

Segmentation of the Labour Market And The Employee Rights in Croatia¹

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Despite all-encompassing applicability of the relevant laws, Croatian labour market is in practice segmented. Employees in different sectors tend to experience substantial differences in protection of their legal and contractual rights. Due to the institutional insufficiency of the judicial system, segmentation largely results from the patterns of unionisation and collective bargaining. Employees of the highly unionised public sector and state-owned enterprises, or some larger companies, tend to enjoy job security, above-average wages, and good working conditions. The workers in the SME sector and some larger privately-owned companies, where unionisation is ineffective or even discouraged by employers, experience more problems in the protection of their rights. Having analysed the crucial legal provisions and the available data on (un)employment, wages, unionisation, social dialogue and labour disputes, we discuss the effects of such segmentation on the labour market, particularly focusing on the current reforms aimed at increasing the levels of flexibility of industrial relations, and offer some policy recommendations.

Key words: employee rights, labour market, flexibility, social dialogue.

INTRODUCTION

Despite some opposing views (cf. Alchian and Demsetz, 1972), there is a wide recognition of specificity of labour as a re-

source and commodity (Solow, 1990; Hodgson, 1999), which justifies a relatively high degree of the regulation of the labour market. The regulative measures include laws and administrative activities of the sta-

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te; collective bargaining; corporatist bodies that facilitate the dialogue among social partners (employers' unions, trade unions and the government) and social networks that constrain the behavioural and policy actions of the participants (Regini, 2000). The degree and means of regulation of the labour market have become highly debated political and economic issues in the last couple of decades, usually under the assumptions that too much regulation hinders the adaptability of an economy, creates or maintains higher levels of unemployment and discourages job creation. Despite the contestability of the issues surrounding unemployment benefits and working time, most of the debate has been focused on wage levels and structures and employment protection mechanisms, i.e. laws and collective agreements that constrain the employers' ability of firing at will, and the costs of hiring or maintaining a particular number of employees.

The debate regarding the labour market reform has often been championed by mainstream economists (cf. Becker, 1999, Rutkowski, 2003). As OECD (2004: 89) notes, most analyses of employment protection have been conducted within a framework that does not justify its existence. Policy advice based on the view that a more flexible labour market leads to a better economic performance has also been endorsed by some international organisations (e.g. World Bank and International Monetary Fund), which was particularly pertinent in the transition countries of Central and Eastern Europe². Although the reform implementation has sometimes attempted to follow neo-liberal prescriptions, the latter often had to be compromised due to poli-

tical unfeasibility and/or institutional traditions of particular countries (cf. Arandarenko, 2004). The reform has often revolved around the reduction of legal 'rigidities' (i.e. employment protection legislation). Both legal rights of individual employees and the activities of trade unions (e.g. collective bargaining, industrial actions) are perceived as obstacles to managerial autonomy and the restructuring of enterprises, which is viewed as a prerequisite of success in the turbulence of the global economy. Such 'rigidities' of the labour market raise the costs of hiring and firing employees and thus hinder the flexible response to shifting economic conditions (including external shocks), as well as the entry of new firms into the market. What is usually proposed instead is deregulation and decentralisation of industrial relations - lowering the costs of dismissals, increased use of fixed-term and temporary contracts and individual or firm-level contracting, whereby employers and employees design their relationships in accordance with particular conditions they face (cf. Rutkowski, 2003). There is an important degree of validity in such claims: competition in the product market and the differentiation of consumption patterns invokes the need for the flexible and differentiated production (cf. Harvey, 1990). That entails the need for a more flexible deployment of labour, which, however, can be implemented in a variety of ways. Moreover, although there is no direct causality between employment protection legislation (EPL) and unemployment, there may be a negative relationship between EPL and employment, due to lower participation of young and female employees interested in more flexible forms of employment (UNDP, 2003). However, it remains to be seen whether shifting

² In the context of South-East Europe, Arandarenko (2004) claims that international organisations with competing agendas, such as International Labour Organization and the European Union have been far less influential in labour policy reform. He attributes such developments to loan conditionalities imposed by the IMF and the World Bank, as well as to more effective articulation and communication of their policies, rather than to the overwhelming evidence of the link between labour market flexibility and superior economic performance.

the balance of power between labour and capital through deregulation of the labour market is the optimal way for achieving flexibility at the levels of firms and sectors. Hereby there is likely a difference between manufacturing and services. The former requires technological upgrading which could be facilitated by trade union co-operation. In the case of services, it is questionable whether deregulation has similar effects on all service sectors. Moreover, stimulation of employment growth in low-end consumer and social services through deregulation of wages and employment protection is often a socially undesirable strategy (Esping-Andersen and Regini, 2000a) – especially in the long term.

The distribution of benefits and costs of deregulation is regularly rather uneven – both within firms and across the labour force. Such reforms tend to reinforce already existing trends within economies and societies, as they take on the post-industrial features related to globalisation – such as weakening of the organised labour, greater individualisation of risks and rewards, and the tendencies toward greater social and economic inequality. In post-industrial socio-economic conditions, there is a growing difference between the core and the periphery of an organisation – between employees who develop the ability to reap the rewards of the socio-economic change and those who lag behind. Although the distinction between them is somewhat blurred, the line usually follows opportu-

nities (or the lack thereof) of certain groups of workers to acquire and utilise knowledge and other resources³. Employees whose human capital gives them either a core position within an organisation, or an advantageous position in the labour market, are much more likely to benefit from the increased flexibility of industrial relations than generic labour in manufacturing or services, which has traditionally used collective means (i.e. trade unions) for securing their interests. General individualisation, legal protection of employees' interests and phasing out of blue-collar jobs have reduced the role of trade unions⁴. Facing the model of individual bargaining, workers without portfolios of skills that can secure their prospects in the job market find themselves in a complex situation. For them, intensified competition in the product market, labour market volatility and lack of institutional protection often mean that increased responsibility is coupled with both low wages and job insecurity.

Recent policy debates have included realisation of the 'double bind' of the current labour market trends (Wilthagen and Tros, 2003). Simultaneous demands for further flexibilisation of labour markets, employment and the work organisation, as well as for providing security to employees (especially to the vulnerable groups of employees) and the unemployed have engendered the concept of 'flexicurity'. Partially based on the Dutch and Danish labour market reforms in the 1990s⁵, flexicurity can be defined as

³ Senior staff and core knowledge workers have become the most important corporate assets able to enjoy autonomy, flexibility and creativity, whereas much of the 'generic labour' (Castells, 1998) without sufficient opportunities to learn – especially lower-ranked, part-time and temporary employees – is often subjected to strict control and low career prospects (let alone social status or self-respect).

⁴ The incapability of trade unions to function in redefined organisational forms, act in service and high-technology industries and represent new categories of workers (such as women, youth, immigrants and, especially part-time and fixed-term workers) have contributed to their weakening (Drucker, 1990; Castells, 1996; Gorter, 2000).

⁵ The Danish model combines flexibility (high degree labour mobility due to minimal employment protection legislation), social security (generous unemployment benefits) and active labour market policies (OECD, 2004).

‘a policy strategy that attempts, synchronically and in a deliberate way, to enhance the flexibility of labour markets, the work organisation and labour relations on the one hand, and to enhance security – employment security and social security – notably for weaker groups in and outside the labour market on the other hand’ (Wilthagen and Tros, 2003: 4).

Potentially laudable as an idea, flexicurity currently still seems to be under-researched as a concept and underdeveloped as a policy strategy, which still waits to be translated into politically, socially and economically viable policies. The viability and effectiveness of the flexicurity approach are likely to depend on the availability of substantial resources, coordinated approach to multiple reforms and considerable fine-tuning, as the Danish case demonstrates (cf. Madsen, 2002).

DEVELOPMENTS IN THE LABOUR MARKET IN CROATIA

Prior to 1990, the majority of firms in Croatia were formally socially owned and operated according to the doctrine of self-management. The system of industrial relations was managed according to two main principles: full employment policy and egalitarianism. Full employment policy entailed that all healthy working-age citizens should be employed. However, due to relatively decentralised decision-making, employment rates were lower than in the other Central and Eastern European countries and some unemployment also existed. Egalitarianism entailed a weak link between the contribution of an employee and the accompanying financial compensation. Employees’ wages were mostly based on the hours worked, regardless of the effectiveness. Direct results were a very low unemployment coupled with overstaffing,

low labour productivity, high labour costs, low motivation of workers and problematic criteria of promotion. According to Vujčić (1994), in 1988 hidden unemployment, i.e. the number of redundant workers that were kept employed for social or political reasons, was around 300.000, or around 10 percent of the working age population. As for the protection of employee rights, since employment protection was semi-explicitly embedded in economic and social policies of full employment, we can talk about ‘quasi-legal protection’ of the position of employees regarding their work status and some material rights such as wages, as well as pension and social welfare contributions. There have also been issues where rights were protected less strongly and where discrimination, nepotism and political influences occurred. Higher hierarchical positions and the status associated with them were mostly occupied by the Party members. Elements of social policy (e.g. housing and subsidised purchases) that were related to employment also enabled a degree of manipulation. Trade unions and the only trade union federation were controlled by the Party. The judiciary system oscillated between relative independence and political influences.

Since the product market already existed, restoration of market economy in Croatia primarily consisted of the introduction of market-based relations into capital and labour relations. Both were primarily done through privatisation. By selling off firms to private owners, the state was giving up responsibility for the assets that constituted those firms, including their employees. In order to balance this process, building of institutions associated with effective market economy within a democratic political system was needed. The definition and distribution of economic assets through privatisation had to be complemented by defining, enforcing and modifying legal and social

frameworks steering business transactions and the agents engaged in them. Although privatisation and institution building were expected to contribute to the constitution of privately owned firms and legal and social prerequisites for their effective functioning, characterised by both accountability and profitability - both of them have been mismanaged to a significant extent, which had a significant impact on industrial relations and the labour market. The complexity of the privatisation model was not balanced by strong legal frameworks and independent judiciary, which enabled widespread political influences, arbitrariness, nepotism and corruption (cf. Franičević, 1999). Widespread neglect of new owners towards the acquired companies (cf. UNDP, 1998) has extended from physical and financial resources to employees. On the one hand, there was an increased tendency towards authoritarianism. When the political transition began, ideological motives and a lack of incentives had already endowed workers' participation in decision-making with an unfavourable reputation. Since the central privatisation issue was not efficiency improvement, but gaining control, the trend has not changed. A tendency towards centralisation of management and leadership accompanied by marginalisation of other employees (especially of the middle management) has been noted in many Croatian enterprises (Sikavica, 1997). The privatisation process favoured insiders and individuals connected to the political elite. It was also coupled with the structural problems of the economy. That resulted in lay-offs and sharp unemployment growth. Unemploy-

ment started to grow in the late eighties, when some market principles were introduced in the Croatian economy. Hidden unemployment led to a sharp increase in registered unemployment at the beginning of the transition process. That was further reinforced by the strategy of defensive restructuring of firms (cf. Vehovec and Domadenik, 2002). Due to the lack of affordable sources of finance, and intensified competitive pressures from domestic and foreign firms, managers were much more focused on cost reductions than on the finding new market opportunities, which could increase the volume of business and reduce the negative impacts on the labour force. Moreover, the taxation system favoured the substitution of labour for capital. High payroll taxes and social welfare in contributions led to high unit labour costs (at least in the first stage of transition)⁶, whereas the taxation of capital gains and interest was non-existent. Under such conditions, managers usually opted to reduce costs, cut employment and improve productivity. For many firms, especially the privatised ones, downsizing has become a prerequisite for a survival in a more competitive environment. Average firm size has almost halved, decreasing from over 22 employees in 1993 to about 12 employees in 2000 (Rutkowski, 2003)⁷. Employment rate dropped from 57.7 percent in 1991 to 50.9 percent in 2001. The outflow was roughly equally distributed by inflows into unemployment and inactivity, including early or disability retirement. Long-term unemployment⁸ accounts for 53 percent of total unemployment, which explains a large number of discouraged workers who often drift into

⁶ In the course of several tax system reforms, payroll taxes and social welfare contributions were significantly reduced. In 2001 they were lower than the average for the EU first round accession countries.

⁷ It should be emphasised that average firm size was also strongly influenced by emergence of new SMEs. According to a calculation by Vedran Šošić, only 36 percent of the differential in average firm size between 1993 and 2001 resulted from layoffs.

⁸ Long-term unemployment occurs when workers fail to find new paid employment after six months of unemployment.

inactivity (UNDP, 2003). After a decade of transition, Croatia still has very high rates of registered unemployment (18.5 percent⁹). The ILO measure was at 14.4 percent in the second half of 2002. Moreover, the government in early nineties allowed a wide use of early retirement schemes, as a seemingly convenient way to reduce unemployment figures and social problems at the same time. Consequently, a sharp growth of the number of new retirees occurred between 1990 and 1994 (around 200.000 new retirees), which caused a dramatic fall of the ratio of employed to retired persons (from 3.00 in 1990 to 1.97 in 1994 and 1.36 in 2001). The need to finance the corresponding pension fund and budget deficits entailed high taxes on labour. Even though these taxes were eventually lowered, wage growth robustly surpassed productivity growth in the period 1994-2001, resulting in high labour costs. That contributed to lower competitiveness of enterprises, especially in labour-intensive sectors, reinforcing the trend of job shedding (as outlined above), and weakening the export performance.

Also, transition brought about labour reallocation from large socialist firms (especially in traditional manufacturing) and the public sector to services, new private SME and self-employment. Restructuring of the economy entailed a shift from manufacturing to services, much of which occurred due to the lack of competitiveness of domestic manufacturers and rapid growth of imports. The structure of employment by firm size has thus changed. Employment in large firms went down by almost 5 percent per annum between 1993 and 2000. The same trend appeared in medium-sized firms, although less precipitously (by about 4 percent annually). At the same time, employment in small firms increased by

over 8 percent per annum. Looking from a different perspective, employment in state-owned firms fell by over 12 percent while in private firms increased by 11 percent (Rutkowski, 2003). However, employment growth in the SME sector has not been sufficient to offset the losses in the public sector and larger companies, which contributed to the problems discussed above.

Most SMEs engage in retail trade, cost-competition in standardised products and services with low innovative content, which generally entails low skill levels. At the same time, one would expect low levels of unionisation in such enterprises. Restructuring and the growth of the SME sector occurred in turbulent circumstances – ranging from the war for independence to privatisation and various institutional reforms, many of which have been coupled with the institutional insufficiency and arbitrariness of the state administration. In the following section we examine whether these processes resulted in increased segmentation of the labour market and high vulnerability of particular groups of employees regarding the protection of their rights.

FUNCTIONING OF LABOUR MARKET INSTITUTIONS

In this section we tackle the main institutions that characterise the labour market and define the scope of employee rights, including the labour law, trade unions, collective agreements and tripartite social dialogue, simultaneously examining their effects on the segmentation of the labour market.

Labour Law

Croatia has developed an institutional framework regulating industrial relations

⁹ The recent decrease in registered employment rates has more to do with more strict application of the rules related to that status, than to newly created jobs.

that is very similar to the more developed Continental European countries. Labour Law, which was adopted in 1995 (Official Gazette 38/95)¹⁰ and came into effect in 1996, used to be the cornerstone of that framework. Apart from the individual employee rights¹¹, the Law also dealt with the collective rights: worker participation in decision-making through work councils, the establishment and activity of trade unions, collective agreements, the peaceful settlement of collective labour disputes, strikes and lock-outs, and the establishment of the Economic and Social Council as a tripartite body for the facilitation of the social dialogue.

During the last decade, unemployment has been perceived as a major economic and social problem. According to some interpretations, the Labour Law played a major role in discouraging the employers to take up new employees, due to relatively high costs of their dismissal. Individual dismissals were costly due to the long advanced notice period and high severance pay. Severance pay was determined as two weeks of salary per year of service, with no upper limit. Laying-off redundant workers was difficult and costly due to both high procedural and monetary costs of dismissals. Employment protection regulation in Croatia by some researchers was among the strictest in Europe (Biondić et al., 2002).

Inflexibility of the Croatian labour market was reflected in a high value of a composite index of the strictness of employment protection legislation (EPL) developed by OECD¹². When compared to other countries, Croatia had the second highest value of the index (3.6), which was significantly higher than the OECD average (2.0), EU countries (2.4) and the transition countries for which the data exists (2.2). Main generators of such conditions were complicated dismissal procedures and the restrictions on temporary contracts, as well as unlawful and collective dismissals.

The actual liberalisation of the labour market in Croatia started much before the legislative one. This can be measured by the structure of employment contracts according to duration, because fixed-term and temporary contracts entail a lower level of rights than permanent contracts. A comparison between 1997 and 2002 reveals an increase in temporary employment and a fall in permanent employment (see Table 1). Temporary contracts became shorter in average, with a particularly sharp increase of the proportion of contracts expiring in less than five months (see Table 2). Based on the 2001 Labour Force Survey, Rutkowski (2003) estimated the incidence of temporary employment contracts in the case newly created jobs at 55 percent.

¹⁰ The Law was subsequently corrected and/or amended several times (cf. Official Gazette 54/95, 65/95, 17/01 and 82/01).

¹¹ The Law explicitly addresses the rights connected to life, health, privacy and dignity, education and training rights, motherhood rights, protection of permanent or temporary disabled employees and right to participate in decision-making.

¹² EPL index is calculated as a weighted average of 22 indicators that quantify different procedures, costs, limitations and terms related to cancellation of the employment contract. One could be critical about the definition of the index component tackling unlawful dismissals, which accounts for 13 percent of the total value of the EPL index. Hereby the compensation and the obligation of the employer to return an unlawfully dismissed worker to an appropriate position take up 50 percent of the component, which seems inappropriate.

Table 1.
Employment contracts by duration – in 1997 and 2002.

Types of employment contracts	1997	%	2002	%
Permanent contracts	1,147,803	88.3	1,092,040	87.5
Fixed-term and temporary contracts	87,416	6.7	121,161	9.7
Seasonal contracts	25,948	2.0	16,034	1.3
Specific assignment contracts	38,107	2.9	18,905	1.5
Total	1,299,274	100.0	1,248,140	100

Source: Crnković-Pozaić (2004)

Table 2.
Duration of fixed-term and temporary contracts - in 1997 and 2002.

Employment contract duration	1997	%	2002	%
Less than 1 month	4,402	2.9	4,851	3.1
Between 1 and 5 months	30,678	20.3	80,046	51.6
Between 6 and 12 months	31,773	21.0	24,406	15.7
1 year or more	22,934	15.1	13,830	8.9
Employment at will	61,685	40.7	32,109	20.7
Total	151,471	100	155,242	100

Source: Crnković-Pozaić (2004)

The initial stage of reform enabled the foundation of private employment agencies. Other legislative inadequacies, which have been perceived both by the domestic social partners and the international institutions, were expected to be addressed by the Labour Law reform. So a debate has been initiated by the government, with the intention of reaching a consensus with the representatives of trade unions and em-

ployers. Many of the amendments proposed were not markedly contentious, but an intense public debate emerged around three main issues: severance payments, dismissal periods, and the definition of micro enterprises (whereby dismissal procedures are less strict)¹³. Despite a basic agreement that some employee rights regarding severance payments and dismissal periods should be somewhat reduced, the degrees

¹³ All these issues would require concessions by trade union representatives, to which the overall membership was strongly opposed. Moreover, flexibilisation would weaken the relative position of trade unions. That made the issue of devising means of compensation to trade unions also a subject of negotiations. A partial solution was found in introduction of compulsory contributions of non-members to trade unions (based upon referenda) and in the increase of the maximum level of unemployment benefits (by 11 percent). The aforementioned referenda mostly pertain to the public sector, where universal coverage of collective agreements prevails.

and the applicability of those reductions have been contested by trade unions. What sparked an even more intense debate was the definition of micro-enterprises, which are subject to less labour regulation, including easier conditions for dismissals. The old Law set the threshold at 10 employees, whereas the proposal was to increase it to 20 employees¹⁴. The Croatian Employers' Association strongly supported the proposal as a way to extend the autonomy of small entrepreneurs, and the trade unions saw it as a way of reduction of employee rights that neither produced any benefits for them nor was compensated by some other concessions. The consensus has become unattainable, but in July 2003 the Parliament nevertheless adopted the amendments to the Labour Law (Official Gazette 114/03) that adopted most of the changes. Although all components of the EPL index were reduced, reforms affecting temporary employment had the greatest impact¹⁵. The new value of the EPL index (2.8) still places Croatia among the more regulated labour markets in transition countries (cf. Matković and Biondić, 2003).

The new Law and other regulatory changes should bring some new incentives to a greater participation in the labour market, but will not automatically create an effective labour market, let alone a pattern of sustainable job creation. The experiences of some other countries, such as Spain (cf. Toharia and Malo, 2000), demonstrate that deregulation and flexibilisation of temporary employment contracts (especially if the regulation of permanent contracts remains mostly unchanged) can engender a dual

labour market. Hereby 'insiders' tend to retain permanent positions and 'semi-outsiders' occupy inferior labour market positions in which temporary work is accepted because few permanent jobs are available. Another potential pitfall comes from asymmetries whereby firing is not followed by hiring, as it has occurred in Italy (Samek Lodovici, 2000b). More generally, empirical evidence from OECD countries suggests in the 1990s the occurrence of temporary contracts has grown faster in countries where their regulation has been significantly eased in relation to the regulation of permanent contracts (OECD, 2004)¹⁶. The Croatian case brought simultaneous deregulation of permanent and temporary contracts, with the latter being more pronounced. Although the available theories emphasise the relative difference in regulation of permanent and temporary contracts as the critical factor that engenders labour market duality, empirical evidence of the outcomes of simultaneous reforms of both contract forms is scarce (cf. OECD, 2004). It remains to be seen whether liberalisation of the Croatian Labour Law will intensify the substitution of permanent employment contracts by the fixed-term and temporary ones or not. If it does, the position of 'flex-workers' in the labour market may weaken even further, due to an ineffective judicial system and low levels of unionisation.

Trade Unions

Workers in Croatia are entitled by law to form or join unions of their own choosing without prior authorisation. The participa-

¹⁴ The threshold was eventually set at 20 employees, but the leeway given to micro-enterprises was reduced: the employer now needs to state a justified cause for dismissals.

¹⁵ The initial proposal also included extensive deregulation of temporary employment and reduced severance payments and dismissal periods for long-term employees of a company, which would have reduced the value of the EPL index to 2.25 (Matković and Biondić, 2003).

¹⁶ Stricter rules applied to regular contracts 'may tend to increase the incidence of temporary work and to limit the extent to which temporary contracts will be converted into permanent ones' (OECD, 2004: 87).

tion rate in trade unions is decreasing. In 1994, the proportion of workers belonging to trade unions was approximately 60-70 percent. In 2002, it was around 45-55 percent. The negative trends can be explained by privatisation and restructuring of the economy, and change of the age structure of the working population (Cimeša and Marinković Drača, 2002). The former resulted in a higher proportion of companies in which unionisation is either considered unnecessary or actively discouraged. Moreover, younger employees are less likely to join trade unions. They are mostly engaged in fixed-term and temporary employment contracts and their level of identification with trade unions is lower. There is no data on the total number of employees to whom collective bargaining agreements apply. In the public sector, the application of such agreements is usually universal. Collective bargaining in the private sector is both more decentralised and less common, so the coverage of employees is somewhat lower.

The labour movement involves six national labour federations. Unionisation is associated with a relatively strong position in the labour market. All federations seem to represent a proportion of the core workforce, usually the employees of larger companies and public sector, whose interests are relatively well protected. However, the unions' actions for the protection of the rights of existing employees may harm the unemployed and thus deepen the insider-outsider divide. However, there are internal differences among the federations stemming from the division of their membership according to sectors. Membership structure has important implications on the negotiating positions of the federations. The largest federation, Union of Autonomous Trade Unions (UATUC), gathers 46 percent

of all unionised workers (Gatarić, 2004), most of them in manufacturing, retail trade and hospitality industry. Their membership is declining due to declining employment in traditional manufacturing and substitution of unionised jobs by the non-unionised ones. The second largest federation, Independent Trade Unions of Croatia (19 percent of total union membership) encompasses former or current state monopolies in oil and petrochemicals, electricity generation and transmission, telecommunications, postal services, as well as the employees in financial institutions. Of three other major federations, one (Union of Public Service Trade Unions) represents public sector employees, whereas the other two are more heterogeneous. Since four federations share the target group (employees in the business sector), there is a competitive struggle for members, which involves not only competitive lowering of membership fees and decentralisation of spending decisions to the firm level, but also takeovers of other trade unions' members. The struggle for the membership base undermines the relationships between federations and the formation of the common position in the social dialogue with the employers (cf. Cimeša and Marinković Drača, 2002).

Collective Bargaining

The system of social dialogue is rather complicated. It takes place at four different levels i.e. at national, regional, sector, and company levels. A crucial role is given to the process of collective bargaining, which takes place at sector and company levels¹⁷. Collective bargaining is adequately regulated by the Labour Law, but its application is patchy and often fraught with problems. Mutually beneficial agreements occur mainly in larger and more resourceful priva-

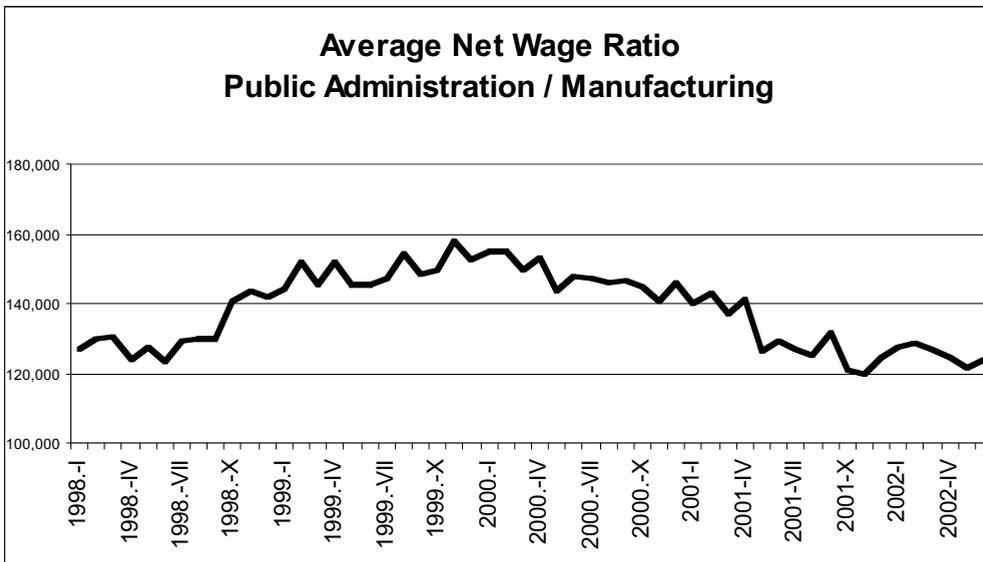
¹⁷ National and regional levels of social dialogue mainly occur through Economic and Social Council, which is tackled in the next section of the paper.

te firms, and agreements are also regularly reached in public services and state-owned monopolies. However, the public sector agreements are often conditional upon excessive government concessions to trade unions, which thus often follow maximalist negotiation strategies. The involvement of public-sector trade unions contributes to a more egalitarian wage distribution than in other transition countries (cf. Rutkowski, 2003), but also results in marked wage differentials between public and private sectors. The graph below compares the wage dynamics in public sector and manufacturing between 1998 and 2002. The wage differentials, which vary between 20 and 60 percent, cannot be attributed solely to educational differences between sectors. They reflect the fact that manufacturing is mostly privatised, the level of unionisation is lower, and collective bargaining is more decentralised, which means that collective agreements do not cover all the employees.

Sharp growth of these differentials in 1999 shows the influence of an attempt of the government to steer the election results by pre-election wage increases in the public sector.

Underdevelopment of the social dialogue is acknowledged by all parties, although the government is still more likely to participate in collective agreements. The problems encountered in the social dialogue in companies are related to the lack of motivation and initiative on both sides. Managers often display a tendency towards centralised decision-making accompanied by marginalisation of other employees. Under such conditions, most employees are not interested to contribute more than it is required, because of low likelihood of the success of their efforts. Moreover, workers' participation in decision-making has an unfavourable reputation due to the past experiences of self-management. Consequently,

Graph 1.
Average Net Wage Ratio - Public Administration / Manufacturing, 1998-2002.



Source: CBS

although the law enables the existence of employee councils in firms with more than 20 employees, their implementation has not produced discernible results.

According to Cimeša and Marinković Drača (2002), private sector shows many examples of employers' procrastination to engage in negotiations and failures to fulfil the existing collective agreements, which results in a negative climate in further co-operation. Employers and trade unions find themselves in positional negotiation whereby both parties maximise their claims, which seemingly ensures their credibility in relation to their key stakeholders (shareholders and trade union members, respectively). However, the escalation of conflict becomes detrimental for both sides, because it locks them in an unproductive relationship in which is nearly impossible to build trust and effective partnership in the development of the enterprise. Moreover, lack of trust does not only affect the relationships at firm or sector levels, where collective bargaining occurs. It becomes a negative factor in the tripartite dialogue, therefore hindering the possibilities for an effective social partnership.

Tripartite Social Dialogue

At the level of the whole economy, efforts have been made to build an effective tripartite social partnership among the government, private employers and trade unions, but the results have been moderate. The central body that should provide the

representation of these interests at the national level is the Economic and Social Council (ESC), which was established in 2001. It is established as a consultative body that should facilitate co-ordinated economic and social policies, encourage effective collective bargaining, implementation of collective agreements and reconciliation among partners when necessary. At the regional level, there are also ESCs in most counties, whose role is to deal with similar issues from a more practical perspective¹⁸.

Functioning of the ESC has been burdened by the ambiguous position of the government as a social partner. Despite the participation of the highest-ranking officials (such as Deputy Prime Minister) on the ESC, its recommendations do not bind the government¹⁹, which results in misunderstandings and conflicts. Evaluations of functioning of the ESC by the social partners differ considerably (Cimeša and Marinković Drača, 2002). In addition to generally positive opinions, government officials still claim that the other two parties are unrealistic and reluctant to assume responsibility for difficult decisions. From the employers' perspective (which is mainly advocated by the Croatian Employer's Union²⁰), trade unions fragmentation²¹ hinders the effectiveness of collective bargaining processes. As the trade unions represent different types of workers, they often follow different negotiating strategies. That may even produce an advantageous negotiating position for Croatian Employer's

¹⁸ There are also other bodies that should play a supportive role in the social dialogue. The governmental Office for Social Partnership was established in 2001 to support the work of the ESC. Social partners also participate as external members of parliamentary committees (work, health and social policy; finance and state budget; economy, development, and reconstruction), and various quasi-governmental institutions.

¹⁹ Recommendations of the ESC are just an input into the legislative procedure, and the position of the government may deviate from it due to other considerations. An important factor has been the divisions among the parties in the government.

²⁰ Croatian Employer's Association is the main private sector employers' organization in Croatia. Its 5.000 corporate members have more than 300.000 employees.

²¹ There are representatives of 5 trade union federations on the ESC.

Union. The main trade union representatives' complaint addresses the insufficient involvement of trade unions in the initial stages of the legislative process, when the crucial outlines of new regulations are debated. Their involvement in later stages is thus often reduced to a choice between endorsement and opposition to new legislative proposals.

Until the end of 2001 the ESC functioned with some difficulties, but some agreements were reached, including the Partnership for Development. Hereby almost all main social partners (with the exception of third largest trade union federation) agreed on 17 goals related to economic and social issues. Its implementation required the agreement on four documents dealing with social policy, wage policy, restructuring and privatisation, and an analysis of the European Social Charter. None of these documents was agreed upon and endorsed by the end of March 2002, as initially agreed. Moreover, meanwhile the government published the proposal of amendments to the Labour Law, with which the trade unions strongly disagreed. Consequently, the largest trade union federation UATUC left the Partnership for Development, soon to be followed by other federations, which effectively meant the agreement's collapse. That had substantial consequences on the relationships among the social partners and the functioning of the ESC, and was further reinforced by the debate surrounding the Labour Law amendments (see above). Despite the ineffectiveness and distrust characterising the ESC, in 2002 the representatives of the same social partners (with the addition of representatives of academic community) gathered within an additional

consultative body - the National Competitiveness Council, whose results are yet to be seen.

VIOLATIONS OF EMPLOYEE RIGHTS

As stated above, the legislation defines a comprehensive scope of employee rights, and anecdotal evidence suggests that many of them are occasionally endangered. However, since most of the labour disputes revolve around the fulfilment of financial obligations, it makes sense to focus on them. This does not imply that the protection of other rights is less important, but the reliable data on them is scarce. Few such violations are reported, let alone followed by legal action. That can be explained by factors like widespread authoritarianism of managerial practices, high unemployment and inefficient judiciary, each of which reduces the likelihood of reporting. In some cases, some indications are provided by aggregate data²², or occasional surveys.

Wage Issues

Wage arrears were one of the most serious problems in the Croatian labour market. The number of affected workers grew from 55.000 in 1993 to 140.000 in 1998. In 2001 around 92.000, which represented 7.2 percent of the employed, did not receive their wages and associated taxes and social welfare contributions on time. Until the 2001 amendments to the Labour Law, workers were not allowed to strike for that reason. Since the failure to pay wages was often caused by insolvency of enterprises, the problems often accumulated over time. In non-performing state-owned enterprises

²² For instance, during the last five years women have comprised almost three fifths of first-time job seekers (cf. HZZ, 2004). That may be partly attributable to their occupational choices and dependence of some social security entitlements on unemployment status (which was abandoned in 2002). However, it also suggests a degree of discrimination of women due to uncertainty regarding their family plans.

a common occurrence was the exertion of political pressure on the government in order to obtain subsidies to pay wages, which usually only prolonged the enterprises' agony. Bankruptcies and liquidation of enterprises entailed different problems, because employees' claims were not secured against specific assets (like many bank loans), which meant that the likelihood of their fulfilment was low. An additional problem was that the employees whose employers failed to pay the contributions into the social welfare system associated to wages were denied health coverage – until the Constitutional Court ruled otherwise.

Due to high unemployment, and inefficiencies of judiciary system and state inspectorial agencies, there are several other problematic practices. According to the estimates by the Croatian Employment Service and State Inspectorial Agency, there were around 120.000 people illegally employed in the unofficial economy in 2001²³, which implied a low protection of their rights²⁴. According to the State Pension Insurance Fund, in 2000 around 200.000 workers were reported as receivers of the minimum wage. However, a large number of workers in SMEs seemingly receive the minimum wage because that minimises the associated taxes and social welfare contributions, i.e. the employers' cost of labour. However, when the minimum wage is lower than the market wage for their jobs, such workers also receive additional payments in cash or, more rarely, through fictitious contracts. Due to the differences in taxes and social welfare contributions, such practices

deprive the state budget and its pension and health funds of significant resources. Since the introduction of the private pension funds in 2002, employees (as future beneficiaries of those funds) have been losing resources too. The proportion of workers declared on the minimum wage in 2000 was highest in service sectors low skill jobs prevail²⁵ (Madžarević-Šujster, 2002). Most of the employees on the minimum wage work in small companies, where 17 percent of all employees purportedly received the minimum wage, and the average net wage was 23 percent lower than in the rest of the business sector (FINA, 2003). The employees of the public sector and larger companies are in a much better situation regarding wage rate, job security and employee rights. Finally, there is the issue of the wage discrimination of women. On average, women's earnings are comparatively lower – regardless of their age and duration of employment (Crnković-Pozaić, 2004). On the other hand, the differentials between wages of men and women, which have been observed in 2002 (10 percent)²⁶, were lower than in any other transition country. Moreover, they were small even in comparison with most OECD countries (Šošić, 2004).

Labour Disputes

There were about 35.000 unresolved labour disputes at Croatian courts in 2002. 70 percent of the disputes are linked with wages arrears and other material claims, some tackle unlawful dismissals etc. The burden

²³ The share of unofficial economy in GDP is estimated at around 10 percent.

²⁴ Some of them were simultaneously registered as unemployed because that status entailed certain welfare benefits. The reform of 2002 began to link the benefits to a person's social status, rather than the (un)employment status (UNDP, 2003).

²⁵ These were construction (17 percent), wholesale and retail trade (16 percent) and hotels and restaurants (11 percent).

²⁶ This figure should be treated with caution, because it does not take into account the characteristics of individual employees (e.g. education and experience) or particular jobs (cf. Šošić, 2004).

of ineffectiveness and inefficiency of the judiciary system is disproportionately borne by the low-wage workers. Due to their low negotiating power and weak position in the labour market, they are more likely to face the violations of rights. It is likely that some employers take advantage of institutional inefficiency of the judicial system, knowing that rectification of wrongdoings may not even happen. Engaging in legal disputes is risky and costly, and the problems of the judicial system hinder the opportunities of low-wage workers to exercise their rights and receive compensation for the infringements. Trade unions make attempts to protect that category of workers, but they primarily serve the interests of their members, which mostly come from the public sector and larger companies. Since unionisation is lowest in small firms, where low wages are relatively more common, the protection of their rights is weak. On the other hand, the courts are also processing a large number of lawsuits whereby employees in the public sector, partly assisted by trade unions, sue the government ministries due to the latter's failure to fulfil minor claims embedded in collective agreements. Having tackled 202.812 labour disputes initiated between 1996 and 2003, Crnić (2004) notes a decrease in the number of disputes revolving around dismissals, and a significant increase in the number of disputes initiated by employees because of employees' failure to fulfil specific material claims.

THE EFFECTS OF LABOUR MARKET POLICIES

Although there are no comprehensive data, there are indications that Croatian labour market policies are not sufficien-

tly aimed at improving the position of the worst-off categories of employees and the unemployed. In this section we examine the main effects of passive and active labour market policies on the segmentation of the labour market.

Passive Labour Market Policies

Passive labour policy²⁷ has as a goal the improvement and protection of the material status of the unemployed. The unemployment allowance represents the most significant policy measure in terms of its costs and coverage of the unemployed. According to UNDP (2003), the monetary compensation in Croatia does not vary significantly from the averages of the other CEE countries, regarding the proportion to the average salary (26 percent) and maximum duration of the rights (one year). Furthermore, total expenditure level on passive measures in Croatia, measured as a proportion of GDP, is similar to other transition countries. However, Croatia differs in terms of the lowest coverage of the unemployed (18.5 percent of individuals registered with the Croatian Employment Service receive the allowance). This is a direct consequence of higher youth unemployment rates, who have less working experience. Consequently, their rights to unemployment allowance, if they have it at all, are quickly exhausted. Therefore, it would be justified to increase the number of individuals, especially in the younger age groups²⁸, who would have the right to the unemployment allowance. There is also the need to improve the efficiency of the funds being spent, and to establish links between passive and active policy measures, which would increase the employability of the unemployed persons,

²⁷ Passive policy measures may include unemployment allowance, pension schemes, health insurance, right to child's allowance and various forms of material insurance.

²⁸ Furthermore, an effect in improved position of young people, especially through easier entrance into employment, is expected from the flexibilisation of the Labour Law.

which is particularly pertinent in the case of long-term unemployed, which account for majority of unemployed persons.

Active Labour Market Policies

Active policy measures (ALMP) are used to reach more effective outcomes in the labour market through the removal of imperfections that exist in it, as well as through the modification of market outcomes towards socially acceptable ones. The goal is to increase employment and the wages of particular categories in the labour market that seem to be particularly exposed to the risk of unemployment and poverty. According to UNDP (2003), the expenditure levels on ALMP in Croatia do not differ significantly from the advanced transition countries, but its structure does. In recent years, the emphasis was on wage subsidies, measures stimulating self-employment and small enterprises as well as job search assistance. In OECD and many transition countries, most resources are spent on training programmes, job search assistance and public works. The new cycle of active policy measures, which started in 2002, focused again on subsidising wages, with too strong emphasis placed on young university-educated individuals who constitute only 1 percent of the registered unemployment and are largely well-positioned in the labour market. Furthermore, the measures target 95 percent of all unemployed persons. Non-specific definition of target groups may somewhat increase the overall employment, but it often leads to insufficient creation of employment chances for the most endangered groups. Current results indicate a favourable impact on middle age workers unemployed for at least sixth months, and opportunities for stronger impact on the first-time job seekers who have completed secondary vocational education (Babić, 2003). Given the structural disproportions in the labour market, future ALMP

should be directed towards adjustment of the qualification structure of the labour force in accordance with labour demand, and on (re)training of groups experiencing the most difficulty in finding employment. A systematic evaluation of the effects of ALMP, followed by their adjustment in accordance to needs, should also be implemented.

LABOUR MARKET SEGMENTATION REVISITED

The conditions of employment contracts are governed by laws, collective bargaining, and individual contracts. The level of flexibility of industrial relations is neither economically nor socio-politically neutral. Although laws and contracts are both legally enforceable, they differ in their levels of generality, design processes, flexibility they offer to employers and employees, and in implications for different groups of employees. More general instruments (laws and more centralised collective bargaining) predominantly define the position of relatively vulnerable groups of employees. The better-positioned categories of employees display stronger tendencies towards decentralised collective bargaining and flexible individual contracting. All these institutions require an effective legal system offering not only sufficient legal provisions, but also a prompt resolution of labour disputes and sanctioning of rights violations. Although employee rights seemingly act just as constraints that limit the autonomy of the firm in the labour-related decisions, towards which they may often be opposed. However, such rights have both enabling and constraining aspects – for instance, through positive effects on employee morale or cooperative attitudes of labour unions which facilitate productivity improvements. Any rights need to be rooted in an effective legal system offering not only sufficient legal provisions, but also prompt resolution of

labour disputes and sanctioning of the violations of the employees' rights. The latter is especially important in the cases of the most vulnerable categories of employees.

There are significant deviations from these principles in the reality of the Croatian labour market. There are notable differences in the levels of protection of rights of different categories of employees, with particularly burdensome situations faced by the long-term unemployed. On the one hand, there are the employees in the public sector and larger and more advanced companies, who tend to be highly unionised and occupy relatively secure and well-paid jobs with adequate working conditions (cf. Rutkowski, 2003). On the other hand, there are many employees, mostly in the SME sector, whose rights are more easily endangered and even violated. This is reinforced by the concentration of the SME sector in low-skill / low-value-added activities, which is associated with the weak position in the labour market of such employees. Consequently, despite a relatively more egalitarian wage distribution than in other transition countries, the incidence of low pay is quite high. Over 20 percent of all Croatian employees earn less than two-thirds of the median wage (although this figure could be somewhat inflated by underreporting wages). In the EU countries, that figure rarely exceeds 15 percent (cf. Rutkowski, 2003). Similar patterns of segmentation in terms of relative positions of employees in larger and smaller companies have been observed

in the UK and Ireland, as well as in Southern European countries (cf. Lapeyre and Blassel, 2003), with which Croatia shares some institutional and cultural features. Furthermore, high levels of unemployment in general and long-term unemployment in particular create another group of outsiders - labour market participants who fail to secure any jobs in the official economy at all. Some of the long-term unemployed may be active in the unofficial economy, but the majority of that group forms the segment that occupies the worst-off position in the labour market²⁹.

Labour market segmentation is caused by various factors. There is an underlying tendency, both within corporations and at the societal level, of interest groups capturing their share and ignoring opportunities where co-ordinated strategic restraint from maximal short-term claims could make most actors better off. Firstly, ineffective judicial system makes the rectification of any rights violations difficult and costly. That is particularly problematic for low-wage workers, whose socio-economic status makes it more difficult for them to utilise the totality of their legal rights. On the other hand, their contractual rights are likely to be limited due to their weak negotiating power, unless this problem is moderated by unionisation and collective bargaining. However, unionisation is often ineffective or openly discouraged by the employers, as in the cases of various small-size private employers, as well as larger retail chains. Furthermore,

²⁹ It may be interesting to look at gender and regional differences that could also contribute to segmentation processes. As for gender issues, the differential in employment rates of men and women in 2002 amounted to 13.1 percent. That was somewhat higher than in the EU first wave accession countries, but lower than the average differential in EU countries. However, in this regard men were more strongly affected by transition. Men's employment rate has fallen twice as much as women's employment rate. As indicated above, wage differentials between men and women are persistent but seem to be relatively low, although more precise calculations are needed. On the other hand, there are substantial regional unemployment differences; labour demand is strong only in few counties (Zagreb, Istria and Primorsko-goranska), whereas counties with a large proportion of rural population are particularly disadvantaged. Such conditions are mainly due to extensive regional differences in economic development, which have been amplified by war and low labour mobility. Effective regional policy that could rectify some of these disparities still needs to be developed.

the activities of trade unions and system of collective bargaining are steered in favour of those employed in the public sector and some state-owned companies. For example, the trade unions in state-owned utility monopolies regularly resort to political tactics to gain concessions from the management, and, indirectly, from the government. That has resulted in a privileged position of such employees, effectively prevented restructuring of such companies, and fuelled similar wage claims of the public sector employees. Moreover, the lack of effective dialogue between social partners at various levels prevents focusing on constructive and proactive solutions, and hinders the effectiveness of the attempted labour market reforms. Finally, the economic and social policy measures are unsystematic and often seem to be motivated by short-term political goals. Consequently, they do not address the needs of the disadvantaged employees and the unemployed sufficiently.

CONCLUDING REMARKS

The current introduction of more flexible industrial relations provides an opportunity for rethinking the functioning of the labour market institutions. The levels and structure of unemployment necessitate action, which should include more attention to the processes that govern these institutions. We can expect that the labour market reform in Croatia will follow a pattern usually negotiated in various European countries. This pattern comprises of the following: preservation of the basic system of employment protection (as a safeguard against unfair behaviour), liberalisation of fixed-term, temporary and part-time employment contracts, decentralisation of collective bargaining, reduction of passive labour market policies, and the reallocation of resources towards the active ones (Samek Lodovici, 2000a). Although such reforms are likely to enable an easier entry into the

labour market, they might also exacerbate the existing segmentation tendencies – for example, by loosening the means of the institutional protection of low-skill workers. Unequal distribution of the cost of reforms is a challenge to policy makers whose resolution requires simultaneous attention to economic efficiency and socio-political legitimacy. The effectiveness of labour market reforms depends on their linkages with other policy measures. At least, labour market policies need to be devised and implemented in combination with adequate and consistent policies tackling enterprise development, education, and social policy. The success of reforms also requires a much more effective functioning of social (and particularly judicial) institutions. The effectiveness of the legal system is currently reduced by slowness and occasional inconsistencies, and that creates problems regarding the rectification of wrongdoings.

In the short term, there is an urgent need to improve the system of resolution of labour disputes, which would include more effective mediation and arbitration mechanisms and thus unburden the judiciary. A more efficient resolution of existing labour disputes should serve as a deterrence mechanism against unfair behaviour. Another important issue is the creation of more trust among the social partners in bipartite and tripartite social dialogue at the national, regional and local levels. That could facilitate a more constructive negotiation climate and foster the implementation of a more effective and mutually beneficial system of collective bargaining, as well as co-operation in the achievement of commonly agreed goals. The issue of social dialogue is particularly important for SMEs, which account for a growing proportion of the economy, and for the majority of the newly created jobs. At the same time, the social dialogue in them seems to be rather underdeveloped, and the protection of

employee rights is more problematic. This has to be complemented by restructuring of state-owned enterprises and a reform of the public sector in general. Increasing their efficiency will help curb the differentials between the employees of public and private sectors. Moreover, sustainable increases in labour market demand can only come through enterprise development and attraction of investment. As the example of Ireland demonstrates, that requires adequate economic policy measures coupled with social partnership. However, above else is the need for the highly competent and productive labour force, which requires the provision of opportunities for life-long learning, and the co-evolution of the educational system with the labour market demand. That entails an upgrade of competencies of major institutional players in the labour market (relevant government

ministries and agencies, employer associations, trade unions, Economic and Social Council, Croatian Employment Service, Employment Inspectoral Agencies). Further necessary measures include tackling of the undeclared economy and the improvement of the situation of the working poor. Finally, reconsideration of both passive and active labour market policies seems indispensable, with the aim of creating an integrative approach that will bring about synergies between active and passive policies and measures, as well as periodical evaluation of their effectiveness. Hereby the emphasis should be on the improving the skills, employability and the incentives of the unemployed to actively search for a job. That is especially applicable to the long-term and low-skill unemployed persons, who are in relatively worst-off positions among the unemployed.

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