

STUDYING TRANSITION

THE RUSSIAN MODEL OF LABOR MARKET: WHAT IS AHEAD? (article one)

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At expiration of ten years since the start of economic reforms, we have a good cause to consider a specific Russian model of labor market that has taken shape by now. Regrettably, in Russia key characteristics of this model are not fairly recognized even by experts, not to mention politicians or public opinion. The overall picture is usually lost in discussions about a host of paradoxes and "non-standard" adjustment mechanisms. The Russian labor market is identified as a heap of malformations rather than as an internally consistent system, main characteristics of which are closely interrelated. However, evidence suggests that the Russian labor market performs not in a random way, but follows a certain logic, which is implied by the established model.

What is important, this model was not constructed by anybody from above according to any pre-arranged scheme. It has developed spontaneously under the influence of independent decisions, which were taken by the government, entrepreneurs and workers. Overlapping reactions of main market participants often produced outcomes, which had never been anticipated by anybody and therefore were taken as unexpected. And though they initially could look as some accidental aberrations, more and more evidence came with the passage of time that this was the case of stable and self-reproducing forms of labor relations.

Recognition that there are two alternative models of a "transitional" labor market can be considered conventional wisdom in the literature on transformational processes [1]. The first one is characteristic of Central and East-European countries (CEE), and the second, of Russia and other CIS countries (Baltic countries are usually regarded as a specific

intermediate case). Unfortunately, Russian researchers are used to leave this conclusion unnoticed. As a result, even such problem as reforming labor legislation is most often discussed aside from actual functioning of the Russian labor market, with no regard to distinctive features of the model that has taken shape in the "shock" 1990's.

Evolution of labor relations in the CEE countries went generally in accordance with the initial expectations, which rose at the start of market-oriented reforms. All these countries reproduced, with certain variations, the pattern of labor market that had been quite familiar from the experience of leading West European countries (Belgium, Germany, Spain, France, Sweden et al). Their labor markets are characterized as having high degree of employment protection, complex mechanisms of collective bargaining, considerable segmentation of labor force and substantial long-term unemployment [2]

As expected, transitional shocks inevitably affected the functioning of labor markets in the CEE countries. Many problems of critical importance, which they faced, were unknown to mature market economies (such as, say, adjustment of wages to sharp decline in labor demand under a transformational crisis, or necessity of a massive workforce reallocation from the public to the private sector, etc.). Moreover, they had no financial resources on hand that could be sufficient to completely copy the institutional framework of "mature" labor markets. On the other hand, whenever such a set of institutions was mechanically imported, the outcome was quite discouraging. Perhaps the most impressive example gives Eastern Germany, where such an "importation" resulted in extremely high and extremely long unemployment. Nevertheless, orientation of the CEE countries towards West European experience can hardly be disputed, and the more this experience was assimilated, the closer their markets came up to their West European prototypes with their merits and demerits, problems and limitations.

At the start, nothing could foretell that evolution of the Russian labor market would follow a different scenario and end up in a specific model,

in many ways different from the one that was established in the CEE countries. From the outset, Russia followed other reforming economies, joining with them in "importation" of a standard set of institutions in this sphere: minimum wage was introduced, a system of unemployment insurance was founded, an elaborate multi-layer system of collective bargaining was authorized, payroll taxes were established, tax-based income policy was launched, attempts of wage indexation were made, and so on.

There was nothing "non-standard" in all these steps. This gave way to quite natural expectations that labor market would work in Russia in about the same mode as in other post-socialist countries, which had entered the path of reforms earlier. However, taking into account that the transformational recession was deeper, the scale and severity of problems could have been expected to be different: enterprises would be more active in labor shedding, unemployment would be higher, labor disputes would be more numerous, inflationary pressure from labor costs would be greater, etc. Moreover, having acquired additional "stiffening ribs" of newly introduced institutions, the Russian labor market inherited from the former system a large number of legal rules and regulations that were never discarded. No surprise that the first years after the start of the reforms passed in expectation of an impending catastrophe, which as most observers believed, was unavoidable in the employment sphere of the Russian economy.

"Portrait Number One" - the Actual One

However, these catastrophic forecasts were never to be realized. How did the Russian labor market actually behave under the transformational recession? Let us try to sketch its makeshift portrait [3].

1. Employment in the Russian economy happened to be surprisingly stable and not too susceptible to transition shocks. It declined just by 12-14% over the entire post-reform period, which was obviously disproportional to the scale of decline in GDP that, by an official estimate, reached 40% (in the bottom of the recession). The picture was

different in most CEE countries: there was a rough parity between production and employment dynamics. Employment dropped by 20-25%

along with a comparable or even smaller rate of decline in GDP.

2. Since Russia surpassed the CEE countries in the scale and duration of transformational recession, it could be naturally expected to be a country with the highest unemployment rate. For instance, in Bulgaria where the fall in GDP was comparable with that in Russia, unemployment in the worst years of crisis took in almost a quarter of total labor force. However, the Russian labor market behaved quite unconventionally in this respect. Although the transformational recession

was much deeper and more protracted, unemployment growth was lower and much more gradual.

In all CEE countries, the start of market-oriented reforms was marked by a surge in open unemployment. It rose quickly above the 10%-mark almost everywhere, and even above 15-20% in some cases (in Bulgaria, Poland, Slovakia). The situation stabilized in the mid-90's, when most CEE countries entered their recovery period. Nevertheless, even later on, each economic downturn, even a rather mild one, was immediately translated into a new surge in unemployment.

In contrast to this, there were no such jumps in the unemployment rate in Russia. It was growing slowly and gradually, so that only on the sixth year of market-oriented reforms it surpassed the 10%-mark to reach the level, which had been established in the majority of other transition economies *after* the rebound in their post-transformational recovery [4]. (Only the Czech Republic and Romania demonstrated lower unemployment rates than Russia over most of the 90's).

However, as soon as Russian economy entered a recovery phase, unemployment indicators plunged, declining to less than a half: from the peak of 14.6% in the early 1999 to 7.2% in the mid-2002. No other transition economy experienced such a swift reduction in unemployment.

To summarize, the behavior of Russian unemployment was quite atypical: (a) its dynamics was relatively smooth without any jumps

caused by massive inflow of laid-off workers; (b) unemployment rates never reached the peak values that were typical of most other post-socialist countries; (c) as soon as post-transformational recovery was over, unemployment shrunk much faster than in any other transition economy; (d) and finally, if the situation in the labor market were assessed by the highest of two indicators - the level of either general or registered unemployment, - Russia with her 7% unemployment rate would appear to be one of the most successful transition economies.

3. A sharp decline in working time was a unique feature of the Russian economy. During the first half of the 90's, average number of hours worked by employees in the industry has decreased by almost **a whole month**. No CEE country knew such a decline. Numbers of hours worked stayed quite stable everywhere, changing little from the pre-reform period. Although since the second half of the 90's, working hours went steadily up in the Russian economy, they are still short of their initial length.

What is no less important, wide differentiation was observed in the indicators of working time. Deviations from standard workweek, both to longer and to shorter hours, were very substantial. For instance, about 15% of all employed persons worked more than the standard 40 hours a week. This means that the Russian labor market has demonstrated a high flexibility in working time that was not observed in other transition economies.

4. According to official data, fall in real wages in Russia over the period of 1991-2001 was about 60%. Although this estimate looks overstated for a number of reasons, the very fact that real wages have declined dramatically leaves no room for doubt.

In the Russian situation, wage flexibility was ensured by several factors. In the absence of mandatory indexation, it was quite easy to bring real wages down at times of high inflation, either by freezing nominal wage or by raising it at a slower pace than price rise. (As is well known, major "troughs" in real wages happened under acute macroeconomic shocks and subsequent acceleration of inflation, when

monthly increases in prices broke far away from monthly increases in wages). Bonuses and other incentive payments given at deliberation of enterprise managers amounted to a substantial fraction (about 15-20%) of total worker compensation. Managers could deprive certain groups of workers of such payments, completely or partially, at their own discretion. Another, in a sense extreme way of bringing real wages down

were systematic delays in their payment (this mechanism usually came to the forefront when inflation decelerated). Finally, very high "flexibility" was typical of "shadow" compensation, which as a rule was the first to react to any market fluctuations.

However, other transition economies have also experienced substantial declines in labor incomes. Although in most of them the decline was less sizeable than in Russia (as a rule, in the range of 30-35%), in some cases, it was of comparable scale. For example, real wages in Bulgaria were more than halved during the period of reforms.

Specificity of Russian experience looks still more striking when we turn our attention from dynamics of **consumer wages** (deflated by consumer price index) to dynamics of **producer wages** (deflated by producer price index), which in fact determine employers' demand for labor. Real "producer" wages have increased in comparison with their pre-reform level in almost all CEE countries, in some of them quite substantially - by 20-30%. Gradual increase in labor costs inevitably weakened labor demand, contributing to keeping unemployment at a persistently high level.

In Russia, producer prices were rising faster than consumer prices during most of the 90's, so that from the employers' point of view, the fall in real wages was even deeper than from the workers' point of view. Contrary to the CEE countries, real "producer" wages in Russia did not tend to return to their pre-reform level so that fall in labor costs was continuing without any sign of a reversal. This reduction in the price for work force contributed to higher labor demand, preventing a surge in open unemployment.

5. In all post-socialist countries, transformation of economic regime was accompanied by increased inequality in labor incomes. However, in the CEE countries it was still fairly moderate. In Russia, differentiation in earnings became exceptionally deep: while in 1991 Gini coefficient was 0.32, it was as high as 0.45 by the late 90's. At present, in Russia Gini coefficient is half as high again or twice as high as that in the CEE countries. This means that not only average level, but also relative wages in Russia have been extremely flexible.

6. During the entire period of transition, Russia had intensive labor turnover. A coefficient of gross labor turnover, which is defined as a sum of hiring and separation rates, reached 43-50% in the whole economy and 45-65% in the industry, which is a sign that employed personnel underwent a large-scale reshuffle every year. Russia substantially exceeds the majority of CEE countries in the rate of inter-firm reallocation of work force, which resulted not only from more active separations but from more active hiring as well. This seems to be quite unexpected in a situation of deep economic recession. In other transition economies, hiring rates, as a rule, went sharply down at the start of market-oriented reforms. In contrast, hiring kept at persistently high level in Russia, which is one of the most paradoxical characteristics of her labor market. This implies that while hiring new employees, enterprises were not much worried that they would be unable to get rid of them afterwards whenever economic conditions deteriorated. (If dismissals would cost them a lot of money and much time, enterprises should have been much more cautious about hiring new workers).

Another no less paradoxical feature is prevalence of voluntary separations. In the CEE countries, the majority of separations were involuntary. In Russia, separations initiated by managers never became widespread. Lay-offs were fewer than 2.5% of enterprises' personnel, or 10% of total separations. Quits were prevailing and reached 16-20% of enterprises' personnel, or 64-75% of total separations. Even if a part of involuntary separations were disguised as voluntary, it is hard to doubt that the majority of separated employees were those who did it on their own initiative.

7. Various "non-standard" ways of adjustment have flourished on the Russian labor market: part-time working, involuntary administrative leaves, multiple job holding, informal employment, delays in wage payments and shadow remuneration. Market agents spontaneously worked out these adjustment mechanisms in order to be able to react immediately to unexpected changes in economic and institutional environment. As a rule, they were the first to take the initial blow, and adjustment in more conventional forms came later and therefore was smoother.

Here, the term "non-standard" does not mean that these adjustment mechanisms should be considered absolutely unique. They certainly could be found in other transition economies as well, in various modifications and combinations. However, their scale and scope were nowhere as large, concentration as dense, and roots as deep as in Russia.

No great surprise, from a certain point on, such ways of adjustment were taken as daily routine, as common practice, as a standard of industrial relations. In certain years, almost a quarter of total personnel at large and medium-size enterprises in Russia were transferred to shorter working day or given administrative holidays; 10-15% of employees were multiple job-holders; almost every fifth worker was engaged in some kind of informal employment; in the worst years, wage arrears involved three quarters of total employees; according to the estimates by Goskomstat of the RF, "shadow" wages reached 40% of the official ones.

All these "non-standard" mechanisms had one important feature in common - they were informal or semi-formal. They either evaded the law and other formal rules or ran against them. Untimely and "shadow" worker compensation, part-time and secondary employment personified relationships between employees and employers so that explicit labor contracts gave way to implicit ones.

8. Considering all shocks that the Russian economy had to bear in the 90's, it could be natural to expect a wave of acute and prolonged

industrial conflicts. Strangely enough, disputes stayed at a rather low level. In the first half of the 90's, from 3 to 25 workdays were lost in strikes per 1000 employees; in the second half of the decade, the number of lost workdays rose to 45-84, but by the end of decade it declined to 3 days. This is a fairly moderate level by international standards. For instance, average number of days lost in strikes in the OECD countries in 1985-1992 reached 340 per 1000 employees. And although strike activity in most CEE countries was also quite moderate, in some countries it exceeded the Russian indicators (for instance, 230 days were lost per 1000 employees in Poland in 1992). Moreover, most Russian strikes were evidently demonstrative and lasted no longer than 2-3 days.

References and Notes

- [1] Boeri, T., and K. Terrell. Institutional Determinants of Labor Reallocation in Transition. - "Journal of Economic Perspectives", 2002, vol. 16, No 1.
- [2] For a detail analysis of evolution of labor markets in Central and East-European countries, see: Boeri, T., Burda, M.C., and J. Kollo. Mediating the Transition: Labour Markets in Central and Eastern Europe. N.Y.: Centre for Economic Policy Research, 1998.
- [3] For a more detailed analysis, see: V. Gimpelson and D. Lippoldt. The Russian Labour Market: Between Transition and Turmoil. Lanham: Rowman & Littlefield, 2001; R. Kapelyushnikov. The Russian Labor market: Adaptation without Restructuring. Moscow: The Higher School of Economics, 2001; Bureau of Economic Analysis, Survey of Employment in Russia, 1991-2000. Moscow.: TEIS, 2002.
- [4] In this case, we deliberately content ourselves with assessments of **genera/ unemployment**, which is measured on the base of sample surveys of labor force according to the criteria established by the World Labour Organization. As for **registered unemployment**, it has been maintained at a surprisingly low level throughout the 1990's, and is only 1.5% today. No other transition economy can boast of such an achievement. However, study of reasons for divergence between indicators of general and registered unemployment is beyond the limits of this paper.