

EXECUTIVE SUMMARY

Serbia has achieved high rates of economic growth since 2000, and its transition to a competitive market economy is well underway. But precious time was lost in the 1990s, with the result that GDP per capita is now among the lowest in Europe. The country suffers from a large labour surplus, and the restructuring of the economy is still in a phase when many jobs are bound to disappear at the same time as new ones are created.

In this situation, it is crucial to establish the best possible conditions for creating more new jobs on market conditions. Key policy objectives must be to foster greater flexibility in employment, a consistent and equitable application of labour law and a transparent job market. The on-going transformation of the National Employment Service should be completed with a further shift of emphasis from administrative register functions towards counselling and job-search assistance to the unemployed.

This report first reviews the labour market trends in the years after 2000 and the principal challenges to labour market policy. It then considers the available policy instruments, beginning with the institutional framework including industrial relations, labour law and issues about compliance and enforcement. This is followed by an assessment of the role of the public employment service and its different programmes.

In all considered policy areas, Serbian policy makers have drawn significant lessons from experience in OECD economies and other transition countries. However, it is argued below that Serbia, in order to catch up economically, should aim to make its labour market *more* flexible than those of most EU countries.

An annex takes a longer historical perspective. It considers the experience of the former Yugoslavia's peculiar labour market model and draws some policy lessons from the ways in which the different successor states have dealt with this legacy.

Major employment reductions have occurred

Chapter 1 observes that employment declined in every year from 2001 through 2006, followed by a small recovery in 2007. Over the period as a

whole, major employment reductions occurred in big enterprises and peasant farming, while net job creation was observed mainly in small non-farm family businesses. The survey-based unemployment rate peaked at almost 22% in 2005 and 2006. But it fell to just under 19% by October 2007, reflecting the combination of economic recovery and a shrinking labour force.

The working-age population is set to decline further as a result of population ageing and net emigration. However, Serbia still has large potential labour supplies because only about 50% of the working-age (15-64) population is employed. Employment rates are low by OECD standards for most demographic groups, especially youths, women and the elderly, although the situation is comparable in several countries in south-eastern Europe. Moreover, a significant but declining part of employment concerns subsistence farming and other low-productive forms of self-employment, which often are informal. In some part, the recent decline in total employment appears to reflect a growing reluctance among parts the population to accept the most low-paying types of work.

Disappointing employment growth in small firms

The economic transition has brought profound changes in the structure of the job market. Almost two-thirds of employment is now in the private sector, where labour turnover is on average much higher than in the public sector, and the average size of enterprises has declined significantly.

However, a worrying weakness in Serbia's recent labour market performance has been the anaemic growth of employment in new small firms. Non-farm self-employment still plays a modest role by international standards. The authorities have sought to facilitate business start-ups by streamlining administrative procedures, but international comparisons show that these are still relatively cumbersome. It should be a high priority for the authorities to remove these barriers and make the public administration more helpful to small firms.

Chapter 2 finds that Serbia's formal labour market regulations are broadly appropriate and in accordance with international standards. But this observation has limited consequence as long as *implementation* is weak. For the same reason, it can be difficult to determine to what extent various provisions in the law might in fact be too rigid if they were to be rigorously enforced in future.

Serbia needs more flexible EPL than most EU countries have

Numerous rules in Serbia's Labour Law have been aligned with EU practice, which is relatively stringent on certain points such as employment protection legislation (EPL). As a result, EPL is now less flexible in Serbia than in most of the other transition economies, and much less flexible than in, for example, the English-speaking OECD countries. However, international experience shows that low and medium-income countries need more flexible EPL rules than those typically found in continental western Europe. Serbia should simplify its rules about dismissing workers and remove unnecessary restrictions on the use of temporary job contracts.

The Labour Law cites collective bargaining as the preferred method for wage-setting, and it stipulates strict rules for recognition of trade unions and employer associations. But in reality, trade unions and collective agreements have little impact outside the public sector and large firms. Where unions do not exist, the law permits employers to decide on wages and working conditions.

Social dialogue should involve potential winners and losers

Given Serbia's history and the difficulty of its economic and labour market reforms, policy making must involve an element of social dialogue. For this purpose, tripartite Councils have been established at the national and regional levels, in which the existing labour market associations are represented. However, in policy matters of great importance for economic development, the social dialogue remains insufficient if it does not encompass both growing and declining segments of the labour market. In order to achieve this, it appears important to consider possible ways of giving voice to groups that are not well represented in the tripartite councils, as for example the workers of small firms. The range of participants in such discussions should be flexible and not necessarily linked with a status as collective-bargaining partner.

Strengthen tax enforcement and the labour inspectorate

Better enforcement is needed in several policy areas of relevance to employment, including labour law, social insurance, business and labour taxation, and occupational health and safety. The report identifies three types of compliance problems: *i*) many jobs are informal; *ii*) some formal enterprises are so low-productive that they cannot afford to fulfil their

legal obligations; and *iii*) some rules, such as those on working time, are widely disregarded even in profitable formal enterprises.

According to OECD experience, the most important instrument for formalising informal employment is usually the tax administration and its ability to promote good accounting standards. Enhanced tax enforcement should be coordinated with the on-going development of Serbia's official registers of enterprises and entrepreneurs, as well as with that of the social insurance administration. Enterprises should not be allowed to stay in business if they cannot fulfil their obligations. The remaining socially-owned firms, which on average have the worst record, should be privatised or liquidated as planned.

In order to fulfil its functions, the labour inspectorate needs more resources and stronger legal powers, for example in terms of its right to inspect various types of business and to decide about sanctions.

Client-oriented employment services

Chapter 3 is devoted to the modernisation of the National Employment Service (NES) and its programmes. These reforms are guided by national strategy documents that take account of international experience, reflecting Serbia's cooperation with the European Union and various countries. Several strategy papers emphasise the need to develop client-oriented services to job seekers and employers. In Serbia as elsewhere, varying views have been expressed about the need to increase spending on the more expensive types of active labour market programmes, especially training. With about 0.1% of GDP devoted to such programmes in 2007, their annual participant intake corresponded to barely 5% of the stock of registered unemployed persons.

To develop its main service functions, the NES needs to modernise the job-seeker and vacancy registers. These should concentrate on the *actual* information needs for job search and filling vacancies. An important step in this direction was taken in 2007, when the principles for registering clients as unemployed were changed and numerous persons not seeking jobs were eliminated from the register. Similarly, vacancy registers should focus on the job openings for which employers are actually seeking candidates.

Limited capacity for counselling justifies a focus on benefit recipients and motivated clients

Given a large stock of registered unemployed clients, and the likelihood of continued large inflows in the near future, the NES must prioritise. It recently introduced a system for profiling of clients, and individual employment plans are developed for those deemed most employable. Following current practice in many countries, unemployment benefit recipients are asked to sign mutual-obligations agreements with the employment service. However, only about 10% of the clients are eligible for such benefits, and even for them, the mutual obligations have questionable legal consequence because the benefit payments are in arrears (by four months in 2007).

According to the profiling outcomes in 2007, a majority of the registered unemployed were considered as employable only after participation in substantial active programmes (training or job subsidies), if at all. But despite a recent increase in programme spending, budgetary and efficiency considerations make it unrealistic to expect such expensive programmes to play more than a very marginal role in resolving Serbia's unemployment problem.

In this situation, the best use the NES can make of its limited budget is to concentrate on the basic employment service functions, especially filling vacancies, job-related individual counselling and related group activities. Existing self-service systems for job information, which are accessible to anyone, should be developed, while available resources for counselling and monitoring of individual job-search efforts should target benefit recipients and the most motivated among the other registered clients.