

COMPETITIVENESS IN THE NEXT DECADE

*Workforce Competitiveness
The cases of Macedonia and Kosovo*

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Global labor markets are routinely characterized in terms of “critical skills shortages.” Such shortages of skill in specific occupations can be documented in times of both economic expansion and contraction. Skills demand surveys reveal unmet needs not only in knowledge-intensive, research, design, and innovation positions, but also in high-skilled technical production positions. Most also cite the poor quality of preparation of even applicants for low-skill occupations.¹

Whatever the statistical realities, no one seems satisfied. Even in the United States, ranked number one in competitiveness by the Forum, dissatisfaction with education and with the preparation of and attitude among workers ranks in the top four or five challenges to competitiveness. The National Association of Manufacturers complains that “current workers do not have the knowledge and skills necessary for today’s high-tech manufacturing jobs” (Gillespie and Weems, 2008).

Technical skills by themselves are not sufficient. Interpersonal and other behavioral or “soft” skills also influence employers’ hiring decisions. Initiative, perseverance, time management skills, teamwork skills, being able to present oneself and one’s company, empathy, the ability to provide service, problem-solving skills, and flexibility are also in high demand (Teaching and Learning Research Programme, 2008).

A recent report on education, globalization, and the knowledge economy conducted in Britain suggests that OECD countries are not alone in acknowledging such skills gaps and preparing education and training strategies to address them. Newly industrializing powerhouses such as India and China are doing likewise (TLRP, 2008). To address the “global skills race,” the United Kingdom seeks to provide access to both a university education and to lifelong learning opportunities for a larger proportion of its workforce. TLRP reports that skill formation and human resource strategies are becoming increasingly important to corporate competitive advantage.

As a result of shortages in the largest industrial markets, demand for skills is relocating to tap emerging technical skills pools found elsewhere. Multinational companies are increasingly facilitating the creation of centers of innovation in various localities, from Bangalore to Casablanca to Kyiv to Tel Aviv to St. Petersburg to Shenzhen, wherever the talent to innovate and design can be found. The availability of skills in foreign markets is one of the determining factors of these companies’ foreign investment decisions, TLRP notes.

¹ Much of this analysis is drawn from workforce assessments carried out in 2009 in Macedonia and Kosovo. Principal authors are Erik Butler (assessment lead in both countries), with Lynn Salinger (Kosovo), Clare Ignatowski (Macedonia), Denise Lamaute (Kosovo and Macedonia), Chris Murray (Kosovo), Jovan Madjovski (Macedonia), and Zoran Velkovski (Macedonia). Full reports are available from the respective USAID Missions in Macedonia and Kosovo.

Two recent workforce development assessments in the Europe and Eurasian region – in Macedonia (March 2009) and in Kosovo (May 2009) -- illustrate the relevance of these points and others to the region. Here are a few headlines:

Labor Market Policies and Practices have economic impacts: Labor market policies relating to wages, social protection costs, labor market regulations, and workforce development greatly influence the level and extent of job creation and employment growth in a country. It is often a difficult challenge for governments to institute policies that enhance the current and future supply and demand for labor when a variety of other compelling needs and options such as consideration of macroeconomic policies, demographics, transportation, national security, and housing, just to name a few, compete for resources. Ideally, the combination of labor market policies coupled with other influencing policies should promote a healthy environment for businesses and workers. The rewards for a country are enormous when the policy mix is right. Conversely, they will likely be anemic when the policies ignore market forces or are slow to be adopted and implemented. With an erratic or slow response to today's and tomorrow's labor market needs and challenges, workers, households, and the private sector all pay the price.

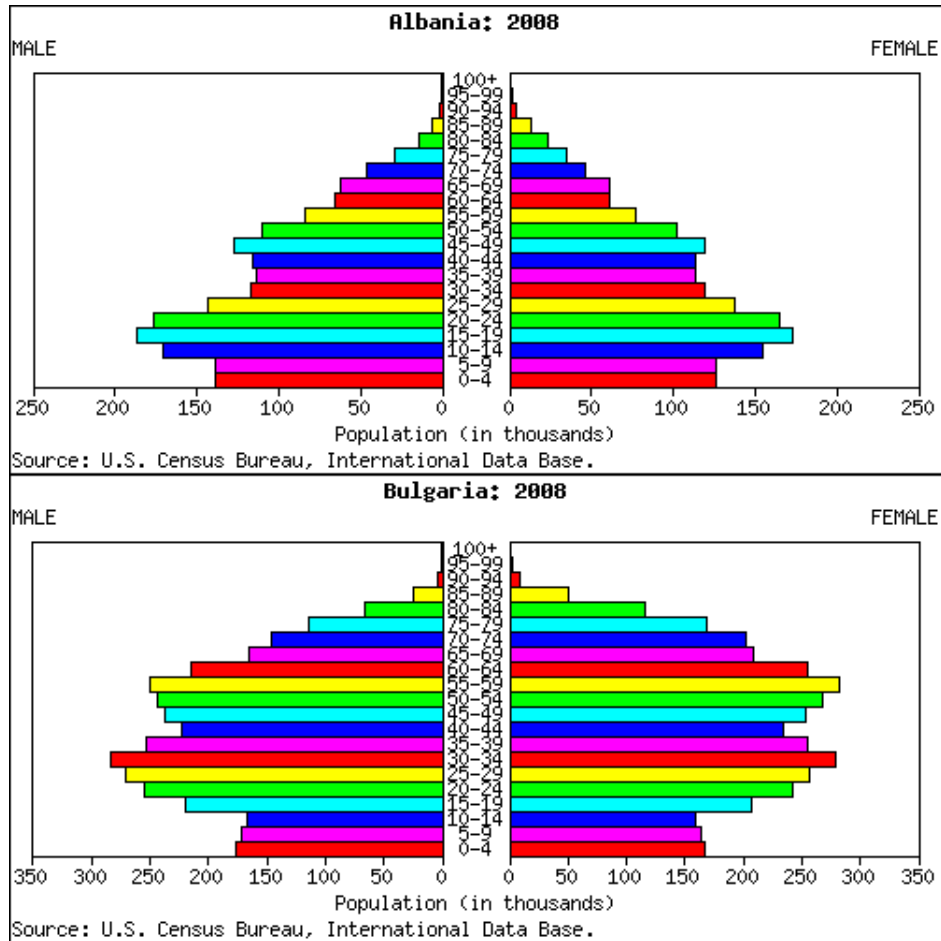
The cost of labor can be both a cause and effect of economic growth: For example, labor in Macedonia is among the most expensive in the region, more expensive than labor in neighboring EU member Bulgaria². This justifies the government's decision to cut the taxes on salaries, and thus make labor cheaper for foreign investors and hiring illegal workers less attractive for domestic employers. The recent cuts are expected to slightly reduce the country's informal economy, which is estimated to be 40 percent of the formal economy. In addition to the direct labor costs of hiring workers, firms also have to bear the costs of complying with regulations in hiring and firing workers. Within the West Balkans, Croatia and Macedonia have the strictest employment protection legislation, followed by Bosnia and Herzegovina and Serbia. For Bosnia and Herzegovina, this rigidity, along with its relatively high wages, creates disincentives for investment and job creation. This is also true for Macedonia. Its relatively high employment rigidity index combines with wages that, on several measures, are second only to those in Bosnia and Herzegovina.

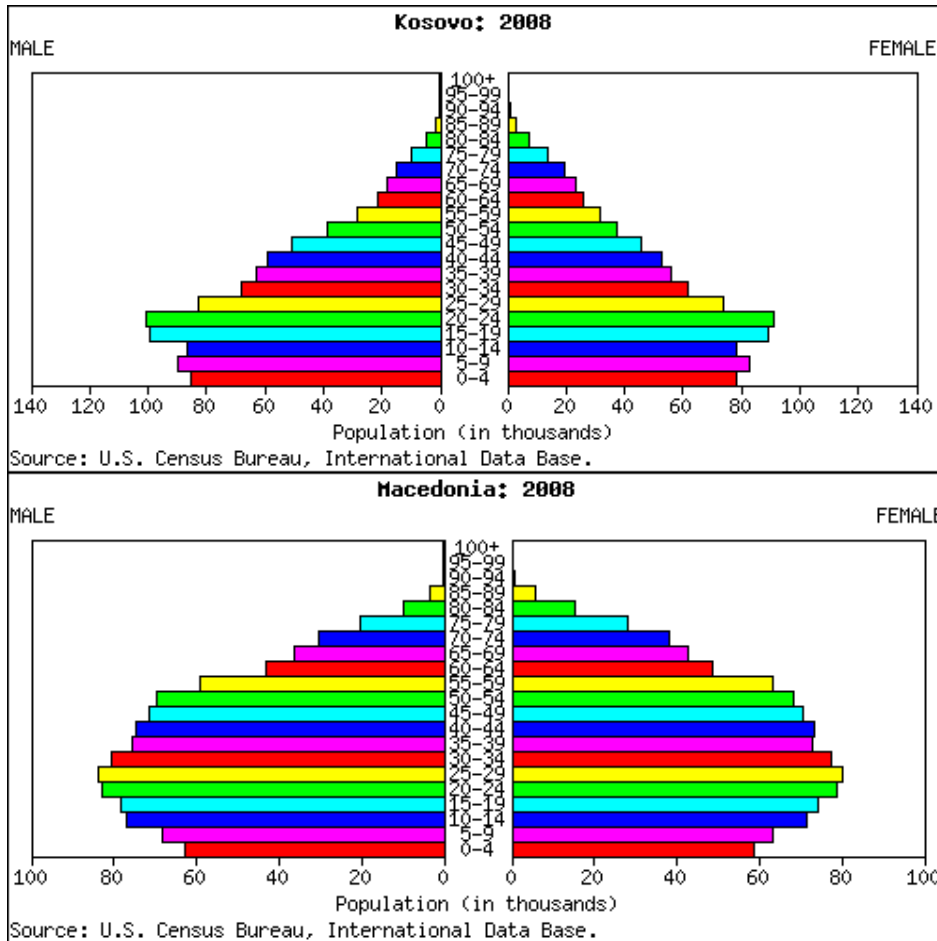
Age Matters: A burgeoning population of youth and young adults is Kosovo's biggest workforce challenge, and is also potentially its most significant competitive asset. While less extreme in Macedonia, the relative youthfulness of its out-of-school and out-of-work population presents a similar dilemma. By comparison, Bulgaria, which has a similar "youth bulge" shows another significant bulge in the 45-59 year-old cohort, which suggests a

² World Bank. "Western Balkans Integration and EU: An Agenda for Trade and Growth." Ed. Sanjay Kathuria. 2008

challenge now or soon to make an adjustment to an aging workforce. Albania looks more like Kosovo, with only a slightly less 'pyramid' shape, tilted towards the 15-24 population.

Figure 1: Demographic Distribution by Age and Gender, 2008





Poverty is both symptom and cause of competitiveness failures: poverty is a significant factor in the region, nowhere more so than in Kosovo, Europe's poorest nation. In 2005-06, 45% of the population was estimated to be living under the poverty line, of which 15% were living in extreme poverty, unable to afford basic nutritional requirements (World Bank, 2007). Poverty is overwhelmingly a rural phenomenon, with more than two-thirds of the poor living in rural areas. Poverty is lowest in Cjilani (southeastern Kosovo) and highest in Mitrovica (in northern Kosovo, where tensions continue with Serbia and Kosovo Serbs), as seen in **Error! Reference source not found.** The higher incidence of poverty in rural areas creates increased incentives to leave in search of work elsewhere. Although Kosovo was previously a predominantly rural country, informants suggest that with rural-to-urban migration the population is now balanced 50-50 between urban and rural residents. In other states in the region, this rural-to-urban shift has taken place sooner, and the poverty rate in urban areas approaches rural rates. This matter is compounded by land-ownership traditions, wherein a subsistence family farm – able only to sustain a single family – is passed to a single child (often eldest son), and the remainder of the children find it preferable to move – in the changing economy, mostly to urban environments.

Figure 2: Comparison of poverty in selected countries in the region (source: CIA Factbook)

<u>Kosovo</u>	\$2,300*	\$5.00**
<u>Albania</u>	\$6,400	\$23.07**
<u>Bosnia and Herzegovina</u>	\$6,600	\$30.49**
<u>Serbia</u>	\$8,200	\$83.14
<u>Macedonia</u>	\$9,200	\$18.97**
<u>Montenegro</u>	\$10,600	\$7.16
<u>Croatia</u>	\$16,900	\$75.93

2008 Per Capita / GDP (expressed as Purchasing Power Parity) in billions

* *Estimate*

** *Large informal sector*

Emigration and remittances offset poverty to some extent, but complicate the labor market picture: For example, despite Kosovo’s rapid population growth rate, USAID’s employment and labor market profile suggests that the Kosovo labor force is shrinking by 2.5% per year, due to emigration (USAID, 2009). Migration out of the rural areas, either to urban areas in Kosovo or abroad, has been a key safety valve (UNICEF, 2008).³ The remittances generated by such overseas work have been an important source of income for the families who send members abroad, fueling immediate consumption and investment (especially in housing construction). The World Bank estimated that about 1 in 5 Kosovo residents has at least one family member abroad (World Bank, 2007). Emigration is a clear livelihood improvement strategy, as the incidence of remittances results in poverty rates that are 20 points lower as compared with households that do not receive remittances. In addition, households who receive income transfers from abroad are able to subsist more easily in the face of high domestic unemployment rates – and may also therefore require a higher wage (what economists call a “reservation wage”) to bring them out of inactivity and into the workforce.

³ According to the authors, “Kosovo stands no chance to create enough jobs to absorb the unemployed” (UNICEF 2008, 9). This is true in the short- to medium-run. Domi (2008) estimates that a sustained economic growth rate of 7.3% is needed over the next ten years simply to halve present unemployment rates.

The so-called “gray market” inhibits developing a formal workforce system. In the words of one informant in Macedonia: “Until many more people are working in the formal sector – real jobs with regular schedules and higher wages that carry benefits and require payment of taxes – we will not have a modern economy.”

A large grey economy operates to reduce the efficiency of the labor market. In such a situation, the wage costs depend on how easily a business can conceal its activities. The loss of tax revenues from informal activities causes low quality public services, increases susceptibility to public corruption by depressing public wages, and exerts pressure to increase the tax burden on the formal sector.

The Republic of Macedonia, like most formerly planned economies, has been going through a difficult period of transition which has resulted in low participation in the labor market, high unemployment rates, and increasing levels of poverty. Despite significant progress in macroeconomic stabilization and the process of privatization, which is almost complete, job creation has been limited. As a result, many people end up working in the informal sector, which has acted as a temporary buffer.

With the grey economy estimated between one-third and one-half of the formal economy⁴, the government of the Republic of Macedonia has identified this issue as one of the areas that requires immediate and substantial actions. Some of the planned government activities to address this issue are: tax reductions on certain activities and products, simplification of administrative procedures for obtaining different licenses and permits, and increasing the efficiency of the Public Revenue Administration, among other measures.

Projecting labor supply and demand is an uneven art throughout the region. The *supply side data* -- while uneven and incomplete -- are nonetheless available on both countries, and probably useful for policymaking. Analysis of the unemployment problem in both Kosovo and Macedonia show a similar pattern:

- **Long-term joblessness** is the most dominant feature – 84.9 percent of the registered unemployed in Macedonia in 2007 had been without work for one year or more.
- **Many of the unemployed are uneducated** or have incomplete primary or secondary education – the registered unemployment rate in 2007 of workers without education and/or unqualified or semi-qualified was 46.1 percent.

⁴ A comparative study conducted by Prof. Friedrich Schneider of the Linz University⁴ has estimated the size of the Macedonian grey economy in 2000 and 2001 at 45.1 percent of the country’s GDP. According to this author, this represents a significant increase compared to the period of 1990-1993, for which the estimate was 35.6 percent.

- **The employment rate for young people is low** –the employment rate for workers aged 18-24 is only 15.2 percent.
- In 2007, **activity and employment rates for females were very low** as compared to EU averages -- 32.2 percent and 50.4 percent, respectively, for females aged 18-64.

On the other hand, *demand side data* are harder to come by, and largely anecdotal. There are some promising developments, however. In Macedonia, with EU support, the Center for Labor Market Analysis within the National Employment Service Agency (Ministry of Labor and Social Policy) has formed and developed a system of ongoing “demand” surveys of the labor market. The Center developed the methodology in 2006 – adapting a Swedish labor market survey – and fielded the first survey with 1600 firms in 2007. The first survey is complete, the first report published and distributed to “the relevant agencies in government”, according to the director of the Center. The survey has fifteen questions – several on business “demographics” – and is administered by face-to-face interviews.

This survey holds real promise for beginning to make policy and create initiatives according to actual information from firms. While the survey technology is quite good, and administration appears thorough, there seems to be little observable connection between its findings and policies or practices of governmental agencies. Apparently some USAID-sponsored competitiveness projects in the region are undertaking similar efforts, though they are sector-specific, and not “economy-wide” in any country. The Serbian and Kosovo competitiveness projects are both developing “skills gap analysis” procedures to help in targeting workforce development efforts in selected sectors.

Where demand for labor is weak, the supply also lags behind: Public and private sector alike believe that there is a “gap” between supply and demand, and the data seem to support this conclusion. Despite continuing GDP growth in both Macedonia and Kosovo, for example, there are, simply put, not enough jobs in their economies to absorb the supply of available and future workers. This tends to inhibit needed reforms in education. The education system and the market economy are two separate worlds in too many economies. However,

Education clearly matters: According to the nearly unanimous opinion of employers interviewed in the two assessments, few candidates for jobs possessed adequate levels of technical skills for the jobs presented; all needed further company training. While most had acceptable levels of cognitive ability (i.e., reading and language ability), there were several descriptive complaints about lack of quantitative ability, even mastery of the basic arithmetic functions.

In Macedonia, nearly half of the entire population over 15 years of age did not complete primary school; in Kosovo it is still higher. Dropout rates in secondary education in both countries suggest a steep drop-off during the adolescent years, with a small proportion of

students reaching and then completing higher (tertiary) education. While both countries have mandatory education laws, the pipeline between primary education and employment is leaky indeed.

There is universal criticism of the lack of practical education and soft skills: Echoing criticism heard in a 2007 workforce assessment in Georgia, and in reports from nearly every country in the region, employers fault both secondary and tertiary (higher) education for emphasizing theory over practice, and for teaching both with outmoded and out-of-date technologies. In a related but different complaint, employers observe an absence of “soft skills” in their applicants for employment: interviewing, possession of an adequate CV, facility with working in teams, ability to communicate with supervisors and colleagues, and so on. Here is a summary, drawn from the Kosovo assessment, but with very similar results to the Macedonia interviews and focus groups:

While the assessment team did not conduct a wide, systematic survey of the private sector, we did conduct interviews with a number of firms, inquiring about their experience in hiring, their opinions about the people who apply for work, and their experience (if any) with training providers, schools, and universities. The firms included several former socially-owned enterprises, light manufacturing, agro-processing, ICT or technically-oriented firms, and consulting firms. We asked similar questions of all. Despite their differences, we can summarize their feedback in a handful of points:

- All have done hiring in the last year, and nearly all hired university graduates only;
- The formerly socially-owned enterprises had all transitioned to private ownership, upgraded technology, and laid off significant percentages of the former workforce; they had hired few back, instead hiring selectively for technical specialties, and often from abroad through networks of foreign owners;
- Few candidates for jobs possessed adequate levels of technical skills for the jobs presented; all needed further company training;
- While most had acceptable levels of cognitive ability (i.e., reading and language ability), there were several descriptive complaints about lack of quantitative ability, even mastery of the basic arithmetic functions;
- Few exhibited any “soft skills” in interviewing, possession of an adequate CV, experience with teamwork, ability to communicate with supervisors and colleagues, and so on;
- All firms interviewed believed generally that secondary schools, and even universities (with a couple of notable exceptions among the private universities) were outmoded, and were preparing students for obsolete jobs;
- Some believed that their jobs were really too elementary for university graduates, and that well-prepared secondary students could succeed in them, but had never hired one;

Conclusion: thinking about practical measures: Clearly all countries in the greater Eastern Europe region are not the same: they vary by political tradition and status, by maturity of the economy, by trade and investment patterns, by size, and by ethnic make-up. Yet there are common themes in the general topic of workforce development: similar demand-side criticisms about education as work preparation, about the quality and aims of vocational training, and about the readiness of students, the unemployed and even the current workforce to contribute in a modern economy.

There is no shortage of ideas for what to do to improve in this area. In both Macedonia and in Kosovo, the examples used most in this brief review, the workforce development assessment teams listened to and considered many suggestions and recommendations. Most had a kind of “face validity,” and seemed sensible; of course not all were feasible for the kinds of investments being contemplated by USAID⁵. In both assessments, the teams grouped the options into five beneficiary or “target” categories:

- *Options for serving the presently unemployed*
- *Options for serving the presently employed but under-skilled*
- *Options for the preparation of future workers*
- *Options for policy improvement initiatives*
- *Options for capacity-building initiatives*

The teams then made recommendations about these ideas based upon several criteria:

- *Systemic importance, impact:* If it worked, what difference would it make?
- *Leverage:* Could USAID’s investment leverage useful change?
- *Feasibility:* Could it be done successfully?
- *Innovation:* Will it break new ground?
- *Compatibility with context:* Could it fit national/local policy and organizational realities?

⁵ Since both assessments were sponsored by USAID, and intended to yield recommendations for USAID investments, these criteria paid special attention to USAID’s interests, and to feasibility for USAID approaches to investment.

- *Potential for scaling up and sustainability*
- *Public-Private Partnerships*: Does it advance this interest?
- *Donor coordination*: Is someone else already doing it?

It may be that such an approach would be useful for other teams and projects seeking to develop effective workforce development initiatives in this region. As cited above, workforce development and competitiveness appear to be closely linked, and this author, at least, would not do one without the other.