capitalism” that emerged in Central Eastern Europe (Bohle & Greskovits 2007, Babos 2010). Thus we investigate Slovenia, Latvia and Slovakia.

Output to Employment Institutional Buffers

In theory, the easiest and most preferable firms’ reaction to the production fall would be a decrease in the labour input. However, the national economies are not a virtually perfect free market. Due to the institutional constraints, the immediate decrease in the labour input is not possible. Moreover, all the EU members enacted some type of the employment protection legislation (EPL) that imposes further administrative and financial costs when firing employees.

It is almost impossible to compare the EPL directly among the countries of interest due to the lack of comparative data. However, there is a way for an indirect comparison. In the OECD EPL Index 2008 (the latest available) Slovenia scored higher than both Slovakia and Estonia (supposedly the LME type; Latvia was not included since the country is not an OECD member state). According to the World Bank’s Doing Business report (2011), Latvia has relatively stronger EPL provisions than Slovakia (notice periods and severance payments for redundancy dismissal; no data available for Slovenia), with the exception of the severance payments for a redundancy dismissal of a worker with 20 or more years of tenure. Due to the post-communist history and the major structural changes that business sphere underwent during the last two decades (Myant & Drahokoupil 2011), it is reasonable to expect this specific provision to have marginal if any effect at all. Considering the

industrial relations, the VoC theory assumes Latvia to have the most flexible labour market rules and Slovenia to have the most rigid ones.

The strictest EPL applies usually only to full-time employees with permanent contracts. It is therefore necessary to have a closer look on other forms of employments.

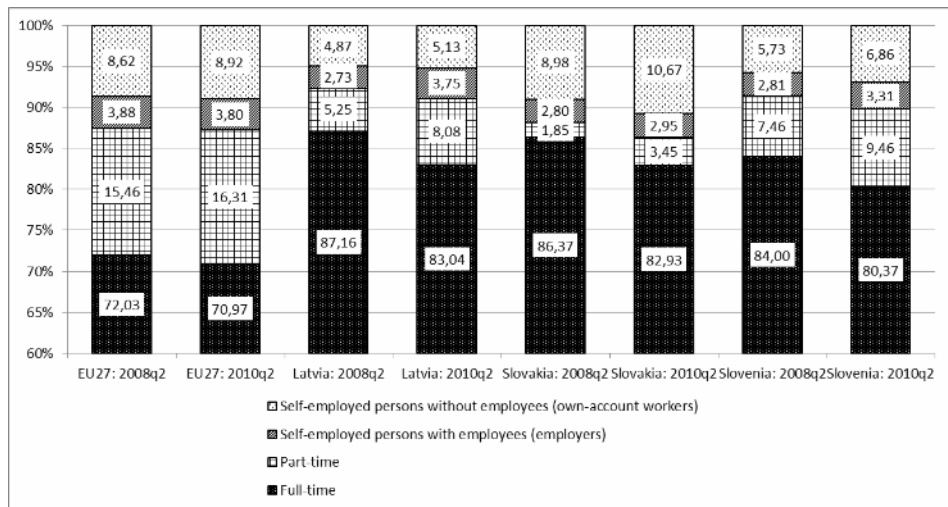
It is the usage of ftypes of employment other than full-time employment contracts, usually part-time work and temporary work, which provides more flexibility to the employers.¹ Figure 2 below shows the employment structure and its change from the 2008 Q2 to 2010 Q2. In all the three countries the share of full-time employees decreased, most severely in Latvia. On the other hand, the rise of the part-time workers and self-employed persons increased. This increase was not big enough to compensate for the full-time employees loss and therefore the overall level of employment was lower in 2010 Q2 comparing to 2008 Q2 (see figure 1). Thus the change in the employment structure might have relieved the pressure on firms and further limited the fall of headcount employment.

Another adjustment took place in the form of assigning employees to non-productive tasks, that led to the decrease in hourly productivity. Since the abovementioned adjustment would occur within the companies, there is little comparative data available. Figure 3 presents an annual percentage change in the labour productivity. Until 2007, the labour productivity was rising every year, mostly in Latvia, slightly less in Slovakia and Slovenia and considerably less at the EU27 level. During 2008 the labour productivity increased further in Slovakia and remained

¹ On top of the part-time work and temporary work there are two other channels that should not be overlooked in post-communist countries. However, due to the low data availability, these are reviewed out of the main text. Based on newspaper articles and political statements, it is clear that there were two major channels that employers used extensively in order to avoid full-time contracts. These are agency work and so-called “false self-employment.” An option which had experienced relatively high popularity among employers, agency work, has fallen victim among the first with the crisis worsening the pressures. The reason is that agency work is usually a very flexible type of employment from the company’s point of view. Despite a great deal of newspaper articles there are not reliable data available to prove the trend in laying-off the agency workers on the first place. However, ILO report concluded, among others, that “agency-placed workers have fulfilled a pressure-valve role, protecting “core” work forces from the initial consequences of the economic crisis” (ILO 2009: 35). Another phenomenon occurred in several countries, where major companies pushed their employees into self-employment arrangements and contractor-type of relationship. This allowed to avoid paying social insurance contributions and thus became much cheaper form of employment. This is especially a problem in construction, as Harvey points out (2001).

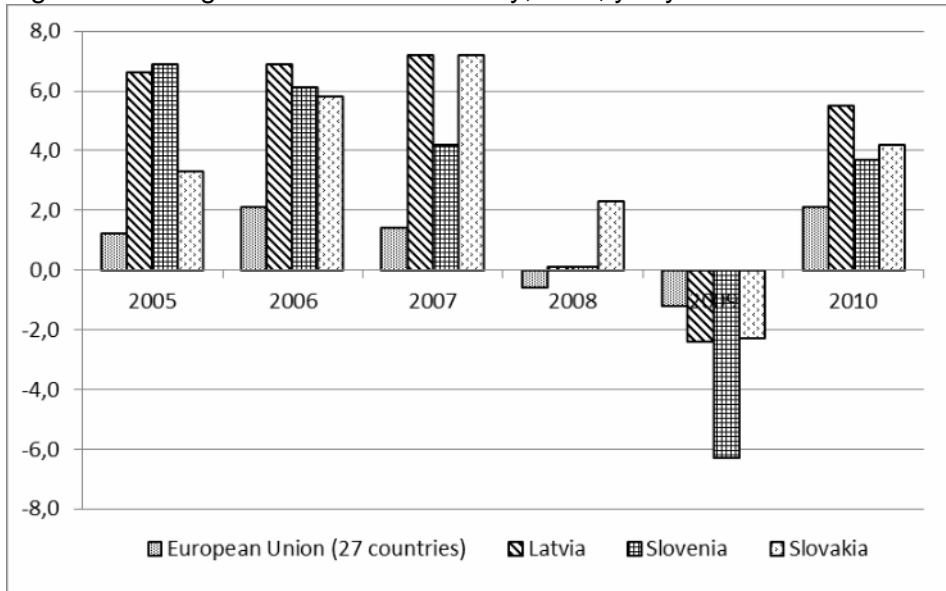
stable in Slovenia and Latvia. Data for 2009 show a further decrease in the labour productivity, again mostly in Slovenia. This indicates that shifting employees from productive to unproductive activities was used to maintain the headcount employment rates despite the economic problems that companies encountered. In 2010 the labour productivity increased in all three countries, however, the least so in Slovenia. This indicates that the institutions such as training programmes were the most effective in Slovenia.

Figure 2: Change of the Employment Structure, from 2008q2 to 2010q2



Source: European Commission, LFS

Figure 3: Change of Labour Productivity, in %, y-o-y



Source: European Commission, Ameco

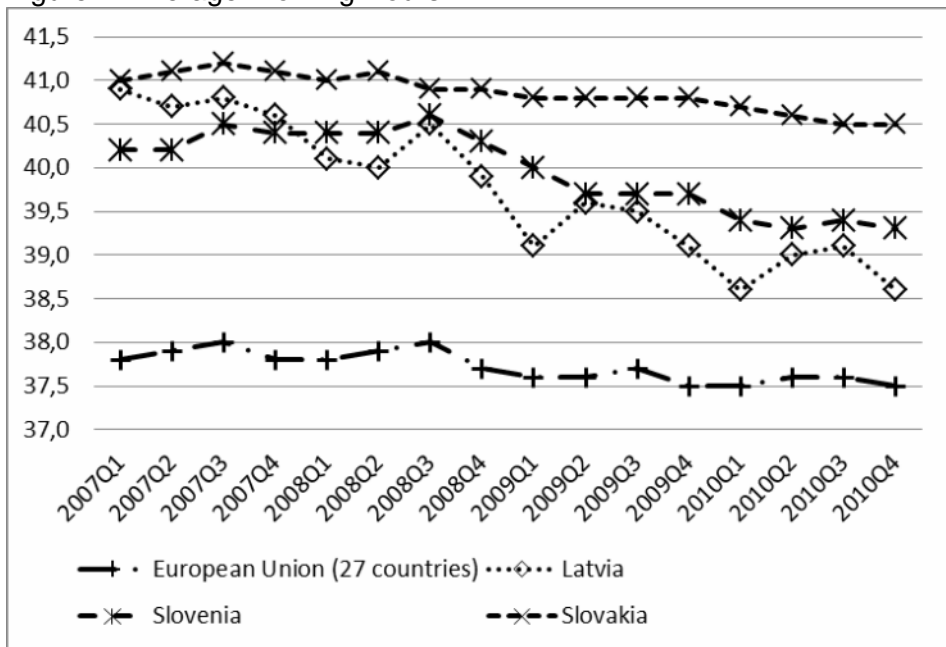
Adjustments in the working hours operated as another buffer. According to the European Commission report (EC 2010a), the introduction of the short-time working (STW) schemes increased internal flexibility, especially in a state with a low external flexibility. Calavrezo et al (2009) confirmed in their study that the introduction of the STW schemes led firms to decrease average working hours.

Latvia, Slovakia and Slovenia did not have any experience with similar provisions before the crisis. The newly introduced STW schemes differed among the countries. Latvian state support was directed exclusively towards private owned companies under the conditions that working time was reduced due to the economic crisis and a new workload was less than 20 hours a week. The so-called “contribution to support maintenance of workplace” was introduced in Slovakia. Employers that reduced the working hours but still continued to pay employees more than 60% of their salary were entitled to the contribution that covered the social insurance or payroll taxes. In addition, “flexi-accounts” were introduced as a temporary measure. Upon agreement with trade unions the employer may have reduced the working hours while economic difficulties occur and keep paying the basic wage. Subsequently, when the economic obstacles are removed, an employee might be asked to work overtimes with no extra compensation. In Slovenia, two similar schemes were introduced for subsidizing workers’ salaries with reduced working hours. Firms using

the subsidy had to pay full social security contributions for the workers and were forbidden to pay management bonuses. This indicates that the country with the supposedly highest external flexibility (Latvia) introduced only minimalist provisions of the STWs. Moreover, application of the STW measures had to be agreed on by the unions in both Slovakia and Slovenia, which is again in line with the VoC expectation. This suggests again that the institutional setting has its influence on the adjustment policies.

No comparable data is available to compare how many people and/or companies have been involved in the SWT schemes so far and how many workplaces were saved. The development of an indirect measure, the average working hours per week, is shown in Figure 4. Latvia experienced the relatively biggest negative change in the average working hours. A peak-to-bottom difference is 2.3 hours in Latvia, 0.7 hours in Slovakia and 1.3 hours in Slovenia, showing that the largest adjustment occurred in Latvia. This indicates both the stronger external pressures for such an adjustment and stronger use of institutions that allowed thereof. A smaller adjustment of working hours in the other two countries might have been caused by companies' preference for other measures such as non-standard types of contracts, and of course by a smaller external economic pressure.

Figure 4: Average Working Hours



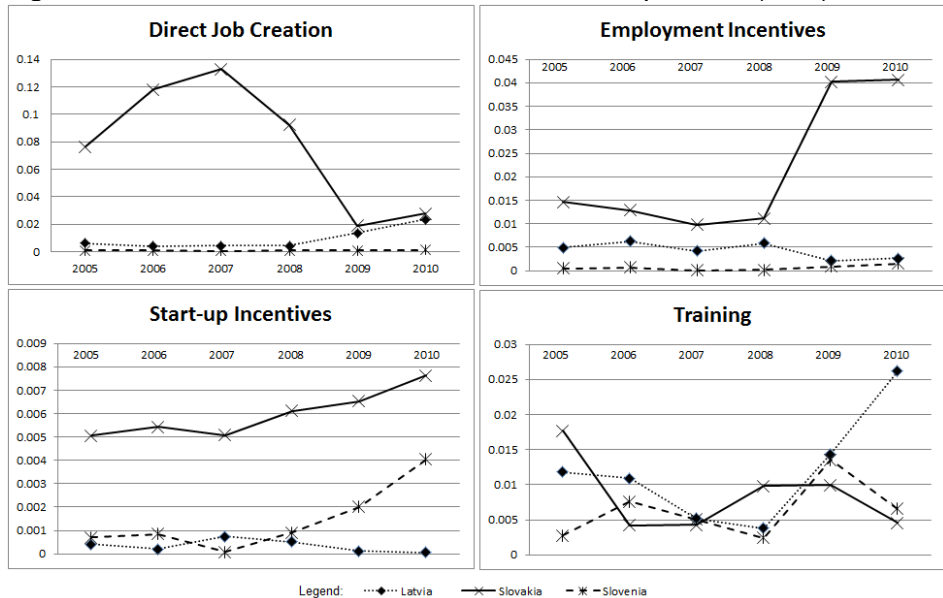
Source: European Commission, Ameco

Employment to Unemployment Institutional Buffers

During the 1990s the unemployment was exceptionally high in Latvia and Slovakia and the rate of unemployment kept double digits almost the whole time, contrary to Slovenia. Latvia achieved a single digit unemployment rate in the mid-2000s while Slovakia did so only in the run-up to the crisis (figures not shown). The institutional buffers between the employment and the unemployment consist mainly of the active labour market policies. The reason is that many of the programmes are not compatible with the official unemployed status and thus individuals in any ALMP programme are not counted as unemployed. Since these programmes are designed differently across the national states, it is not easy to compare their effect internationally. Eurostat provides some comparable data based on broad categories of services, subsidies and out-of-work income support. Data show an upward trend in the number of people using different ALMPs (figures not shown) until 2009. Since there is no data available for all the categories of the ALMPs, and some of the policies were introduced in Latvia only during the crisis, having been implemented for a longer time in Slovakia or Slovenia, it is not possible to compare the development in all the categories.

Figure 5 below shows the ratio of persons in the selected ALMPs to the active population. The Latvian training scheme was able to increase the integration of people in the training programs from about 1,500 in 2008 to almost 10,000 in 2010. In Slovakia the increase in the same reference period was roughly 400. Slovenia experienced a rise in the number of training schemes participants from about 3,400 to 9,500. Taking into account the labour market size, Latvia had the strongest institutional buffer in the form of training programs with Slovenia being only slightly behind. On the other hand, Slovak labour market policies focused more heavily on the financial support of the existing employment. The number of people receiving the employment incentives was the highest in Slovakia, in both relative and absolute terms. Slovakia also provided the start-up incentives to the most people.

Figure 5: Ratio of Persons in ALMPs to Active Population (in %)



Source: European Commission, LFS

This and the previous section show that in Slovenia the most successful institutions (in terms of buffering the crisis impact) were those taking place within companies and requiring cooperative industrial relations: assigning workers to non-productive activities and partly the STWs. On the other hand, Latvia's adjustment proved to be more effective out of the firms' environment: mostly government training programmes and, to a certain extent, start-up incentives (and international emigration, discussed in the next section).

Discussion: Adjustment Mechanisms and VoC

The empirical analysis identified a fistful of adjustment mechanisms functioning in the selected countries. However, some of the measures were used more frequently in one country than in the others. This section discusses the varying use of adjustment measures and suggests a classification that seems to emerge. Latvia experienced the most severe GDP fall within the EU. In absolute numbers; the level of un/employment was fluctuating more than in Slovakia and Slovenia. However, in relation to the GDP fall Latvia outperformed other countries. Adjustment channels mainly took form of shortened working hours in the public sector and government sponsored training programmes.

Regarding the elasticity of the relationship between the economic output and un/employment, Slovenia ranked relatively high in cushioning the

crisis impact. However, the buffering institutions were different from those in Latvia. While in Latvia the buffers were driven mostly by forces outside firms (government training schemes, working-hours adjustments, outward migration), Slovenia opted for the solution requiring intra-firm coordination (short-time working schemes, employment subsidies and early retirements)¹.

As the regression analysis showed, Slovakia performed relatively poorly in cushioning the effects of the crisis on the socio-economic outcomes. In contrast, for Slovenia and Latvia we cannot conclude that there were either market-driven or strategically coordinated institutions prevailing. Clearly, the government relied on providing financial means for sustaining the existing jobs and (self-) employment incentives (figure 5).

This paper explored the measures taken and the frequency of their use in the three countries. Two lines emerged along which the adjustment measures could be divided. Firstly, we observed that the adjustments took place either within the firm (measures as STWs or flexi-accounts preventing the loss of employment) or outside the firm (training programmes, start-up incentives or migration, all of which limits the increase of unemployment). Secondly, the measures were either in a financial form (subsidies for maintaining employment, direct job creation, start-up incentives, etc.) or in non-financial form (here belong training schemes, STWs, job-sharing and others).

When exploring the frequency of the specific measures' use in the three post-communist countries, there is also a pattern emerging. In Slovenia, the adjustment occurred dominantly within the firm and via non-financial mechanisms. Strategic coordination between employers and the state might have facilitated the use of STW schemes as well as subsidized training. Relatively strict EPL in combination with the developed welfare state provided protection for older workers, since unemployment in the category of workers age 55 and above remained relatively stable. Therefore, we suggest the country's variety of capitalism might influence the form of adjustment in case of the external economic shock.

In Slovakia, the prevailing adjustment type has a financial form and took place out of the firm. The country had previously attracted the majority

¹ We intended to include the early retirement as another buffer. However, the situation in the three countries is different to an extent that hampers international comparison. However, we know that early retirement was not an option in Latvia, while this was possible in Slovenia. In years 2008, 2009 and 2010 there were roughly 30-, 20- and 30- thousand new early retirees in Slovenia. Numbers are not available for Slovakia by Eurostat, possibly because of several changes of the legislation in this field.

of its investors and big employers by neo-liberal tax policies and looser employment protection legislation. However, the underlying institutions sustained to be closer to a strategic type of coordination, based on collective agreements and ALMPs oriented toward protection rather than prevention. Relatively generous welfare benefits did not create strong incentives for the employment alternatives such as training programmes or outward migration. Moreover, many newspaper articles indicate that Slovak workers were coming back to the country after losing their jobs abroad. Thus, the mixed institutional setting is in line with the lower LMI efficiency found by this study.

These observations could be possibly explained by the Varieties of Capitalism theory. It is in line with the VoC expectation that in Slovenia, supposedly the CME model, the adjustment would take a form of coordinated action that, in combination with a strong EPL, would focus on preventing workers from losing jobs. On the other hand, in Latvia, the hypothetical LME type, the most frequently used measures were out of the firm (possibly due to the lack of coordination mechanisms).

We argue that the welfare system also plays a role as a motivating factor in some of the adjustment channels. Arguably, the minimum level of the social protection could have contributed to the outward migration in Latvia. A minimal welfare state and a huge increase in unemployment put more pressure on the outward migration. Fluid labour markets would explain the high fluctuation of the employment and unemployment indicators. On the other hand, a developed welfare system might have an attracting effect for migration in Slovakia and Slovenia. According to some authors, the welfare system is an integral part of the capitalist variety (Bohle and Greskovits 2007). Thus, it is possible to see links between the VoC explanations and crisis adjustment in this regard as well.

Conclusion

This paper investigated how labour market institutions softened the impact of the economic crisis on the un/employment in three selected post-communist EU countries. We have identified several institutions with the buffering effect, and have explained the extent to which they were used in different countries.

What we observed is that the labour market institutions and the intensity of the specific measures' usage interact so that varying degrees of institutional complementarity emerge. It was beyond the scope of this study to test whether the VoC developed in the individual states causes the form of adjustment. However, the observed variance in the

adjustment forms and its complementarity to the VoC typology suggests that there is a link between the two.

Testing the causal relationship between the VoC typology and the form of institutional adjustment, however, remains a task for future research. One of the limitations that presented itself in this research is the limited availability of comparable data for large-N cross-national research. Bearing this in mind, the small-N case studies seem to be the way to explain the institutional adjustment in further detail.

References:

- Arpaia, A., Curci, N., Meyermans, E., Peschner, J., Pierini, F. (2010, June): Short time working arrangements as response to cyclical fluctuations. *European Economy, Occasional Papers 64*, European Commission, pp.1-93. doi: 10.2765/53330
- Babos, P.: *Varieties of Capitalism in Central and Eastern Europe* (2010): Measuring the Coordination Index of a National Economy. *SEER Journal for Labour and Social Affairs in Eastern Europe*, Vol. 13, No. 4
- Bahna, M. (2008): Predictions of Migration from the New Member States after Their Accession into the European Union: Successes and Failures. *International Migration Review*, Vol. 42, No. 4, pp. 844-860. DOI: 10.1111/j.1747-7379.2008.00149.x
- Bohle, D., Greskovits, B. (2007, May): Neoliberalism, Embedded Neoliberalism and Neocorporatism: Towards Transnational Capitalism in Central-Eastern Europe. *West European Politics*, Vol. 30, No. 3, pp. 443 – 466, DOI: 10.1080/01402380701276287
- Calavrezo, O., Duhautios, R. and Walkowiak, E. (2009): "The Short-Term Compensation Program in France: An Efficient Measure against Redundancies?", Working paper no. 114,
- Divinský, B. (2007): Labor market – migration nexus in Slovakia: time to act in a comprehensive way. *International Organization for Migration*, Bratislava, , pp. 1-229. ISBN 978-80-89158-17-1
- Égert, B., Drine, I., Lommatzsch, K., Rault, Ch. (2003): The Balassa-Samuelson effect in Central and Eastern Europe: myth or reality? *Journal of Comparative Economics*, Vol 31, No. 3, pp. 552-572. DOI:10.1016/S0147-5967(03)00051-9
- Gal, Zs. (2009): Immigration to advanced countries - five main approaches. *Panorama of global security environment*, Bratislava: CENAA, 2009, pp.. 607-624
- Hall, P.A., Soskice, D.W. (2001): *Varieties of Capitalism: The Institutional Foundation of Comparative Advantage*. Oxford University Press, New York

- Harvey, M. (2001): Undermining construction The corrosive effects of false self-employment. Institute of Employment Rights, London, pp. 1-56
- Hijzen, A. and D. Venn (2011), "The Role of Short-Time Work Schemes during the 2008-09 Recession", *OECD Social, Employment and Migration Working Papers*, No. 115, OECD Publishing. DOI: 10.1787/5kgkd0bbwvxp-en
- Kaczmarczyk, P., Okolski, M. (2005): International Migration in Central and Eastern Europe – Current and Future Trends. United Nations, pp. 1-31. Available on 13 May 2012 at: http://www.un.org/esa/population/meetings/ittmigdev2005/P12_Kaczmarczyk%26Okolski.pdf
- Knell, Mark; Srohlec, Martin.(2007) Diverging Pathways in Central and Eastern Europe. In Lane, David; Myant, Martin (Eds.): *Varieties of Capitalism in Post-Communist Countries* (New York: Palgrave Macmillan), pp. 40-62. DOI: 10.1057/9780230627574
- Lane, D., Myant, M. (2007): *Varieties of Capitalism in Post-Communist Countries*. Palgrave – MacMillan, DOI: 10.1057/9780230627574
- Leschke, J., Watt, A. (2010, April): How do institutions affect the labour market adjustment to the economic crisis in different EU countries? Working Paper, European Trade Union Institute, 2010. pp. 1-66
- Mansor, A., Quillin, B. (2007): *Migration and Remittances: Eastern Europe and the Former Soviet Union*. World Bank, pp. 1-208, ISBN 978-0-8213-6233-4. DOI: 10.1596/978-0-8213-6233-4
- Myant, M., Drahokoupil, J. (2011): *Transition Economies: Political Economy in Russia, Eastern Europe, and Central Asia*. Wiley Publishing, pp. 1-391
- OECD Employment Outlook 2010 (2010): *Moving Beyond the Jobs Crisis*. OECD, pp. 1-310. ISBN 978-92-64-08614-2. DOI : 10.1787/empl_outlook-2010-en
- Purfield, C., Rosenberg, C. B. (2010, September): Adjustment under a Currency Peg: Estonia, Latvia and Lithuania during the Global Financial Crisis 2008-09. IMF Working Paper WP/10/213.
- Rose, A. K., Spiegel, M. M. (2009, September), : Cross-Country Causes and Consequences of the 2008 Crisis: International Linkages and American Exposure. NBER Working Paper 15358, DOI: 10.3386/w15358
- Skribans, V. (2009): Influence of Labour Migration On Latvia's Labour Market. MPRA Paper no. 19253. Downloaded on June 25th 2011, available at: <http://mpira.ub.uni-muenchen.de/19253/>
- Wood, S. (2001): *Business, Government and Patterns of Labor Market Policy in Britain and the Federal Republic of Germany*. IN: Hall, P.A., Soskice, D.W.: *Varieties of Capitalism: The Institutional Foundation of Comparative Advantage*. Oxford University Press, New York, 2001

World Bank: Doing Business 2011 (2010): Making a Difference for Entrepreneurs. Washington, USA, pp. 1-267. ISBN: 978-0-8213-7960-8

Appendix 1: Correlations Between Changes in Economic Output, Employment (both Headcount and Hours) and Unemployment

| Change in: | OUTPUT | EMPLOYMENT | TOTAL WH | UNEMPLOYMENT |
|--------------|---------|------------|----------|--------------|
| OUTPUT | 1 | -,826** | -,817** | ,756** |
| EMPLOYMENT | -,826** | 1 | ,985** | -,813** |
| TOTAL WH | -,817** | ,985** | 1 | -,827** |
| UNEMPLOYMENT | ,756** | -,813** | -,827** | 1 |

** . Correlation is significant at the 0.01 level (2-tailed).

Appendix 2: Residual values from regression analysis

| Country | Output vs. Unemployment | Output vs. Employment | Output vs. Working Hours | Employment vs. Unemployment |
|---------|-------------------------|-----------------------|--------------------------|-----------------------------|
| AT | 0,1653 | 0,510931 | -0,44554 | 0,700887 |
| BE | -1,23555 | 0,237585 | 0,635451 | 1,921155 |
| BG | 0,24669 | -5,05436 | -4,36847 | -5,60121 |
| CY | -5,44851 | 0,126623 | 0,692964 | 5,869009 |
| CZ | -2,41546 | -1,54634 | -1,78772 | 0,9988 |
| DE | 0,936872 | 0,265057 | 1,162296 | -0,15567 |
| DK | -4,22941 | -0,96583 | -4,07055 | 3,057476 |
| EE | -3,57853 | 0,411978 | 0,506435 | 2,573619 |
| ES | -1,89429 | -6,15527 | -5,82348 | -4,68281 |
| EU27 | -0,27297 | -0,75438 | -0,68605 | -0,26855 |
| FI | 3,662689 | 1,702237 | 1,898755 | -1,80843 |
| FR | -1,09911 | -0,74681 | -0,42285 | 0,70373 |
| GR | 1,029207 | 0,927 | 1,564162 | -0,03251 |
| HU | 3,438513 | 3,300591 | 3,408109 | 0,054422 |
| IE | 1,525463 | -2,52252 | -2,62562 | -4,73709 |
| IT | 2,647191 | 1,032943 | 0,914981 | -1,36487 |
| LT | -0,26242 | 3,751663 | 4,301112 | 2,817383 |
| LV | 11,91745 | 5,58585 | 6,269374 | -7,60983 |
| MT | -0,99514 | 2,938961 | 3,254064 | 4,585685 |
| NL | -1,20961 | -1,5892 | -1,38994 | -0,18957 |
| PL | -8,14944 | -4,9015 | -5,86796 | 3,757142 |
| PT | -2,00028 | -4,47206 | -3,72927 | -2,41595 |
| RO | 7,108083 | 7,667128 | 7,530264 | 0,972153 |
| SE | -1,56293 | -1,20627 | -0,1336 | 0,617905 |
| SI | 3,860505 | 4,966 | 3,470076 | 1,246848 |
| SK | -2,98142 | -4,59948 | -4,69364 | -1,52599 |
| UK | 0,7971 | 1,089489 | 0,436632 | 0,516263 |