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LABOUR MARKET FLEXIBILITY AND MIGRATION IN THE BALTIC STATES: MACRO EVIDENCES

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Abstract

The Eastern enlargement of the European Union and the requirements of the European Monetary Union call for increased flexibility of labour markets in both the current EU members and candidate countries. If labour markets and institutions are rigid in the monetary union, market disequilibrium is likely to grow. The present paper aims to give a macroeconomic overview of the Baltic States' labour market in the period 1995–2001, laying emphasis on the issues of labour market flexibility and labour migration in the context of EU eastward enlargement. The Baltic States comprise a particular regional cluster and an interesting case for making generalizations about the processes of transition and EU eastward

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enlargement, and developing a new field of economics — the economics of transition and integration. In real terms, one has to admit, the influence of the Baltic economies on the EU eastward enlargement processes can hardly be significant, as the very small size of the Baltic markets bears no comparison with either the markets of the current EU member states (EU15) or the other candidate countries (CC).

The Baltic States have dutifully observed the main international standards regulating labour relations in accordance with the EU rules. Comparing the Baltic States' labour market with those of EU15 and the other candidate countries, one comes to the conclusion that the Baltic States' labour markets are flexible. The most flexible among them is the Estonian labour market followed by that of Latvia. However, predictably, after joining the EU, the labour markets of the new members may become more rigid due to the increasing influence on them of institutions and trade unions, and due to more generous funding of labour market policies. Moreover, a decline of wage flexibility can be predicted.

Free movement of labour as a natural consequence of EU enlargement will also exert pressure on the Baltic labour markets due to the possible migration of better-qualified and flexible labour force, and cross-border movement of labour within the Baltic Sea Region countries. Coupled with ageing of the population, it may increase shortage of skilled labour. Consequently, if labour mobility increases and labour market flexibility declines remarkably during the enlargement processes, market disequilibrium is likely to grow in the Baltic States as well.

JEL–Classification: J21, J30, J50, J61, J80, H50

Keywords: Labour market flexibility, labour migration, the Baltic States, eastward enlargement of the European Union

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Introduction

The Eastern enlargement of the European Union and the requirements of the European Monetary Union (EMU) call for increased flexibility of labour markets in both the current EU members (EU15) and the candidate countries (CC)[5]. In the conditions of the EMU, following the requirements of the optimal currency area (OCA), the growth of labour market flexibility is unavoidable. Should labour markets and institutions fail to become more flexible, market disequilibrium is likely to grow in both groups of countries.

The EU candidate countries have to combine their transition processes with the accession requirements. Their labour markets deserve special attention because their flexibility may be needed in order to offset asymmetric shocks, especially when other means such as monetary and fiscal policies are constrained. If the labour markets of the accession countries are not able to adapt to the challenges of the monetary union, the convergence process will be hindered. This, in turn, may result in high unemployment and growing labour migration. As a result, social conflicts may occur both in the accession countries and the current EU member states.

The first round of EU eastward enlargement will take place in 2004 at the earliest. Of the former Soviet republics only the Baltic States are presently candidates for EU accession. These States' favourable location between the East and West, their historical and cultural traditions of co-operation with the countries around the Baltic Sea, and the market economy experience they gained in the period between the two world wars are important initial conditions as determinants of the transition affecting the economic development and the EU accession processes of these countries. After regaining their independence in 1991, the Baltic States' governments have followed almost similar principles in their economic policy as

[5] The candidate countries (CC10) are Hungary, the Czech Republic, Slovenia, Poland, Slovakia, Estonia, Latvia, Lithuania, Romania, and Bulgaria.

those which guided solving the following main tasks: 1) liberalization of prices and gradual elimination of all state subsidies; 2) privatization of state-owned enterprises; 3) introduction of a separate currency by means of a currency board system (Estonia and Lithuania) or regular pegs (Latvia); 4) maintaining a conservative fiscal policy; 5) implementing a comparatively liberal foreign trade regime (Estonia).

The Baltic States provide an interesting case for making generalizations about the processes of transition and EU eastward enlargement and thus helping to develop a new field of economics — the economics of transition and integration. In real terms, the influence of the Baltic economies on the EU eastward enlargement processes cannot be significant, the very small size of the Baltic markets bearing no comparison to the markets of the EU current member states or the candidate countries. The Baltic States' population is only 2% of that of EU15 and 7.4% of that of CC10. Their GDP forms about 0.3% of that of EU15 and 6.3% of the total CC10 GDP. The level of GDP per capita (PPP) is only about 30% of the EU15 countries' respective indicator (34% in Estonia, 26% in Latvia and 28 % in Lithuania) (Straubhaar, 2001) (*Ibid*).

The present paper aims to throw light upon the main changes in the Baltic States' labour market, laying emphasis on the macro evidences of labour market flexibility and labour migration in the context of EU eastward enlargement. Both issues have a remarkable impact on the European labour market, which obviously varies in different regions. Our empirical analysis is mainly based on the data available from the statistical offices of the Baltic States and various international organizations (ILO; World Bank, Eurostat, etc). The period under investigation is mainly 1995–2001.

In Sections 2–4 of the paper various aspects of labour market flexibility are discussed. On the macro level, labour market flexibility can be divided into institutional flexibility and wage flexibility. Institutional flexibility characterizes the extent to which state institutions and trade unions are involved in the regulation of the labour market. Wage flexibility shows how responsive wages are to market fluctuations. High institutional involvement may lead to a decrease in labour market flexibility. If trade unions are weak,

wage flexibility is usually high. Following that underlying logic, the discussion of institutional flexibility (Section 3) precedes the section on wage flexibility (Section 4). Labour migration problems are discussed in Section 5, laying emphasis on the push and pull factors of migration and on the analysis of the labour migration experience during the previous stages of EU enlargement. The possibilities for cross-border movement of the Baltic States' labour force are likewise discussed.

1. The concept of labour market flexibility

The term 'labour market flexibility' has been defined variously. Wage and employment flexibility are rather intuitive concepts, but there are also numerical versus functional flexibility, internal versus external flexibility and, for the most exigent, the intensive versus extensive margins of flexibility. Indeed, the term 'labour market flexibility' has got so many definitions that the user may start to suspect that he/she is grappling with a catchword devoid of any theoretical rigour.

However, this is not entirely the case. From the point of view of general equilibrium theory, perfect flexibility may be thought of as a situation in which all the resources on a given market are allocated in a Pareto efficient way (Hahn, 1998). But it could also be asked whether we approach this term as characterizing a state or a process. The term 'flexibility' seems to be more appropriate for describing a process. For instance, a market is more flexible than others if it moves faster towards Pareto efficient resource allocation. In principle it means that we use the framework of the neoclassical equilibrium model and any kind of intervention in the labour market will slow down the adjustment speed. So, we can say that labour market flexibility shows the speed of adjustment to external shocks and changing macroeconomic conditions.

This definition is very broad and measuring such effects as adjustment speed is empirically very difficult. Therefore, for practical reasons this term has a wide range of applications. For example, Treu (1992) considered numerical (or external) flexibility, i.e. the freedom employers enjoy to expand or contract their workforce as

they wish and to employ workers on a temporary or part-time basis; working time flexibility, functional flexibility; and pay flexibility. In what follows these terms are presented and explained using examples from the EU.

- The issue of employment protection, in particular the regulation of dismissals, has been widely discussed. The European labour relations systems, which all have some institutionalised arrangement of protection against dismissal provided both by law and by collective agreement, have been contrasted at length with the extreme models presented by the United States, traditionally characterized by the legal freedom to dismiss (Grenig, 1991), and Japan, well known for its practice of lifetime employment, at least for the core labour force (Dercksen, 1989). This picture would be misleading if we failed to consider the various forms and growing incidence of "atypical" employment. The introduction of different types of employment contract has probably been the major development in European law and practice in the labour field during the past 15 years and has played a leading role in increasing labour market flexibility (Kravaritou-Manitakis, 1988).

- Working time was another important and controversial testing ground for flexibility in Europe, particularly in the late 1970s. Far-reaching changes have taken place in this area, possibly even greater than those in the area of employment protection (Treu, 1989). The initiative for change came mostly from employers. Although the trade unions initially reacted defensively, eventually there emerged the outlines of a consensus on the needs and values of a workforce that now contained more women and more people working in the tertiary sector. However, the trend towards more flexible working patterns was also influenced by unions pressure for reduced working hours, which met with considerable (and continuing) success in a number of countries (Treu, 1992)

- Functional flexibility involves a reversal of the division of labour and the fragmentation of work organization which were typical of the traditional production-line model; this is achieved both by extending the range of tasks and skills involved in a job

and by increasing internal mobility. The traditional rigidities attributed to European labour relations in this area derive not so much from legal restrictions as from management and union practices, which reflect the basic nature of labour-management relations in Europe and of company strategy and organization. For this reason they have been called "built-in rigidities" (Boyer, 1988; Dore, 1986). Functional flexibility has come to be widely accepted and practised throughout the European Union. Research evidence suggests that there was a significant trend towards greater functional flexibility throughout the 1980s (Bamber, 1989).

- Wages have not remained untouched by the pressures for greater flexibility. Indeed, companies have repeatedly blamed their failure to adjust to turbulent markets on the complexity and rigidity of wage structures. In Europe wages are determined mainly through collective agreements, so here too introduction of flexibility has been a major task for the social partners. However, legislation has also played some part in reducing certain forms of automatic wage increase, particularly indexation. In the 1980s indexation came under attack as a major factor contributing to inflation, and in most countries its use was gradually reduced, if not abolished, under the combined influence of legislation and collective bargaining.

Nickell (1997) pointed out three aspects of labour market flexibility: employment protection, labour standards, and labour policy. The employment protection index was drawn up by the OECD and is based on the strength of the legal framework governing hiring and firing. The labour standards index refers to the strength of the legislation governing a number of aspects of the labour market. Labour policy was divided into active and passive labour policy. Benefits systems were characterized by replacement rate, showing what share of income is replaced by unemployment benefits, and the duration of receiving these benefits. Active labour market policies refer to expenditures on activities for the unemployed that are geared to help them back into work (labour market training, assistance with job search, subsidized employment and special measures for people with a disability).

The most common interpretation of labour market flexibility is connected with labour market regulations and institutions (e.g. Siebert, 1997; Berthold, Fehn, 1996; Jackmann, Layard, Nickell, 1996; Lazear, 1990). All the OECD countries have rules and regulations governing the employment relationship between workers and firms. Those referring to hiring and firing practices are often referred to as employment protection legislation (Boeri *et al*., 2000). These rules and regulations govern unfair dismissals, restrictions on lay-offs for economic reasons, compulsory severance payments, minimum notice periods, and administrative authorizations.

Many empirical studies have sought to assess the effects of various types of state intervention in employment, including unemployment benefits, financial support for employment and the minimum wage. The results are disappointing for the defenders of the flexibility approach: both the analyses focusing on the policies that affect labour cost and those considering the impact on the replacement ratio at least yield contradictory results, if they do not actually clash with the expectations of flexibility theories (Gregg, Manning, 1997).

On the labour demand side, it has been estimated that wage subsidies intended to save jobs or to create new ones actually involve "dead weight and displacement effects amounting to 75–90% of outlays, implying that only 10–25% of expenditure generates a net job gain" (Employment in Europe, 1996). There is complete disagreement on the actual efficiency of the policies aimed at enhancing the elasticity of labour supply. Unemployment benefits (guaranteed for long periods) appear to play an important role in explaining persistent unemployment in some studies (Ball, 1996; Jackman *et al*., 1996), but not in others (Revenga, Bentolila, 1995; Blanchard, Jimeno, 1995). Reduction of firing costs, as well as the bargaining power of insiders are important for Revenga and Bentolila (1995), but not for Jackman *et al*. (1996) who argue that reducing the degree of employment protection would in fact lead to a reduction in long-term unemployment, but also to an increase in short-term unemployment, with a scant effect in terms of any net increase in employment. Modest effects would also be obtained (according to Jackman *et al*., 1996) by reducing social security

contributions and working hours, while active policies aimed at retraining and help in job search would have a positive effect. Finally, no definitive result has emerged from the now extensive theoretical and empirical literature about the effects of a minimum wage on employment (Simonazzi, Villa, 1999).

Although the question of whether and to what extent job security regulations adversely affect labour market flexibility remains a matter of continuing controversy, critics have claimed that strong job rights will prevent employers from adjusting to economic fluctuations. It has also been alleged that by inhibiting layoffs during downturns, strong job security provisions will reduce employers' willingness to hire during upturns and thereby contribute to unemployment (OECD, 1986). For instance, if employment protection legislation leads to a lasting work relationship, it may encourage employers to provide training to workers with potentially beneficial effects on human capital and labour productivity. A better skilled worker may also increase internal (functional) flexibility and thus lead to a better functioning of production activity (Piore, 1986).

Several empirical studies have tried to measure the effect of job security legislation on labour market outcomes. Bentolila and Saint Paul (1992) used the "before and after" approach to analyze the Spanish case, showing that labour demand fluctuated more in response to output shocks after flexible employment rules were adopted.

If we consider the tightness of a country's employment protection legislation as a proxy for labour market flexibility, we can see that Western European countries have relatively inflexible labour markets (Bertola, 1990; Grubb, Wells, 1993). A group of experts with a background in business, labour, and government formed by the OECD identified six categories of labour market flexibility and made recommendations for each (OECD, 1996).

- Labour costs: avoid mechanisms, whether institutional or automatic, that would lead to wage increases that are greater than productivity increases.

- Conditions of employment: strike a balance between the workers' desire for job security and the need for economic efficiency.
- Work practices and work patterns: modify the organization of work to enrich the work content and raise levels of skills to provide increased flexibility in the arrangement of working time.
- Rules and regulations: apply rules and regulations in a reasonable manner and reassess their direct and indirect impact at regular intervals.
- Mobility: remove obstacles to mobility such as non-transferrable pension arrangements and rigid housing markets.
- Education and training: improve initial schooling, strengthen retraining programmes, and publicize the importance of lifetime learning for a flexible society.

While the previous sections show that there exists a host of understandings and interpretations of the flexibility concept, we will next try to present an idea about how these different flexibility interpretations are interrelated and connected with general labour market behaviour. At the beginning, some simplifications will be made. Firstly, we will concentrate on the transition economies' labour market; secondly, we will assume that restructuring and labour reallocation are dependent on labour market flexibility, i.e. more flexibility means faster restructuring and reallocation[6]. Thirdly, we will draw our theoretical framework from OST (Optimal speed of transformation) literature, first introduced by Aghion and Blanchard (1994).

Aghion and Blanchard found that these countries which had a large initial shock and thus a large increase in unemployment, were likely to restructure more slowly. We can conclude from their model that gradual implementation of reforms is the best policy

[6] This phenomenon characterises labour markets in transition economies. The dependence has also the opposite direction, if the market situation has stabilised, also institutional stability is achieved, then reallocation and restructuring will slow down and finally we can see fewer flows in the labour market and less flexibility. In a way we can say that less flexibility indicates that restructuring and reallocation (needed for transformation) will soon be over.

option. According to them, transition is shaped by two main mechanisms: reallocation and restructuring. Reallocation means changes in employment structure, how labour is allocated between sectors. Restructuring here means not only changes in the structure of ownership, but also changes in the structure and organization of production. Firms must redefine their product lines, close some plants that are no longer needed and lay off the workers in those plants. Also they must replace most of their equipment and train/replace the managers.

Both reallocation and restructuring are dependent on labour market flexibility. Via labour reallocation and restructuring, an economy will reach Pareto optimum resource allocation, which means efficient use of resources and higher productivity. Comparing two economies, transition to higher productivity appears to be faster in the economy with a less rigid labour market. As far as most transition economies are concerned with convergence and catch up strategies, the issue of labour market flexibility becomes crucial for them. We believe that higher flexibility means lower unemployment, because the matching process is more successful and as a result we have less long-term unemployment than in rigid labour markets.

These are extremely important aspects for the candidate countries. From different sources we can learn that the catch-up process with the EU average income level may take the Baltic States a minimum of 16 to 35 years (Boeri, Brücker, 2001). Hence, if the labour market stays relatively flexible, it will help maintain high GDP growth rates and thus speed up the catch-up process. On the other hand, some authors claim that at least on the micro level the labour market flow rates have already declined, which means an increase in the stagnant pool of unemployment and less flexible labour markets (Eamets, 2002b).

We argue that labour market flexibility should be measured at two distinct levels: the macro level and the micro level (see Figure 1). The former can be further divided into institutional and wage flexibility. The institutional flexibility of a labour market denotes to what extent state institutions and trade unions are involved in the regulation of the labour market. Wage flexibility shows how re-

sponsive wages are to market fluctuations. Micro level flexibility relates to labour market flow analyses. A labour market can be characterized by various flows of transitions to and from employment, unemployment and non-participation, as well as flows of job creation and job destruction.

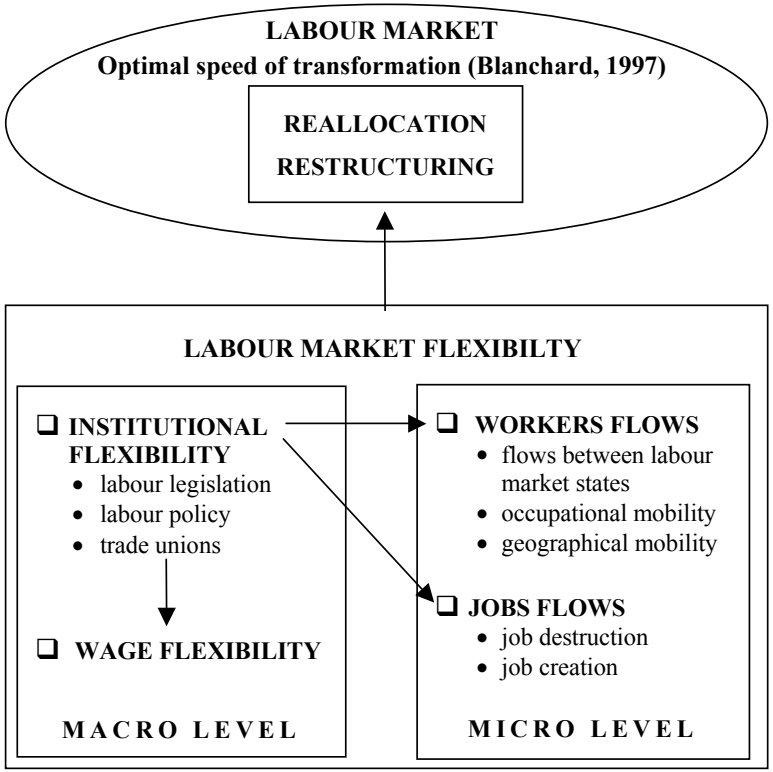

Figure 1. The concept of labour market flexibility. (Eamets, 2002a)

In practice different aspects of flexibility are interrelated, presumably in a hierarchical way. If institutional involvement is very high, workers' transition rates are likely to be low. If trade unions are weak, then wages are more flexible. Thus, macro level flexibility can partly be measured via the indicators of micro level flexibility.

While it is generally difficult to quantitatively measure institutional involvement (although quite a few indexes have been constructed), it is much easier to measure workers flows, job creation and job destruction.

Because of limited space, this paper's focus is on the macro side of labour market flexibility. The other reason for this is the difficulty to obtain comparable micro level data about labour market flows in all the three Baltic States.

2. Institutional flexibility

2.1. Labour market regulations

This part of the paper will review the labour market legislations of Estonia, Latvia and Lithuania by their effect on labour market flexibility, discussing issues such as regulation of dismissals, regulation of work time and wages, and social protection of the unemployed. If not stated otherwise, similar provisions are valid in all the three Baltic countries.

In general there are five sources of legal regulation of labour relations in the Estonian, Latvian and Lithuanian jurisdictional systems: 1) international conventions, 2) Constitution, 3) laws 4) decrees and regulations of administrative authorities, 5) collective agreements. The regulation of employment relations mainly corresponds to international standards: the most important ILO conventions are ratified and the legislation assures the protection of employees' rights in terms of work time, work remuneration, holidays, and in case of termination of contracts. There are several measures to protect employees in less favourable conditions, such as old age employees, pregnant women and women with children, persons with a disability, etc.

In all the three countries the work relations are governed by the employment contract (except for people working in civil service) (The Republic of Latvia Labour Law; Republic of Lithuania Law on the Employment Contract; The Republic of Estonia Employment Contracts Act). On the one hand, there are several similarities across the Baltic States: the laws prohibit differential treatment,

there exist upper limits for regular work time, overtime and work during night-time, workers are granted regular leaves of absence and other holidays, termination of employment contracts is subject to restrictions such as the obligation to give advance notice, pay compensation, etc. Regarding the presence of such provisions, the Baltic States' labour legislations resemble that of the EU countries. On the other hand, there are some differences in the regulation measures between the Baltic States themselves. For instance, in Lithuania the legal regulation has a more adverse impact on labour market flexibility than in Latvia: a higher minimum wage, a longer advance notice period and bigger compensations if the employment contract is terminated on the initiative of the employer.

The notification period varies in Latvia from 10 days (employee's misconducts) to 1 month (lay-offs). In Lithuania the period is 2 months (4 months for minors, parents of children, etc.). In Estonia the notification period varies from 2 weeks (long-term incapacity for work) to 4 months (lay-off of workers who have continuously worked for the employer over 10 years). The compensation for the termination varies in Latvia from 1 to 4 months, the average wage depending on the employee's work experience with the present employer (according to the Labour Code valid until 1 June 2002, the compensation was no less than 1 month's average pay and the notification period was 1 month). In Lithuania the compensation varies from 1 to 12 average monthly wages, depending on the reason of termination and the length of work record with the present employer. In Estonia the compensation for termination varies from 1 to 4-months' average wage.

The aggregate indicators of employment protection regulations

In order to generalize the above information and to compare how strict the regulation of labour relations is across the Baltic States and European countries, summary indicators were calculated, following the methodology of Nicoletti *et al*. (2000) who, using the data available about most OECD countries, applied the methodology for assembling detailed indicators into summary indicators of the strictness of regulations. To aggregate the information, they used factor analysis in which each component of the regulatory

Table 1

Advance notice periods and severance pays in the case of dismissals in the Baltic States

Length of record with the present employer	Estonia		Latvia		Lithuania	
	Notice period	Severance pay	Notice period	Severance pay	Notice period	Severance pay
Up to 5 years	2 months	2 months' average pay	1 month	1 month's average pay	2 months	2 (4) months' aveaverage pay
5–10 years	3 months	3 months' average pay	1 month	2 months' average pay	2 months	3 (6)months' average pay
10–20years	4 months	4 months' average pay	1 month	3 months' average pay	2 months	4 (8) months' average pay
More than 20 years	4 months	4 months' average pay	1 month	4 months' average pay	2 months	6 (12) months' average pay

Source: The Republic of Estonia Employment Contract Act; The Republic of Latvia Labour Law; The Republic of Lithuania Law on the Employment Contract. Note: In Lithuania the higher severance pays (numbers in parentheses) are applied in cases of lay-offs other than liquidation of firms, reduction of production, etc.

framework was weighted according to its contribution to the overall variance in the data. Factor analysis revealed families of detailed indicators that were most associated with different unobserved factors. As a result, countries can be "scored" on each of the factors, using the estimated weights in accordance with the cross-country variance explained by the factor. Here we use the same weights for assembling the data on the Baltic Countries into aggregate indicators.

The calculation of the index proceeds as follows. The regulations on working under regular contracts are divided into three areas:

- Procedural requirements (the delay before the notice of dismissal can start; whether a written statement of the reasons for dismissal must be supplied; whether a third party must be notified).
- Notice and severance pay (for three different tenure periods — 9 months, 4 years and 20 years).
- Difficulty of dismissal (treatment of unfair dismissal, regulation of a probation period).

Indicators of the stringency of the employment protection legislation (EPL) for temporary contracts focus on regulations for fixed-term contracts and for contracts under temporary work agencies (TWA). For both contracts, the following elements were considered:

- "Objective" reasons under which a fixed-term (or a TWA) contract could be offered.
- The maximum number of successive renewals.
- The maximum cumulated duration of the contract.

Individual indicators were first estimated on the scale of 0 to 6. After that they were aggregated into factors, thereafter all the factors were weighted and summed into an aggregate indicator. The results are shown in Table 2. For more details about the calculation see also Appendix 1 and Appendix 2. The index measuring the legal restrictions applied on individual dismissals shows that in Latvia the dismissals are less regulated than in Estonia and Lithuania. The value of the index for the Baltic States is higher than the average for the European Union, which means that, compared to the EU, dismissals do not seem to be less regulated in the Baltic States.

On the other hand, the use of fixed-term contracts is less restricted in the Baltic States, their use in Lithuania being even less restricted than in Latvia and Estonia. So the use of fixed-term contracts may counterbalance the negative effect of restrictions on dismissals on labour market flexibility. Though the law allows fixed-term contracts to be used for short-term temporary work, it has been indicated for Estonia that fixed-term contracts are often used for non-temporary work as well.

The status of civil servants

In the Baltic countries the status of civil servants is regulated by separate laws, therefore employment contracts 'shall not be concluded with civil servants' (The Republic of Latvia State Civil Service Law (1 Jan. 2001); Public Service Act (1 Jan. 1996); The Republic of Lithuania Law on Public Service (8 June 1999)). So civil servants have some advantages, but are also subject to additional duties. The positions of civil servants are grouped into categories and civil servants are given grades (Lithuania, Estonia) or qualification categories (Latvia). Regarding civil service positions, there are several restrictions which, being similar across the countries, are related to citizenship, command of the official language, education, and age.

Civil servants are paid salaries according to their grades, qualification categories and levels of position. They are granted annual leave of absence and other vacations and leaves. They are entitled to special benefits in case of death or work accident; have the right to get their training and improvement of professional qualifications financed from the state, municipal, or other budgets. For public servants there are special restrictions and duties, limiting their possibilities for part-time work elsewhere, political affiliations (Estonia), responsibility for lawfulness of their actions or failure to act (Latvia), etc. So we can conclude as a generalization that the status of public servants is more heavily regulated than the status of employees working under employment contracts.

Table 2

The index measuring the restrictions on dismissals for regular contracts and the use of fixed-term contracts

Index	Country								
	Latvia	**Lithua-nia**	**Esto-nia**	**Average of the Baltic states**	**Average of the EU (1998)**	**Ger-many**	**United Kingdom**	**France**	**Italy**
Regular contracts	2.8	3.2	3.3	3.1	2.4	3.0	0.1	2.5	3.0
Fixed-term contracts	1.8	1.1	1.1	1.3	2.3	2.5	0.3	3.7	3.6
Average	2.3	2.2	2.2	2.2	2.4	2.8	0.2	3.1	3.3

Source: Authors' calculations; Nicoletti, 2000.

Note. The average is here a simple average of the indexes for regular contracts and fixed-term contracts. The same method for comparing strictness of labour market regulations was also used by Järve (2002), but he obtained 2.4 for the average of the indexes for Estonia. In our opinion, this difference from our results is due to deviations from the methodology of Nicoletti *et al*. (2000) in his work.

The alignment of labour legislation with the EU labour law acquis

Although all countries have taken steps towards harmonizing their labour regulations with the EU requirements, there are still some efforts to be made before enforcement of the *Acquis Communautaire* in the field of labour law. The report of the European Commission noted that although Estonian legislation is to a considerable extent in line with the *acquis*, some progress is yet to be made in areas such as gender quality and prohibition of discrimination. Also directives related to involvement of workers in the European Company, and regarding information and consultation of workers should be transposed (Regular Report on Estonia's…, 2002). Latvia's alignment, on the other hand, is well advanced (the new labour code transposing the majority of the labour law *acquis* entered into force in June 2002), but efforts are required in order to transpose the directives related to involvement of workers in the European Company and regarding information and consultation of workers, amendments to the Labour Dispute Law have to be made. Enforcement of the *acquis* in the fields of equal treatment of men and women, and in health and safety at work should be improved (Regular Report on Latvia's…, 2002). Lithuania has reached an advanced stage in the area of labour law (the new Labour Code adopted in June 2002 transposes the bulk of labour law *acquis*); there are still several directives that need to be transposed (those of the European Works Council, posting of workers, involvement of workers in the European Company, the right to information and consultation of workers). Lithuania is well advanced as far as equal treatment of men and women, and health and safety at work (Regular Report on Lithuania's…, 2002) are concerned.

To sum up, the labour regulations of the Baltic States may, at least in some respects, have a negative effect on labour market flexibility. In particular, the restrictions on dismissals for regular employment contracts are quite severe compared to the EU countries' average (the more unconstrained use of fixed-term contracts may counterbalance this negative effect). On the other hand, the Baltic countries have already made good progress towards harmonizing their labour regulations with the EU requirements; although some

steps are still to be made, no big changes are expected any more in the near future. Consequently, the imminent joining with the EU will have no adverse impact on labour market flexibility.

2.2. The role of trade unions

In what follows the role of trade unions in the Baltic States will be discussed. The aim is to give an overview of the trade unions and their development in the Baltic States, discussing the issues of union membership, collective bargaining levels and coverage by collective agreements.

Union density

In most Western and Northern European countries, trade unions have a significant role in wage determination. Even though the number of unionized workers varies greatly among the European countries, from almost 80% of employees belonging to the unions in Northern Europe to less than 20% in Southern Europe, collective agreements are usually extended to non-unionized workers, too. In the Baltic States as well as in the other Central and East European countries the role of trade unions is less important.

Table 3

Union density (%)

Country	Union density	
	1995	1996–2001
Slovenia	60.0 (1)	63.5 (2)
Slovakia	61.7 (1)	35 (3)
Czech Republic	42.8 (1)	30 (4)
Estonia	36.1 (1)	16 (5)
Latvia	30 (1)	25 (6)
Lithuania	40 (1)	15 (6)

Source: (1) — Riboud *et al*., 2002; (2) — Vodovnik, 1999; (3) — Joint Assessment of Employment Policy Priorities in the Slovak Republic, 2001; (4) Vaughan, Whitehead, 1998; (5) Confederation of Estonian Trade Unions; (6) Antila, Ylostalo, 1999.

The Central and Eastern European countries are rather homogeneous in terms of wage bargaining coordination and the role of trade unions. The importance of trade unions[7] has been decreasing in all the CEE countries since the 1980s. If at the end of the 1980s the whole labour force were trade union members, then by the middle of the 1990s the number had dropped to 30–60 %. At the end of the 1990s, trade union density was under 35% in all the transition countries except Slovenia.

In the following part we will discuss the role of the unions in the Baltic States.

Unions in Estonia

There are two central trade union organisations in Estonia with the overall membership of about 16% of the body of employed persons: The Confederation of Estonian Trade Unions, which organises both workers and salaried employees, and the Confederation of Estonian Employees Unions which concentrates its organising efforts on salaried employees. The Confederation of Estonian Trade Unions, the so-called trade union of blue-collar workers, was established in 1990 and is the largest of the central union organisations, consisting of 24 branch unions with less than 58 000 members. The Confederation of Estonian Employees Unions, established in 1992, is the organisation of trade unions of white-collar employees and consists of 9 branches with altogether approximately 40 000 members. There are more trade unions in the public sector. The largest unions are in industry, the energy sector and transportation. There are some sectors where unions are missing, for example, banking (where union membership is low in all the Baltic States), and construction and services. In Estonia, unions exist mostly in the sectors with women workforce, which causes the larger share of women among union membership. Also, there are basically older workers in the unions — the average union member being 40 years old.

[7] The importance of unions is measured in union density and union coverage. Union density is the number of salaried workers belonging to the trade union. Union coverage is defined as the collective agreement coverage of salaried workers.

Unions in Latvia

Latvia appears to be more highly organized than Estonia and Lithuania. One fourth of Latvia's 800,000 employees have joined the unions. (Latvia's only central trade union organization is LBAS — Latvijas Brivo Arodbiedribu Savieniba.) The public sector's level of organizing is higher than that of the private sector. 60 % of the organized labour force consists of women. The largest is the teachers' union, followed by two healthcare sector unions. The main sectors with trade union membership are healthcare, education, transport, communication, public services, agriculture, food and fishery, industry, energy and construction. Although union membership fell sharply in Latvia in the 1990s, this process has recently stopped. The decrease resulted mainly from the splitting up and privatization of large state enterprises and collective farms, but currently in Latvia there is a new mood of optimism among young people joining the unions (Antila, Ylostalo, 1999).

Unions in Lithuania

Lithuania has four central trade union organizations with a total membership of about 15% of all employed persons. These four organisations, the largest among them being the Lithuanian Free Trade Unions Confederation, are not cooperative and are keeping their distance. The main sectors where trade unions are active are healthcare, transportation, construction, railway, agriculture, trade, education and civil service.

In conclusion, measured in union membership and compared with other EU or CEE countries, trade unions in the Baltic States are rather small. In the following part trade unions will be analyzed by their coverage and the levels of collective agreements.

Wage bargaining levels and coverage by collective agreements

Even more important than the number of unionized workers is the coverage by collective agreements. In Western European countries, union coverage is usually much larger than the actual number of union members (with the extreme example of France and Spain where less than 20% of employees belong to unions but about 80% are covered with collective agreements). In most Western European countries at least two thirds of the employed persons are cov-

ered with collective agreements. The surprising evidence from the Baltic States as well as from the other transition economies shows that coverage by collective agreements usually does not differ much from union membership. The result might be partly due to the missing data of collective agreements, because until recently collective agreements were not registered. The other reason for low collective agreements coverage is the small number of sectoral level agreements. The levels of collective bargaining in the Baltic States will be discussed in the following part.

In the Baltic States, as well as in the other transition economies, collective agreements are more common at enterprise or national level, the bargaining process at sectoral or regional level is less developed (Casale, 1997, 1999). The minimum wage is decided at national level. The popularity of national level wage bargaining is probably caused by the traditional coordinating role of the government. The larger scale of enterprise level bargaining compared to that at sectoral level is due to less organized employers.

The state or national level bargaining

The Baltic States introduced national level bargaining already at the beginning of the transition process. National level bargaining takes place mainly in tripartite bodies, which include representatives of the government, employers and unions. One of the main tasks of national level bargaining is to decide the level of minimum wage. Other questions in the bargaining have been reforms of labour market legislation, social reforms and pensions. However, the importance of unions even in national level bargaining is rather marginal and the main function of tripartite bodies is consultative.

Regional level bargaining

Regional level bargaining is not developed in the Baltic States (with the exception of a sectoral level agreement concluded in Ida-Viru county, Estonia, which is characterized by a very high unemployment rate and only large enterprises). In general, social partners in the Baltic States have a weak regional structure; in some cases there are no local organizations. One of the main reasons for the lack of regional level bargaining in the Baltic States is the small geographical unit.

Sectoral or branch level bargaining

Sectoral level bargaining is also rather rare in the Baltic States. According to estimates, sectoral level agreements cover about 10–17% of the workers in the Baltic States. Their aim is usually to provide minimum standards. In some cases they are only wage agreements, fixing the minimum wage in the sector. As mentioned before, the main problem in sectoral level bargaining is weak employer associations. It has been noted that trade unions have been helping to establish employer federations at branch level to have the social partner in the negotiations. It is expected that sectoral level bargaining will develop more when employers organize themselves.

Most of the sectoral level bargaining takes place in the public sector or sectors with large privatized enterprises. For example, Latvia has sectoral agreements covering energy, nursing and healthcare, construction, education, culture, forestry, food industry, trade and fishing. In Estonia sectoral level agreements exist, for example, in forestry, energy, transport, healthcare and education. In Lithuania sectoral level agreements are least developed in the Baltic States. There are only a few examples of sectoral agreements in Lithuania (compared to 26 agreements in Latvia and 13 in Estonia in 2000), for example, the agreement in telecommunications industry (Due, Mailand, 2001).

Enterprise level bargaining

Besides national level agreements, enterprise level agreements are most common in the Baltic States. The initiative to bargain is usually taken by trade unions. It should be noted that employers are not interested in concluding collective agreements but are under a legal obligation to conclude them if their employees wish to do so. In practice there are often disputes where employers attempt to avoid signing agreements. Most enterprise level agreements are concluded in the public sector, in large public sector enterprises or in privatized enterprises. Enterprise level bargaining is remarkably less developed in foreign companies (Due, Mailand, 2001).

The estimates about enterprise level agreements coverage in the Baltic States vary.

- According to Due and Mailand (2001), the coverage by collective agreements in Estonia is 6–14%. According to the data from the largest union in Estonia, in the year 2000 about 14% of the workers were covered by enterprise level collective agreements. (According to the same source, 16% of employed persons in Estonia are trade union members.)
- In Latvia Due and Mailand (2001) report the coverage to be 10–30%. (They report the rate of unionization to be 10–40%. According to Antila and Ylöstalo (1999), Latvia is the Baltic country with the highest rate of unionization — 25%.)
- In Lithuania Due and Mailand (2001) report the coverage to be 10–30%. (Antila and Ylöstalo (1999) report the union density in Lithuania to be 15%.)

It can be concluded that trade unions in the Baltic States are rather small in terms of both union density and collective agreements coverage. Collective agreements are more common at enterprise level or national level. At sectoral or regional levels, the bargaining process is less developed. We can thus conclude that most employees in the Baltic States rely on individual employment contracts. As most employees are not covered by collective agreements, the effect of labour unions on labour market flexibility is currently very minimal.

The main reasons for the minor importance of unions in the Baltic States can be found in the general labour market developments. In the 1990s, industrial employment in the Baltic States declined drastically, which directly led to a drop in union density, because in the Baltic States, like in most other countries, in the service sector unionization rates are generally lower. The increase in the number of small enterprises, where due to the small number of employees unions are generally more rare, has also led to lower union membership. The general trend of decreasing union membership has been causing the organizations financial problems. And finally, one of the most important reasons that has decreased the bargaining power of unions in the Baltic States is the rising unemployment during the past decade.

In the future, for example, upon joining the European Union, the role of trade unions in determining wages can grow in the Baltic

States' labour markets, causing labour market rigidity. Especially considering that the incentives of the EU labour unions are trying to increase the strength of unions in the Baltic States. Yet, in view of the historical pattern of the development of unions and the large share of small enterprises, a sharp increase in the influence of unions in the Baltic States is rather unlikely.

2.3. Labour market policy

Public spending on labour market programmes absorbs significant shares of national resources in most EU members and candidate countries. For analytical purposes, the spending is split into "active" and "passive" measures. The former comprise a wide range of policies aimed at improving access for the unemployed to the labour market and jobs, job-related skills, and the functioning and flexibility of the labour market, while the latter relate to spending on income transfers. The first sub-section will examine the overall funding of labour market policies, in particular the financing of passive policies (insurance against unemployment). The second sub-section will highlight the active labour policy instruments and their implementation in the three Baltic States. The final sub-section will compare the three states with the EU, making assessments and drawing some conclusions.

Passive labour market policies

Table 4 provides a synopsis of the dynamics of labour market expenditures in the Baltic States. In 2001, the expenditures on labour market policies in Estonia accounted for 0.22% of the GDP. The respective figures of Latvia and Lithuania were 0.64% and 0.36%. In Estonia, state allocations for labour market measures have been growing steadily and the major part of the increase has been used to fund the mounting need for benefits. As a result, the share of passive measures in the overall employment policy budget swelled substantially between 1995 and 2001 (from 40.5% to 61.5%). In Latvia, on the other hand, state allocations for labour market measures have been volatile. Expenditure on passive measures has increased considerably, now absorbing the major part (up to 80%) of the total. As a result, the share of passive measures in

the overall employment policy budget has increased substantially since 1995 (in 2001, only 22% of the total expenditure on labour market measures was spent on active measures). Compared to Estonia, Latvia's volume of expenditures on passive measures is remarkable (0.42–0.86% of the GDP) due to their relatively high average unemployment benefits (in the year 2000, 45.30 LVL or 160 EUR). In Lithuania, too, passive measures dominate over the active (41% versus 34.1%). The share of expenditures on labour market institutions is 24.5%, which is well above the respective Estonian indicator (10%).

Status of unemployed persons in the Baltic States

In all the three Baltic States the status of unemployed people is legally regulated and they have several rights (Republic of Lithuania Law on Support of the Unemployed (15 Jan. 1998); Republic of Lithuania Law on Vocational Education and Training (7 July 1999); Social Protection of the Unemployed Act (1 Jan. 1995)). But there are certain criteria that need to be fulfilled before one can acquire the status of an unemployed person (registration at the state employment agency, previous employment record (in Estonia), etc.) Having acquired this status, the person is entitled to unemployment benefit and vocational training (with a training allowance in Lithuania and Estonia); he/she also has the right to participate in paid public works and to get free labour exchange services in looking for job. The unemployed have duties such as 1) to look for a job, 2) to attend state employment service, 3) to attend active labour market measures. Additional guarantees are available to certain groups of people (persons under 16, women with children, persons within 5 years to becoming eligible for an old-age pension). For instance, in Lithuania employers of up to 5% of the total number of employees may be prescribed employment quotas to provide such individuals with work. The comparison in Table 5 below reveals that unemployment benefits are biggest in Latvia, followed by Lithuania and Estonia. All the three countries calculate their benefits differently. While Estonia applies the flat rate, in Latvia and Lithuania the size of the unemployment benefit depends on the length of the insurance period. Especially in Latvia the replacement

Table 4

Expenditure on labour market policies in the Baltic States, 1995–2001

	1995	1996	1997	1998	1999	2000	2001
Total expenditure on active and passive measures (million EUR)							
Estonia	4.3	5.6	6.8	7.3	11.8	11.9	13.3
Latvia	–	–	–	39.3	65.7	59.2	54
Lithuania	13.7	20.3	25.3	33.6	35.6	43.1	48.8
Total expenditure on active and passive measures (percentage of GDP)							
Estonia	0.170	0.170	0.160	0.160	0.240	0.220	0.220
Latvia	–	–	–	0.72	1.05	0.76	0.64
Lithuania	0.29	0.32	0.30	0.35	0.36	0.35	0.36
Total budget on passive measures (insurance against unemployment (million EUR))							
Estonia	1.7	2.5	3.2	3.6	7.7	7.6	8.2
Latvia	15.3	17.1	21.8	29.8	54.0	47.7	42.2
Lithuania	6.4	10.3	10.9	11.3	14.2	21.9	20.0
Expenditure on passive measures (percentage of total budget)							
Estonia	40.5	44.8	47.3	49.9	65.3	63.8	61.5
Latvia	–	–	–	75.8	82.2	80.6	78.1
Lithuania	46.4	50.9	42.9	33.7	40.0	50.7	41.0

	1995	1996	1997	1998	1999	2000	2001
Expenditure on labour market institutions (percentage of total budget)							
Estonia	18.9	15.5	14.5	16.5	9.0	9.6	10.0
Lithuania	23.1	21.3	21.4	28.3	23.6	24.5	24.5

Sources: Estonian Labour Market Board; State Employment Service of Latvia; Social Report, 2001; Ministry of Social Security and Labour of the Republic of Lithuania.

Table 5

Unemployment benefits in the Baltic States in 2001

	Estonia	**Latvia**	**Lithuania**
Average benefit (EUR)	26	71	50
Maximum benefit (EUR)	26	444	70 (twice the minimum subsistence level)
Minimum benefit (EUR)	26	–	38 (state supported income)
Average wage (EUR)	352	282	277
Ratio of average benefit to wage	7.3	25.19	17.9
Maximum time payable	180 days	9 months	6 months
Specific requirements	Age 16 to retirement age, registered as unemployed by the employment service, 180 days of work during the 12 months prior to becoming unemployed.	Total insurance contributions for not less than 1 year, 9 months of insurance contributions in the 12 months before registering as unemployed.	Worked and paid social contributions for at least 24 months during the last 3 years.

	Estonia	Latvia	Lithuania
Source of funding	Insured person: None[8]. Employer: None. Government: Total cost.	Insured person and employer: 1.90% of payroll. Government: Contributes for active military personnel and for individuals taking care of children under 18 months old.	Insured person: None. Employer: 1.5% of payroll is transferred to the unemployment fund. Government: Allocations from the state budget in case of deficit.

Sources: Social Report 2001; Lithuania, Latvia and Estonia — Key Indicators 1999–2001; Social Security Programs throughout the World, 2002; Social Statistics, September 2002; Joint Assessment of Employment Priorities in Latvia, 2002.

[8] The insurance system funded by both employer and employee was launched in 2002 (see text).

rates appear to be sufficiently high to create disincentives for persons in the early stages of unemployment to consider job-offers whose wages are even marginally lower than their previous level of earnings.

Estonia

In Estonia the main passive measures used are unemployment benefit and the recently introduced unemployment insurance. The state unemployment benefit is fixed at 400 EEK (26 EUR; see also Table 5) per month, but additionally the unemployment insurance scheme was introduced in 2001. According to that, both the employer and employee make contributions to the fund (respectively, 0.5% of the total payroll and 1% of one's wage); the period of paying the benefit depends on insurance tenure (minimum 180, maximum 360 days), and the size of insurance payment depends on the person's previous average wage or salary. The upper limit of a monthly payment is 50% of triple national average wage. For instance, for the national average before tax salary 350 EUR in 2001, the maximum unemployment benefit will be $50\% \cdot (3 \cdot 350) = 537$ EUR. So the replacement rates are expected to increase.

The rate of unemployment benefit is currently so small in Estonia that the person who has lost job has to apply for subsistence benefit as well. Thus the unemployment benefit fails to fulfil its function in smoothing down consumption during the unemployment period of the household members. The new unemployment insurance system eliminates the need for people eligible for unemployment insurance benefit to apply additionally for subsistence benefit, but it does not change the situation for people receiving state unemployment assistance. The replacement rate[9] is low in Estonia: it is 27% for a couple without children, 33% for a single person, 39% for a couple with two children and 48% for a single parent with two children. On the other hand, it appears that despite that in various cases it is more beneficial to live on benefits than start working

[9] Replacement rate is the standard indicator of the generosity of an unemployment benefit system, *i.e.* the proportion of expected income from work that is replaced by unemployment and related welfare benefits.

for a minimum wage. The duration of receiving subsistence benefit is not limited. It is thought to lower one's motivation to search for work more than the higher level benefits with a certain termination date practised by other countries. It is also improper that at the time when most of the EU countries tighten up on eligibility conditions for receipt of benefits, in Estonia the criteria have been relaxed. In order to reduce the negative effects of the benefits system on work incentives, different experts have suggested that the eligibility criteria for unemployment benefits should be made stricter and more emphasis should be laid on the elements that would encourage people to search for work (Kuddo *et al.*, 2002).

Latvia

Until January 2001 in Latvia unemployment benefits were determined according to the length of the insurance period and the length of unemployment — the maximum payment period was 9 months and the minimum benefit was 90% of the minimum wage (Social Report, 2001). Since 2001, the size of the unemployment benefit has been proportional to the insurance period and corresponds to one's income from which contributions are made against unemployment (maximum is 65% of that). The benefit is paid depending on the length of the unemployment period — for the first 3 months it is paid in full; for the next 3–6 months — 75%, but not more than 2 minimum salaries; for 6–9 months — 60%, but not more than 1 minimum salary. For those receiving the average wage in the economy, the benefit was equivalent to about 40% of their net after-tax earnings. However, the replacement rate in the early months of unemployment can be significantly higher than this average rate. Also, the replacement rate is higher for those who previously had above-average earnings. Although replacement rates fall relatively sharply as the duration of unemployment increases, these initial rates appear to be sufficiently high to create disincentives for persons in the early stages of unemployment to consider job-offers whose wages are even marginally lower than their previous level of earnings. (Joint Assessment of Employment Priorities in Lithuania. Draft, 2002)

As a matter of fact, only a minority of the registered unemployed receive benefits. In the year 2000, on average approximately ¼ of

the unemployed were benefit recipients. Registered unemployed people who are not entitled to unemployment benefit can apply to their municipality for social assistance benefits. Social assistance benefits are designed "to provide social security and protection for those who are not able to provide for themselves or to overcome specific difficulties in life and do not receive adequate assistance from other sources", and unemployed people therefore appear to qualify. However, it appears that few of them do so — it has been estimated that only 2% of households who have unemployed members are actually in receipt of social assistance. It can be concluded that the overall coverage of the unemployed by the system of income maintenance is relatively low.

Lithuania

In Lithuania the monthly rate of payment varies according to the length of previous insured employment from a minimum of 135 LTL (38 EUR, state supported income) up to a maximum of 250 LTL (70 EUR, two minimum living standards). This payment is calculated following the formula that, along with state-supported income and minimum living standard also takes into consideration the length of the individual's insurance.

People on low incomes can also apply to their municipality for social assistance. Access to all aspects of social assistance requires that the recipient, if able-bodied and at working age, should be registered as unemployed. Data are not available, however, on what proportion of the registered unemployed actually receive social assistance. Generally, coverage of the unemployed by income-support measures appears to be relatively limited in Lithuania.

In general, moreover, the rates of payment are low relative to net earnings when in employment. There are, however, some instances when people on social benefits could face disincentives to moving into employment. For example, a person with one adult and two dependent children receiving maximum level social assistance can get an income which is equivalent to over 70% of the net income he/she would receive if earning an average wage. This rate considerably exceeds the respective rate of Estonia (48%) and reaches the average level of EU member states. This "replacement rate" would obviously be higher if the person concerned were low- skilled and

thus likely to find employment only at below-average earnings. Replacement rates for young single people are significantly lower — not exceeding 50% even for someone considering taking a job at the minimum wage (Joint Assessment of Employment Priorities in Lithuania, 2002).

Active labour market policies

The financing of active labour market policies is rather modest in all the three Baltic countries. In Estonia only 28% of the total expenditures on labour market measures were spent on active measures in 2001. In Latvia the total expenditure on active labour market policy was 0.16% and in Lithuania 0.12% of the total financing of labour market policies in 2001 (see also Table 6).

The most important active measure in terms of participants and expenditure is labour market training. In 2001, expenditure on training accounted for 73.2% of the total budget of active measures, followed by training allowances (13.2 %), business start-up subsidies (7.9%) and subsidies to employers (6.1%). Participation in active programmes is relatively low and has been decreasing since 1995 (see Appendix 4). In 2001, only 8.2% of registered job-seekers participated in active labour market measures, while in accordance with the European Union's employment guidelines the goal is 20%. An increased role for active labour market policies is therefore an important priority of the Estonian labour market policy. The Employment Action Plan 2002 includes a number of new initiatives whose aim is to tackle long-term unemployment. Due to a short track record, the results are not apparent yet.

According to the expenditures (see Table 6), the most important active measure is professional training (60%), followed by public works (36%) and job clubs[10] (4%). Over the last four years, the

[10] Job-seekers' clubs (JSC) are an active measure for social-psychological rehabilitation, which aims to stimulate the initiative of unemployed people, raise their ability to re-orient and adapt psychologically to a new market situation, improve their readiness to meet the needs of the labour market, and promote contact and dialogue between employers and job seekers.

Table 6

Expenditure on active labour market policies in the Baltic States, 1995–2001

	1995	1996	1997	1998	1999	2000	2001
Total budget for active measures (insurance against unemployment (million EUR))							
Estonia	1.7	2.2	2.6	2.4	3.0	3.2	3.7
Latvia	–	–	–	9.5	11.8	11.5	11.8
Lithuania	3.8	5.6	9.0	12.6	12.9	10.6	16.6
Expenditure on active measures (percentage of total budget)							
Estonia	40.5	39.7	38.3	33.5	25.7	26.6	28.0
Latvia	–	–	–	24.2	18.0	19.4	21.9
Lithuania	28.1	27.4	35.4	37.5	36.2	24.6	34.1
Breakdown of spending on active measures, Estonia (%)							
Labour market training	64.2	66.2	68.9	72.2	67.7	65.8	73.2
Training allowances	17.3	14.4	13.3	10.7	12.8	13.2	13.2
Subsidy to employer	1.2	2.3	2.3	2.7	3.9	4.5	6.1
Subsidy to start a business	13.3	10.8	9.7	9.6	8.9	9.8	7.9
Public works	4.0	6.3	5.7	4.8	7.0	6.8	–

	1995	1996	1997	1998	1999	2000	2001
Breakdown of spending on active measures, Latvia (%)							
Public works	–	–	–	34.0	31.0	33.0	36.0
Labour market training	–	–	–	62.0	65.0	62.0	60.0
Job clubs	–	–	–	4.0	4.0	5.0	4.0
Breakdown of spending on active measures, Lithuania (%)							
Retention of jobs	0.0	0.4	0.6	0.8	1.7	2.8	2.1
Labour market training	69.8	63.1	52.3	48.5	52.2	43.9	42.2
Public works	10.3	14.6	13.6	21.9	26.2	34.1	33.7
Start of own business	7.8	2.9	1.4	0.8	0.3	0.4	0.6
Support of employment	12.1	19.3	31.9	27.7	19.3	16.7	18.2

Sources: Estonian Labour Market Board; State Employment Service of Latvia; Social Report, 2001; Ministry of Social Security and Labour of the Republic of Lithuania.

proportions have not changed. In terms of participation, the job club activities are of major importance: 49.2 % of the unemployed involved in active employment measures participated in job clubs, 20.5% were sent to training and 30.3% to temporary public works (Analysis of unemployment situation in Latvia…, 2002). As regards the active labour market programmes, priority of involvement is given to people from disadvantaged groups such as people with a disability, youngsters, long-term unemployed, non-Latvian speakers and pre-retirement age people. In 2000, average participation in combined training and temporary work programmes was slightly over 4% of the average number of unemployed. It is recognised that there is insufficient access to active programmes, particularly for the young and for the long-term unemployed. For example, in 2000, training opportunities could be provided for only 36.6% of the unemployed people who expressed a desire to acquire a new profession or to upgrade their qualifications. Increasing access to active programmes was included among the objectives of the National Employment Plan 2001. However, expansion of active programmes is constrained by the availability of budgetary resources.

Out of the total expenditure 46% were used for retraining programmes, 34% for temporary public works, 17% for employment subsidies, and 1% for job clubs. The balance within the programmes is concentrated on the provision of temporary jobs, which accounts for one-third of the total programme expenditure, and for an even higher proportion of the average number of programme participants (see Appendix 4). The programme expenditure and participation are extremely low, considering the scale of Lithuania's unemployment problem. In 2000 the average number of participants in programmes (excluding job clubs) was estimated to be not higher than 3% of the average number of registered unemployed. The demand for places, particularly in vocational training, greatly exceeds supply.

To sum up, some differences can be perceived in the implementation of active labour market programmes in the Baltic States. While training absorbs the biggest share of funding in all the three countries, in Lithuania the share is somewhat lower than in Latvia

or Estonia. In Latvia and Lithuania public works receive a significantly larger proportion of the budget than in Estonia, where their share is rather modest. At the same time, the percentages of Estonian and Lithuanian participants in public works did not differ very much; consequently, the former's expenses per participant were considerably smaller. The active measures differ across countries: there are job clubs only in Latvia and Lithuania; also, Latvia pays no subsidy to start a business, as do Estonia and Lithuania.

Assessment

Compared to the EU, the Baltic States' labour market policies are rather insufficiently funded. In 2001 the expenditures on labour market policies accounted for 0.22% of the GDP in Estonia, 0.64% in Latvia and 0.27% in Lithuania. This is a very small fraction compared to the respective average rate of 2.48% in the EU or even the respective rates in selected EU candidate countries (see Table 7 below).

Also, the share of active measures is relatively low in both expenditures and participation rates. In Lithuania 34.1%, in Latvia 22% and in Estonia 28% of the overall employment policy budget are allocated on active measures, while the EU average is almost 40%. At the same time, the overall coverage of the unemployed by the system of income maintenance is still low in all the three states.

Replacement rates are likewise low in comparison with the 60% of the EU member states. Slight differences among the Baltic States can be pointed out: the replacement rate is lower in Estonia and Latvia, and higher in Lithuania where it amounts to the EU average in certain cases. Still, it can be noted that in all the three states the income maintenance systems have to a certain extent dampened the people's incentives to look for a job. The influence is still minor in comparison with the well-developed European countries where the replacement rates are sufficiently large to have a significant effect on work incentives and consequently on labour market flexibility. However, given the political conditions, only marginal cuts have been made in the generosity of benefit entitlements. Rather the eligibility conditions for receipt of benefits are tightened up and activation strategies for the unemployed are developed. The Baltic States have the same path ahead of them.

Table 7

Spending on labour market programmes in the EU and selected candidate countries in 2000

	Total spending (% of GDP)	Active spending (% of GDP)	Active spending (% of total spending)
Estonia	0.22	0.06	27.0
Latvia	0.76	0.15	20.0
Lithuania	0.27	0.09	33.1
Czech Republic	0.52	0.22	42.9
Hungary	0.87	0.39	45.3
Poland	2.25	0.54	24.0
EU	2.48	1.12	39.8

Sources: Martin *et al*. 2001, p. 7, Estonian Labour Market Board, Ministry of Social Security and Labour of the Republic of Lithuania, Joint Assessment of Employment Priorities in Latvia (draft).

Currently, participation of registered job seekers in active labour market measures is insufficient. In accordance with the European Union's employment guidelines the goal is to achieve the involvement rate of 20% of the unemployed people (Draft Joint Employment Report, 2001). At the moment, the respective figure is highest in Estonia — 10%, followed by Latvia's 4% and Lithuania's 3%. It is not clear if recruitment to programmes is appropriately targeted. The groups covered are not necessarily those to which greatest priority should be given in the light of changing labour market circumstances. Apparently, there is a need for comprehensive analytical evidence on the effect of the existing programmes. Such essential knowledge would serve as a basis for developing well-targeted and successful programmes in the future.

Obviously, the labour market policies of the Baltic States need to be reformed upon their EU accession. According to recent evaluations, in Estonia one of the main problems is the poor targeting of the programmes (Joint Assessment of Employment Priorities in Estonia, 2001; Tööturupoliitika planeerimine..., 2001). Given the limited resources available, it will be important to ensure that these

programmes remain targeted on the most disadvantaged job seekers and regions and that their impact is closely monitored. One specific example is aid to starting business. Experience elsewhere suggests that this form of subsidy appears to be successful, but only for a small group of unemployed individuals. Currently different support structures are implementing this measure in Estonia. In addition to the Labour Market Board, the business support structures under the governance of the Ministry of Economic Affairs offer start-up aid to beginning entrepreneurs. There is a need for closer inter-ministerial co-ordination in this field as well as for more efficient combining of the subsidy with relevant training and consultancy.

Joint Assessment of Employment Priorities in Lithuania (2002) noted that there is a need to expand active labour market programmes and to re-balance provision away from temporary work in favour of training and other measures designed to increase employability. Also passive policies need to be reformed, in particular, unemployment benefits and social assistance to the unemployed should be reformed in order to improve coverage, eliminate disincentives, and emphasise activation rather than passive receipt of benefits. Public employment service should play a more active role in reintegrating the unemployed, hence a detailed action plan for its reform should be developed and the service's resources should be increased.

The joint report of Latvia and the European Commission indicated the following areas where the country must progress further (Joint Assessment of Employment Priorities in Latvia, 2002):

- The current structure of unemployment benefit payments needs to be developed further, while improving social assistance provision to those unemployed who are not entitled to benefit;
- An active strategy of supporting job search and employability should be implemented, for which purpose efforts are required to raise the level of registration of the unemployed with the State Employment Service;
- Expansion of active labour market programmes should be targeted to disadvantaged groups on labour market by giving preference to training and human resources measures over those providing only temporary public works.

We can conclude that the unemployment benefits are small because labour market policies in the Baltic countries are underfinanced; therefore they fail to remarkably reduce labour market flexibility. On the other hand, by means of laying a stronger emphasis on active labour market programmes, the positive impact of labour policy on labour market flexibility can be increased. In this context, more attention should be paid on education and training, including development of lifelong learning which is now an established priority throughout the EU. At the moment, for example in Lithuania as well as in Latvia, the balance within active programmes is overly concentrated on the provision of temporary jobs, but short periods of temporary employment are unlikely to contribute to the longer-term employability of participants.

3. Wage flexibility

Wage flexibility shows how the wages react to recessions and booms in economy. It shows if the wages are rigid only downwards or if the long-term wage agreements can also slow down the wage rise. According to our concept, the more quickly the wages react to changes in economy, the more flexible the labour market is. Here we try to measure the flexibility of nominal wages. Usually it is the flexibility of real wages that has caught researchers' attention.and can be read about in literature. In our opinion, however, the fluctuation of nominal wages during a business cycle is even a better evidence of wage flexibility than changes in real wages.

Speaking about wage flexibility in the Baltic States, one should first discuss the economic background. The GDP growth in the Baltics over the period 1995–2000 is shown in Table 8.

Table 8

Gross domestic product (GDP) at constant prices, % compared with the previous year

Country	1995	1996	1997	1998	1999	2000
Estonia	4.3	3.9	10.6	4.7	–1.1	6.4
Latvia	–0.8	3.3	8.6	3.9	1.1	6.6
Lithuania	3.3	4.7	7.3	5.1	–3.9	2.9

Source: Statistical Offices of the Baltic States.

It can be seen that in 1999 a remarkable drop in GDP growth took place in all the three countries because of the Russian crisis at the end of 1998. The drop was largest in the case of Lithuania and smallest in the case of Latvia because Lithuanian economy is more tied to Russian economy than the other two countries' economies — Estonian export to Russia in 1998 was 13.4% of its GDP, while Lithuanian export to Russia made up 16.5% of its GDP. In 1999 the shares were 9.2% in Estonia and 7% in Lithuania. In Latvia the respective indicators were smaller. That the GDP growth rate has fallen, too, can be the consequence of changes in different industries.

Figure 2 below shows that the highest wages in the Baltic States are in financial intermediation and public administration, whereas the lowest wages in all the three countries are found in agriculture and the hotels and restaurants industry. It seems that, apart from some small differences, the wage level structure is quite similar in all the three countries. The Estonian and Latvian wage level structures are quite similar, while Lithuania's case differs more.

In Figure 3 minimum wages are depicted as the ratio to trans-Baltic average wages. The logic is that the figure actually relevant for wage flexibility is not so much the absolute size of the minimum wage as its level compared to the aggregate wage level. It can be seen that over the period 1994–2001 the highest minimum wage has been in Lithuania (up to 60% of the average wage) and the lowest in Estonia (around 30% of the average wage). In Latvia the

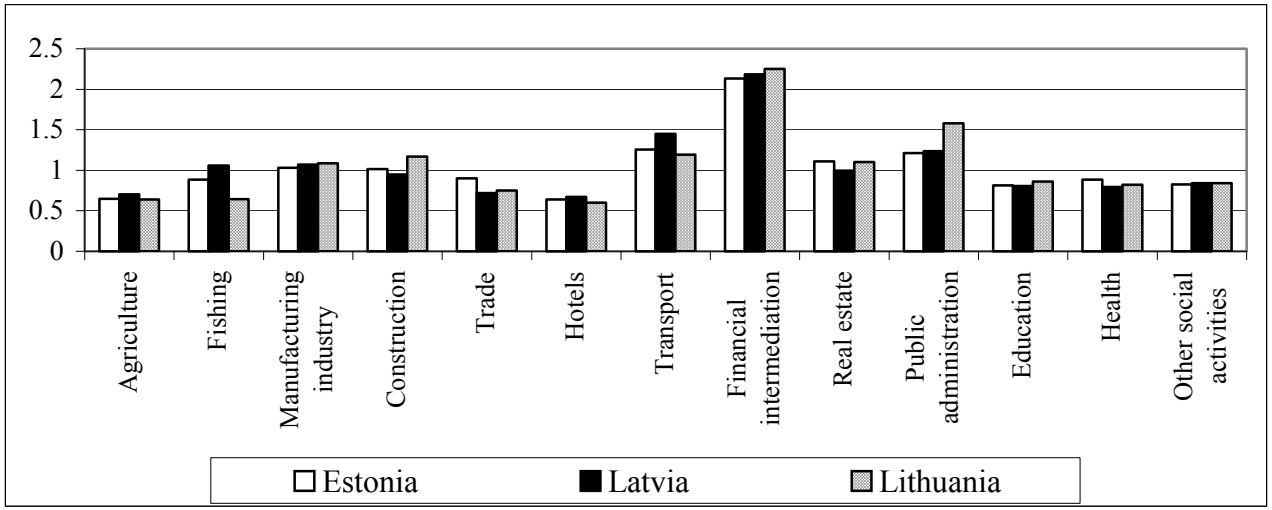

Figure 2. Shares of wages in the total national average in Estonia, Latvia and Lithuania (the average for the period 1995–1999) by separate industries.

Source: Central Statistical Bureau of Latvia; Statistical Yearbook of Lithuania, 2002; Statistical Office of Estonia.

minimum wage since 1 July 2001 has been 104 EUR and in Lithuania since 1 January 2001, 125 EUR (in Estonia — 90 EUR) (Minimum monthly earnings…, 2002; Minimum wages in Latvia…, 2002). Still it is argued that in Lithuania enforcement of minimum wage is almost nonexistent. Taking by way of comparison the level of minimum wage in the EU countries, we can see that although Portugal had the lowest minimum wage in 2001 (390 EUR), it constituted as much as about 57% of the average wage of an employee in the manufacturing sector in 1999. On the other hand, in Luxembourg the minimum wage was the highest of the European Union (1 259 EUR), but it made up only 42% of the average wage of an employee in the manufacturing sector in 1999 (Nobre, 2001). The average ratio of minimum wage to average wage of an employee in the manufacturing sector of the EU was 43%.

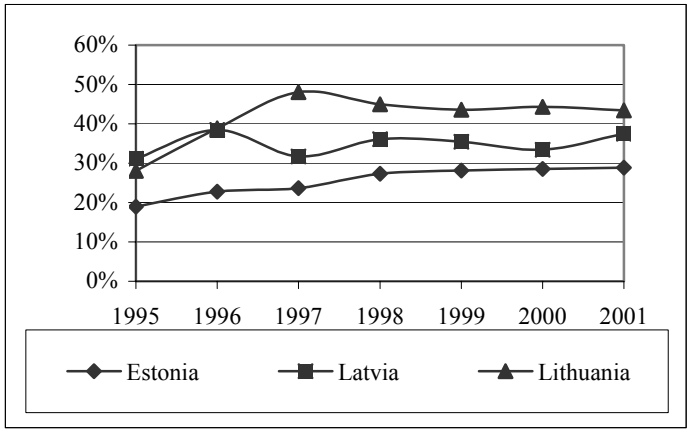

Figure 3. Minimum wages as percentage of average wages in the Baltic States in 1993–2001.

Though the minimum wage in Portugal is about three times and in Luxembourg about ten times higher than in the Baltic States, due to the differences in aggregate wage levels, the Baltic minimum wages in relation to average wages are of comparable size to those

of the European Union. In particular, while the average wage was 282 EUR in Latvia, 277 in Lithuania and 352 in Estonia, the numbers in the aforementioned EU countries were about 680 EUR in Portugal and 3 000 EUR in Luxembourg.

As we observed, minimum wages comprise only a small share of average wages in the Baltic States, compared with the European Union member countries. On the basis of this we can argue that the effect of minimum wages on the Baltic States' labour market, causing labour market disturbances and therefore decreasing labour market flexibility by changing the distribution of wages and eliminating part of the workforce from employment, is smaller than in the EU countries.

The easiest way to say whether wages in the Baltic States are flexible or not is to find out if the wages decreased in those industries that were closely connected to the Russian market and therefore experienced a reduction of output due to the Russian financial crisis in 1998. If there occurred a fall in wages, it may indicate the presence of wage flexibility, as the decreased demand for the output of these sectors reduced the demand for labour input, which in turn put downward pressure on wages.

Estonia

In Figure 4 the wage indexes of these branches of economy where a reduction of nominal wages took place in 1999 are shown in comparison with the aggregate wage index. It can be seen that three of the four industries are those where the growth of wages is slower than the growth of wages in the whole economy. Agriculture is the industry where the growth rate of wages is higher than the total growth but the wages in agriculture make up slightly more than a half of the total average wage (see Figure 2). The same is true about hotels and restaurants, but here the wages grow slower than the total average. In the hotels industry the downward leap of 1999 was steepest. The wage dynamics in other sectors can be seen in Appendix 5.

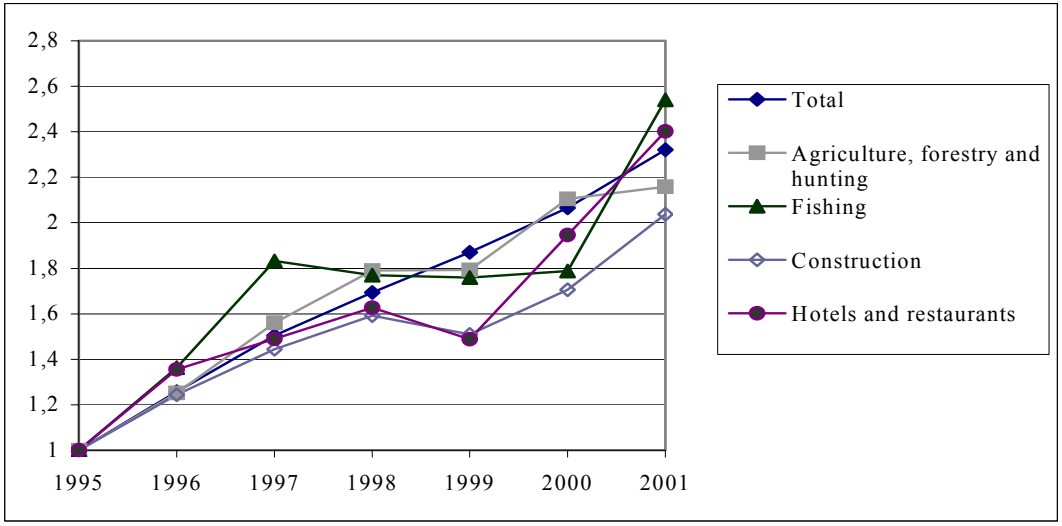

Figure 4. Estonian gross nominal wages by economic activities in 1995–2001 (1995 = 1).

Latvia

In Latvia the drops in wages were mostly smaller than in Estonia. Looking at fishing, we can see that the wages shrank there already in 1998 (as in Estonia). In the case of Latvia the reduction was especially remarkable (Figure 5). At the same time, the wages in construction did not fall before 2000. This may indicate that the Latvian wages in construction are slightly more rigid than in Estonia, which accords with differences in unionization of this sector in these two countries.

Lithuania

Compared to Estonia and Latvia, in Lithuania wages are considerably higher in financial intermediation, public administration and compulsory social security (Figure 2). Slightly higher wages may also be detected in manufacturing and construction, while in agriculture, forestry, hunting and fishing, wages are somewhat lower than in the other Baltic States. In view of the comparatively large share and importance of agriculture in Lithuania (employed persons in agriculture in 2000 made up 21% of all employed persons, while the respective number in Latvia was 15% and in Estonia 7%), the latter must be taken into account.

From the graphs of wage dynamics of the Lithuanian economy by separate industries we see that during the sample period, between 1995 and 1999, there was a reasonable wage growth, which declined after 1998, but in a hardly noticeable amount and not getting negative. This is quite surprising as the Russian crisis influenced the Lithuanian economy most of all among the three countries: the economic growth in constant prices was –3.9% and inflation slowed down to 0.3%. The influence of the crisis on nominal gross wages seems to be smallest in agriculture and the fishing industry (see Appendix 7).

The impact of the shock seems to have been greatest in the manufacturing industry, where nominal wages in construction decreased (see Figure 6). At the same time it is also remarkable that wages in the public sector dropped a little as well.

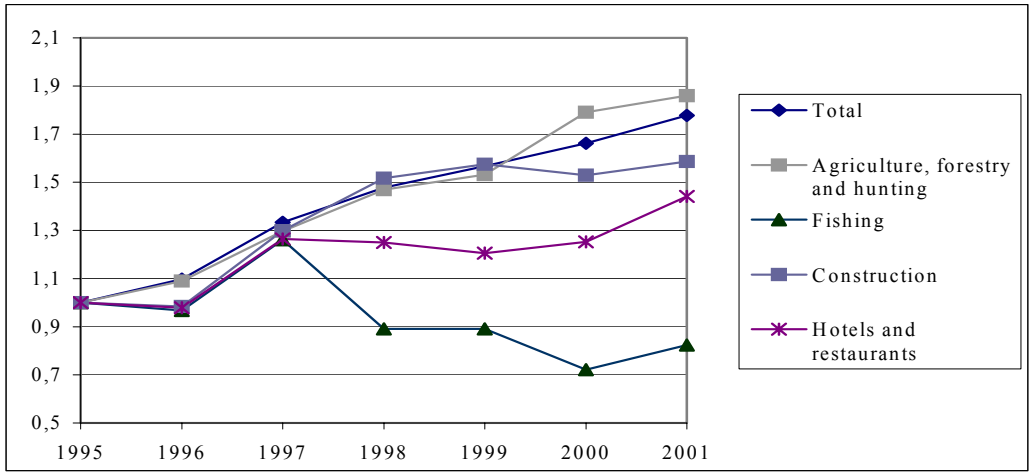

Figure 5. Latvian gross nominal wages by economic activities in 1995–2001 (1995 = 1).

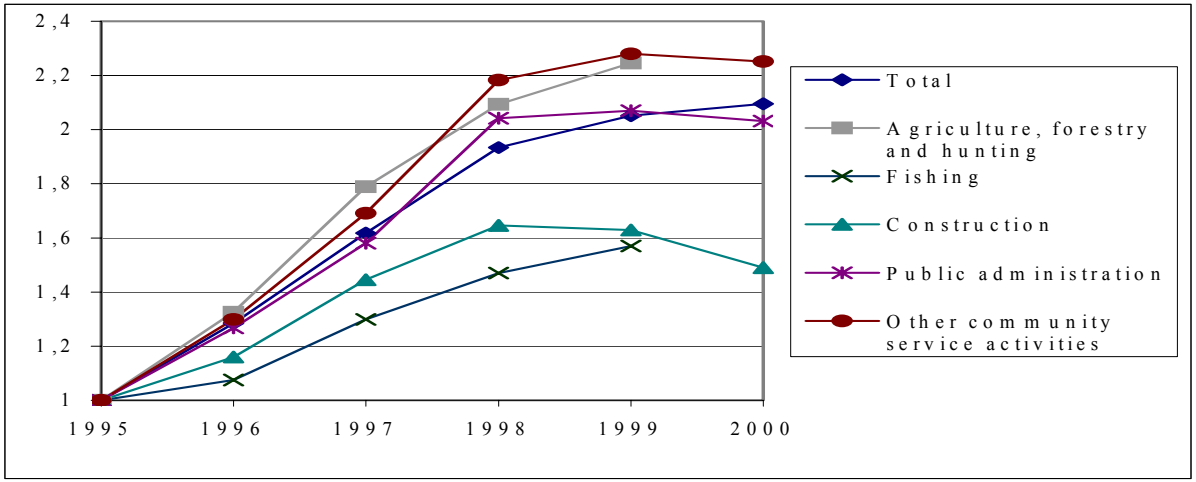

Figure 6. Lithuanian gross nominal wages by economic activities in 1995–2000 (1995 = 1).

Lithuanian nominal wage dynamics differ from those of the other Baltic States. While in other countries the Russian shock had a bigger influence on agriculture and a smaller influence on the branches of non-tradables such as services and public goods, the Lithuanian figures speak of the opposite dynamics. The only industry to suffer similarly in all the three countries after the Russian crisis was the manufacturing industry and even there Latvia did not suffer as much as the others. It can be guessed that the crucial point here is the share of the particular industry's export to Russia, but we should not dismiss the fact that in some countries and some industries wages react in a more sensitive way than in others. In this respect Lithuania seems to have more rigid wages than Estonia and Latvia, and especially in agriculture the rigidity seems to be highest. This may explain why Lithuania suffered longer after the Russian crisis than the other two Baltic States.

In summary, nominal wages seem to be most rigid in Lithuania and most flexible in Estonia. According the economic activities, in all the three countries the most flexible wages are to be found in construction. In Estonia and Latvia wages are also flexible in fisheries, hotels and restaurants, and somewhat less in agriculture. Salaries in the public sector and in the financial industry are mostly rigid. The data show that if the wages are lower, they are more flexible, too (the case of agriculture in Estonia). In the context of EU enlargement one possibility is that wages in these industries where they are most flexible will converge faster with the EU wage level if EU labour market policies are liberalized. The other possibility is that if the labour markets are regulated, as highly as in the EU, wage flexibility will decrease in all the three countries, especially in Estonia. The last possibility seems more realistic.

4. International labour migration

One aspect of labour market flexibility is the geographical mobility of the workforce. In this section we will analyze labour market flexibility from the point of view of labour migration. Increasing labour migration between East and West, which is determined by various socio-economic and political reasons, is undoubtedly one

of the possible consequences of the EU eastward enlargement processes. The latter should be focused on when analyzing possible changes in the labour markets of both the current EU members and the accession countries. Lessons of labour migration in Europe in the 1960s and 1970s, and particularly during the previous EU enlargement processes are the most valuable sources to be drawn on when making predictions about international labour migration resulting from EU and Eurozone eastward enlargement.

Theoretically, labour migration is a consequence of people's rational choice, which is oriented at a certain system of values. One of the conditions for migration is the existence of a more or less stable social context composed of people whose needs are at least minimally satisfied. If those minimal needs within one social context are not fulfilled, some people will emigrate to a new social context, in which they will find better conditions to fulfil their needs, or expect to suffer relatively less deprivation and get better opportunities for development (see also Mangalam and Morgan, 1968). That is one possible explanation for the labour migration phenomenon, which certainly does not completely explain all the factors and consequences of labour mobility during EU eastward enlargement. In fact, there is no single coherent theory of migration, only a fragmented set of theories that have often developed in isolation from one another[11].

According to neoclassical economic theory, international labour flows exist as a consequence of real wage differences between countries. The international labour flows are supposed to create a new international equilibrium in which real wages have the same level in all countries (Borjas, 1989; Öberg, 1997). In Keynesian theory, labour supply depends on nominal wage, not only on real wage. This distinction has its origins in the differing views of the role of money. Money is not only a medium of exchange but also a medium of saving; therefore potential migrants are attracted to re-

[11] The set of theories trying to explain migration processes includes the neoclassical theory of migration, segmented labour market theory, world system theories, human capital theory, the new economics of labour migration, dual labour market theory, the gravity model based approach etc.

gions with high nominal wages. Intensions to re-emigrate or to send remittances increase the importance of nominal wage level compared to that of real wage. This aspect of Keynesian theory allows us to argue that the unemployment difference between the sending and receiving country has a positive effect on the extent of labour migration between countries (see also Jennissen, 2002).

Piore (1979) gives three possible explanations for the demand for foreign workers in modern industrial societies: 1) general labour shortages, 2) the need to fill the bottom positions in the job hierarchy, and 3) labour shortages in the secondary segment, which is characterized by a labour-intensive method of production and predominantly low skilled labour market. Hence, the dual labour market theory also explores reasons and consequences of international labour migration and stresses the need to analyze the low and highly skilled labour flows separately (see case studies "Migration from Portugal to Switzerland: Low skilled, 'classical' labour migration" and "migration from Sweden to Norway: Highly skilled 'post-industrial' labour migration"; Jennissen, 2002), that will certainly provide some lessons for exploring and predicting possible changes in the EU labour market after eastward enlargement.

In general the reasons for migration can be divided into pull and push factors that either promote or restrain migration. They are called pull or push factors depending on whether they emanate from the source (home) or destination (host) country. The main pull factors include good employment opportunities and high potential income in the country of destination, while the main push factors are usually high unemployment and low earnings in the home country. But it is obvious that the reasons for international labour mobility are not only determined by economic factors. Additionally, there are also legislative (legislation regulating labour mobility between the countries, labour legislation), demographic (number and structure of population), political, social, psychological, cultural, and historical factors. Of special importance is the influence of migration networks, which may help potential migrants of the same ethnic origin to find a job and to get information about accommodation and proper labour and social policy measures, etc. Also differences between the educational levels of the sending and receiving countries influence labour migration. For instance, the

high educational level of a sending country may have a negative effect on low skilled labour flows from this country.

In the second half of the 1990s numerous studies concentrated on the prospects of international labour migration after EU eastward enlargement, when the current regime will have been supplanted by the right of free movement of labour. The forecasts of possible labour movement between the countries in absence of administrative restrictions vary considerably, depending on the methodology and assumptions used (Brücker, Boeri, 2000; Sinn, *et al*., 2001; Walterkirchen, Dietz, 1998; Bauer, Zimmermann, 1999; Hille, Straubhaar, 2000). The main methodological distinction is between surveys and quantitative models. Surveys recording intentions and desires do not pretend to predict the actual movement. Model-based studies remain relatively uncertain due to the complexity of factors influencing migration and reliance on strong assumptions. They attempt to transpose patterns observed in major recent migrations, and crucially depend on the assumptions that will be reproduced in the case of enlargement. Uncertainty is further enhanced by reliance on very long-term forecasts of economic development in the EU and candidate countries (see also EC, The Free Movement of Workers…, 2001). The fact that uncertainty remains high regarding future migration is also underlined by the Eurostat studies (Eurostat, 2000a and 2000b) which, however, make two important assumptions: 1) the present distribution of candidate country nationals among the member states will not change, and 2) the share of employees will be based on the present (rather low) share of employees among residents. These assumptions could distort the picture to some degree, insofar as the present distribution and employment rate are the result of rather different historical circumstances and migration patterns than those that will prevail after accession in the context of free movement.

Various research-based estimates put the long-run migration potential from the candidate countries roughly at 1% of the EU15 population (hence, about 3.8 million). Surveys suggest a strong preference of candidate country nationals for temporary work, which implies also important flows of return migration to the candidate countries. Based on some predictions about the situation in absence of administrative restrictions for labour movement, the

initial immigration from the CC8 countries (the European candidate countries excluding Bulgaria and Romania) to EU15 would be around 70 000 workers annually (that means all-in-all 200 000 people, including also family members) or 0.05% of the EU15 population (The free…, 2001).

According to the study by Brücker and Boeri (2000), labour migration will concentrate only in a few member states and enlargement will not significantly affect the wages and employment in the EU. It is thought that two-thirds of the labour migration flows from the candidate countries will be absorbed by Germany (hence, around 45 000–50 000 workers per year from CC8 in the first few years), while Austria will absorb about 20% of these labour flows. The forecasts show that the share of the CC10 people in the population of the present EU member states will rise from 0.2% in 1998 to 1.1% in 2030 (*Ibid*.). In sum, according to the predictions, the movement of labour between the EU countries after eastward enlargement will not be significant.

Analyzing the stock of the labour force in the current EU members that has emigrated from non-EU countries, one can say that this amount is not significant. In 1999 the stock of labour force in EU15 from non-EU countries was about 5.3 million (or 3.1% of the EU's total labour force, and the number of residents was about 12 million (3.2% of the EU's total number of residents). At the same time, the official labour force from the candidate countries (CC) numbered only 290 000. Apart from those people who are officially working in the EU member states, according to some estimates there are also about 600 000 "working CC tourists" (Eurostat, 2000a, b). Hence, one can conclude that the stock of emigrants from the candidate countries is not large, nor are there any well-developed or institutionalized migrant networks to support East-West labour migration.

The number of Baltic States residents in the EU member countries is likewise insignificant. In 1998 these numbers were respectively about 15 000 from Estonia, 7 500 from Latvia and 8 500 from Lithuania (Table 9). The total number of the Baltic States' population is about 7.6 million (1.45 million in Estonia, 2.44 million in Latvia and 3.70 million in Lithuania) and now the share of Baltic

nationals in the EU member states is only about 1% of Estonians, 0.3% of Latvians and 0.2% of Lithuanians. It is obvious that changes in the Baltic States' labour markets and labour flows from these countries will not have any significant impact on the EU labour market as a whole.

Analyzing the labour migration problems of the Baltics, emphasis should first of all be laid on possible labour movement within the Baltic Sea region[12]. The integration of the border regions appears to be relevant in the forthcoming EU enlargement. The countries which mainly attract the Baltic States' labour force are the current EU member states belonging to the Baltic Sea region: Denmark, Finland, Sweden and Germany[13].

According to the Eurostat data (2000), more than 90% of the Baltic nationals in EU15 live in the Baltic Sea Region countries (98.2% of Estonians, 91.8% of Latvians and 92.6% of Lithuanians). At the same time, due to the Baltic States' very small population numbers, the share of Baltic nationals in the populations of these countries is insignificant, not exceeding 0.2%. The main stock of Estonian citizens lives in Finland (66% of Estonian citizens living in the EU member states), while that of Latvian and Lithuanian citizens lives in Germany (respectively 82% and 80%). There are probably some migration networks only in Finland and Germany that may support the migration of labour force from the Baltic States to the Baltic Sea Region countries. But these possible networks are neither institutionalized nor play a significant role in attracting labour force from the Baltic States.

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[12] In 1995 the Baltic Sea was declared to be an inland sea of the EU. This event was of strategic importance for the integration of the countries around the Baltic Sea.

[13] According to the Ministry for Social Affairs and Labour of Lithuania (2001), Lithuanians have mainly worked in the following countries in the recent years: Russia — 20.3%, Germany — 18.6%, Great Britain — 9.9%, US — 8.1%, Denmark — 7.6%, Italy — 6.4%, Sweden — 4.1%. Hence, more than 50% of Lithuanians that temporarily worked outside of their home country did so in the Baltic Sea Region countries.

Table 9

The number of Baltic Citizens in the EU Member States in 1998

	Germany	**Finland**	**Sweden**	**Denmark**	**Holland***	**Italy**	**Greece**	**Spain**	**Portugal**
Estonia	3 173	9 689	1 124	384	100	98	36	31	2
Latvia	6 147	134	387	449	110	168	73	36	1
Lithuania	6 631	163	358	555	260	174	109	65	10
Total	15 951	9 986	1 869	1 388	470	440	218	86	13
Baltic nationals in the EU (% of the total population of the Baltic States)									
	1.01	0.31	0.22						
Baltic nationals in the EU (% of the total population of selected EU Member States)									
	0.02	0.19	0.02	0.03	0.002	0.001	0.002		

Source: Eurostat, 2000 a, b; Authors' calculations.

* The study assumes accession in 2002 of all candidate countries. Its oft-quoted estimate of 335 000 refers to the total number of people migrating from all candidate countries in 2002, of which 35% would be employees.

The main economic pull and push factors that influence labour movement within the Baltic Sea Region countries are presented in Table 10 below. The distance between the Baltic Sea Region countries expresses not only the economic cost of migration but also the cultural proximity and historical relationships between the countries.

Besides the abovesaid, the consequences of EU enlargement for international labour migration depend on the legal conditions for international labour movement. If the citizens of the candidate countries are allowed to work in all the EU countries immediately after joining, then it is likely that the first years of EU eastward enlargement will see significant East-West labour flows. Especially Germany and Austria fear remarkable labour migration. Therefore, it is likely that like in the second and third waves of enlargement, when Greece, Portugal and Spain joined the EU, a transitional agreement will be formulated with respect to free labour movement.

The present conditions of labour market access in the Baltic Sea Region countries that are members of EU15 are shown in Table 11 below. Due to the small size of the Baltic States' labour markets, the Baltic influence on the EU's labour market will not be significant even if people from the Baltics are granted free access to the labour markets of all the member countries immediately after joining the EU. This permission may most significantly influence Finland as a Baltic Sea Region's industrialized country with small open economy.

The average educational level in the Baltic States, like in the other Central and Eastern European countries, is high and therefore it plays a comparatively insignificant role in determining labour migration. If recognition of diplomas of the accession countries is agreed on, some increase of highly skilled labour force movement between East and West (both sides) can be predicted and the wages of highly qualified persons will rather quickly create a new wage equilibrium. The educational level in some accession counties, including the Baltic States, is even approaching the natural upper limit. Thus, with respect to educational level, the former low skilled labour migration from less developed regions to the EU

Table 10

Factors influencing the Baltic Sea Region countries' labour migration in 2000

Factor	The Baltic States	The Baltic Sea Region countries — currently EU members
GDP (PPP) per capita, int.$	Estonia — 10.068; Latvia — 6.893; Lithuania — 7.094	Denmark — 27.404; Finland — 25.154; Germany — 25.290; Sweden — 24.288
GDP (MER) per capita, USD	Estonia — 3.577; Latvia — 2.938; Lithuania — 3.044	Denmark — 30.400; Finland — 23.418; Germany — 22.829; Sweden — 25.627
Number of population (million)	Estonia — 1.45; Latvia — 2.4; Lithuania — 3.7	Denmark — 5.3; Finland — 5.2; Germany — 82; Sweden — 8.9
Unemployment rate (%)	Estonia — 13.9; Latvia — 14.7; Lithuania — 15.9	Denmark — 4.6; Finland — 9.7; Germany — 10; Sweden — 4.7
Distance between the capitals (km)	Est.-Den.: 482; Est.-Ger.: 1,045; Est.-Swe.: 383; Est.-Fin.: 84 Lat.-Den.:733; Lat.-Fin.:361; Lat.-Ger. 850; Lat.-Swe.: 450 Lit.-Den.:826; Lit.-Fin.:611; Lit.-Ger.:828; Lit.-Swe.: 686	Den.-Est.: 842; Den.-Lat.: 733; Den.-Lit.: 826 Fin.-Est.: 84; Fin.-Lat..361; Fin.-Lit: 611 Ger.-Est.: 1045; Ger.-Lat.: 850; Ger.-Lit.: 828 Swe.-Est.:383; Swe.-Lat.: 450; Swe.-Lit.: 686

Sources: Financial Statistics Yearbook, IMF, 2001; World Bank, 2001 (www.worldbank.org); Statistical Office of Estonia, 2001; The Baltic and the Nordic Countries. Central Statistical Bureau of Latvia, 2000. International Labour Organization, 2002 (www.ilo.org); Estonia, Latvia, Lithuania in Figures, 2000; Statistical Office of Estonia, 2000.

Table 11

The conditions for accessing the labour markets of the Baltic Sea Region countries — current EU members, in 2000

Country	Access of third country nationals to the labour market	Special regime for candidate countries	Long-term residence permits
Denmark	Very limited access. A work permit must be obtained prior to entering the country. A labour market need has to exist. The total number of permits granted in 1999 was 73 092.	No special regime	In general, if a work permit is granted, a residence permit is also granted.
Finland	A work permit must be obtained prior to entering Finland. The labour market has to exist. Privileged regimes for qualified workforce.	No special regime	Usually for 1 year, after 2 years a permanent residence permit may be granted
Germany	Residence permits (granted up to 5 years) and work authorization needed. Work permits normally require existence of need in the labour market. The total number of permits in 1999 was 1 083 268.	Quota-based agreements on trainee workers with Bulgaria, the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania, Slovakia, Slovenia.	–

Country	Access of third country nationals to the labour market	Special regime for candidate countries	Long-term residence permits
Sweden	Different countries decide together with the national authorities on the issuance of temporary work permits. Work permits are only issued in case of labour shortage. The total number of foreign workers about 220 000.	Bilateral agreements on trainees.	After 2 years of residence a permanent residence permit may be applied for.

Source: The free movement…., EC, 2001.

cannot be compared with the future low skilled migration from the accession countries. It is also predictable that due to significant differences in real and nominal wages and structural unemployment in most accession countries (also in the Baltic States) comparatively well educated people will move to the industrialized EU countries in order to work there as blue colour workers. In most cases they will get temporary jobs.

It is highly probable that cross-border movement in the Baltic States' border regions will significantly increase after free movement of labour has been achieved. Cross-border movement includes commuting by employed persons, or occasional jobs of a few days', weeks', or sometimes also of a few months' duration. Cross-border workers will keep their house and family in their home countries, thus avoiding the high transaction cost of moving to another country. The cross-border workers will usually take their wages back to their home country. Consequently, the wage gap should be assessed, taking into account the higher purchasing power of their wage at home. It is predictable that cross-border work can be first of all costly to the country of residence, which may not receive the income tax revenue from the worker, but has to finance the social expenditure and local infrastructure for the benefit of the worker's family. The employing country will even enjoy the corresponding financial advantages.

In summary, due to the very small size of the Baltic labour markets in comparison with the EU, labour migration from the Baltic States into the EU15 countries will not be significant in the near future. Based on the experience of the previous stages of EU enlargement and the predictions that labour migration will not exceed 0.2% of the population, it is possible to estimate that in the first years of free movement of labour, migration from Estonia could be about 2 500–2 800 people per year or about 10 000–14 000 during the first four or five years; 5 000–6 000 people per year from Latvia (about 15 000–23 000 during the four or five years' period); and 7 000–8 000 per year from Lithuania (about 27 000–37 000 during the first four or five years). Over a long-term period (10 years) the labour migration will be declining.

Previous experience and research show that labour migration processes have had little effect on unemployment and wages in the host country (Sinn, 2001). Migration of labour from a home country to a country of destination can even provide a gain for the host country, since migrants generally receive a wage below the gain in value added to the economy. The income earned by immigrants usually creates no burden for the domestic population. There are also possibilities of additional investment income, rents and increased consumer spending. As regards public finance, immigration impacts on the government's expenditure and revenues, but the net impact at the national level is negligible. In a long-term perspective, immigration can limit the adverse impact on living standards and the government's budgetary positions due to the tendencies of populations towards declining and aging. Of course, labour migration on its own cannot solve the problem of ageing of the European population. In order to maintain a sufficient labour force, and additionally to import labour through migration, the European countries will have to significantly reduce their unemployment rates and increase the participation rates in their labour markets.

Free movement of labour will put rather serious pressure on the Baltic States' labour markets due to the possible migration of better-qualified and flexible labour force. Movers will be mainly people with good qualifications, also young people with a secondary school (gymnasium) education, who cannot find qualified jobs at home. They are ready to work abroad as blue-collar workers, getting relatively higher salaries than they expected to get in their home countries. Also the possible cross-border movement of workers in the Baltic Sea Region will exert pressure on the Baltic States' labour markets.

In conclusion, the analysis of the labour migration experience of the previous stages of EU enlargement allows us to summarize the following.

1) Free movement of labour will not place any significant pressure on the labour markets (first of all, on the level of unemployment and wages) of the current EU member states. The main absorb-

ers of the labour flows from CC10 will be Germany and Austria.

2) Due to the very small size of the Baltic labour markets in comparison with the EU, labour migration from the Baltic States into the EU15 countries will be insignificant and will not exert any notable pressure on the EU labour market.

3) Due to the historical and cultural conditions and close neighbourhood, the migration of the Baltic States' labour force will be mainly to the Baltic Sea Region countries. Cross-border movement of labour is expected to grow, which can be comparatively costly to the country of residence.

4) Free movement of labour will create a certain burden on the home countries' economy as it is predictably well qualified and flexible labour force that will start moving.

5) The European countries have to significantly reduce their unemployment rate and to raise the participation rate in their labour markets in order to maintain a sufficient labour force for sustainable development. Import of labour is not the only source for solving demographic problems. Hence, in order to achieve sustainable development in all the European countries in the context of EU eastward enlargement, growth of labour market flexibility is unavoidable.

Conclusions

The aim of the paper was to give an overview of the main changes in the Baltic States' labour market over the period 1990–2001, laying emphasis on the problems of labour market flexibility and migration in the context of EU eastward enlargement. Two sides of macro level labour market flexibility were discussed: institutional flexibility (labour legislation, labour policy, trade unions) and wage flexibility.

The Baltic States have followed the main international standards that regulate labour relations. Several measures have been taken to protect employees in less favourable circumstances such as elderly employees, women with children, persons with a disability, etc.

Naturally there are some differences in the regulation measures between the Baltic States themselves. The summary index measuring the legal restrictions on individual dismissals showed that dismissals are less regulated in Latvia than in Estonia and Lithuania; the value of the index for the Baltic States is higher than the EU average. On the other hand, the use of fixed-term contracts is less restricted in the Baltic States than in the EU, and in Lithuania their use is less restricted than in Latvia and Estonia. As the status of civil servants is regulated by separate laws, they have some advantages, but are also subject to additional duties. Although the alignment of labour regulations with the EU labour law *acquis* has advanced well in all the three countries, there are still some steps to be taken to enforce the labour law *acquis* in areas like gender quality (Estonia, Latvia) and transposition of EU directives (e.g. involvement of workers in the European Company). Compared to Estonia and Latvia, Lithuania has reached a somewhat more advanced stage in the area of labour law.

Trade unions in the Baltic States, like in all the Central and East European countries, are rather small in terms of both union density and collective agreement coverage. The importance of trade unions has been declining in the CEE and Baltic countries since the beginning of the 1990s. At the end of the 1990s, trade union density was less than 35% in all the transition countries except Slovenia. In the Baltic States, trade union density is even smaller than the CEE countries' average, with the highest density rate in Latvia. Collective agreement coverage in the Baltic States is not much higher than union density. This is mainly due to the small number of sectoral level agreements. Collective wage bargaining in the Baltic States takes place mainly at the enterprise or national level, while bargaining at sectoral or regional level is less developed. Due to the low coverage by collective agreements, it can be concluded that the majority of employees in the Baltic States rely on individual employment contracts.

The Baltic States' labour policies are rather insufficiently funded in comparison with the EU, the share of active measures being relatively low. In Lithuania 40% and in Estonia even 60% of the overall employment policy budget is allocated on passive measures. At the same time, the overall coverage of the unemployed by the sys-

tem of income maintenance is still low in all the three states. The status of the unemployed is regulated and they have several rights. In Latvia the unemployed enjoy higher unemployment benefits than in Lithuania and especially in Estonia, where the benefit is currently so small that an unemployed person has to apply for subsistence benefit as well.

The participation of registered job seekers in active labour market measures is low as well. In accordance with the European Union's employment guidelines the goal is to achieve the involvement rate of 20% of unemployed people. At the moment, the respective number is largest in Estonia — 10%, followed by 4% in Latvia and 3% in Lithuania. It could be concluded that because of the undercapitalization of the labour market policy, unemployment benefits are low and therefore fail to remarkably decrease labour market flexibility. On the other hand, by laying more emphasis on active labour market programmes, a positive impact of labour policy on labour market flexibility could be increased. In this context, more attention should be paid to education and training, including development of lifelong learning which is now an established priority throughout the EU. In Estonia one of the main problems is the poor targeting of the programmes (e.g. the aid to starting business). In Lithuania there is a need to expand active labour market programmes and re-balance provision away from temporary work in favour of training and other measures designed to increase employability. Also passive policies need to be reformed in Lithuania in order to improve coverage, eliminate disincentives, and emphasise activation rather than passive receipt of benefits. The public employment service should play a more active role in reintegrating the unemployed.

Analyzing wage flexibility in the Baltic States, it is possible to admit that on the whole wages are rather flexible, but there are also differences between the countries and economic sectors. Nominal wages are most rigid in Lithuania and most flexible in Estonia. At the same time, minimum wages are lowest in Estonia and highest in Lithuania. The most flexible wages are in the construction sector in all the three countries. In Estonia and Latvia wages are also flexible in fishing, agriculture, and the hotels and restaurants sector. The wages of the public sector and of the financial sector are

mostly rigid. The data also confirm that if the wages are low, they are more flexible. In the context of EU enlargement, it is possible that wages in those sectors where they are most flexible will converge faster with the EU wage level if EU labour market policies are liberalized. It may also happen that if the Baltic States' labour markets become as highly regulated as those of the EU, wage flexibility will decrease in all the three countries, but especially in Estonia. The last option is rather realistic.

In conclusion, we can say that the Baltic States' labour market is flexible, especially in comparison with the EU member states' average. If we compare the three Baltic States with one another, then the Estonian labour market seems to be the most flexible one, closely followed by the labour market of Latvia, whereas the least flexible is the labour market of Lithuania. So the results of our study are in conformity with earlier findings, e.g. Cazes (2002) also found the Central and Eastern European Countries' labour markets to be rather flexible, while Estonia was in respect to most indicators the most flexible one among them. Taking into account that EU eastern enlargement and the requirements of the European Monetary Union (EMU) will increase pressure on flexibility of labour markets, the growth of market disequilibrium is highly probable in the Baltic States, should labour market flexibility decline remarkably.

Why will the labour market of the Baltic States become more rigid? First, the influence of institutions will increase. From the formal point of view, the legal regulation of the labour market seems to be in place and the calculated indexes show that on average the worker is even better protected in the Baltic States than in the EU. However, in practice it is obvious that at the level of firms the state regulations are not always complied with. There is a lot of evidence that these regulations have been violated, at least in the case of Estonia. The influence of institutions will grow because the control over observance of the regulations will increase caused by increasing administrative capacity.

This leads to the second point, the power of trade unions. At the moment, trade unions are very weak in all the three countries. We believe that trade unions are in the process of recovering and their

strength, both in terms of density and coverage, is increasing. Firstly, more workers will start to realise that they need unions and will get organized. Secondly, unions will learn more from the past and will become more attractive and visible in society. Also sister organizations in the Nordic countries and the central EU level organizations will provide help to local trade unions, training local trade union managers, giving financial support, organizing joint seminars, etc. Thirdly, if trade unions start to expand and strengthen, wage flexibility will accordingly decline, because today the collective agreement coverage rates in the Baltic States are extremely low. Fourthly, the state should contribute more to labour policies and the share of active labour market programmes should be increased.

These tendencies will definitely decline the flexibility of labour markets and there exists a danger that in the nearest future we will have to grapple with the same labour market problems (long term unemployment, high labour turnover cost, weak motivation for job search), which are so common for the EU member states. In order to maintain sufficient economic growth, the Baltic States will have to reduce their unemployment rate, in particular, structural unemployment, and increase labour force participation.

Free movement of labour as a natural consequence of EU eastward enlargement will have its impact on market disequilibrium particularly during the first years of enlargement. It will put pressure on the labour markets of the Baltic States due to the possible outflow of better-qualified and flexible labour force. Movers will be mainly people with good qualifications, also young people with a secondary school (gymnasium) education, who cannot find qualified jobs at home. They are ready to work abroad as blue collar workers, getting relatively higher salaries than they would expect to get in their home countries. Analyzing the labour migration problems of the Baltic States, attention should also be paid to the possible cross-border labour movement within the Baltic Sea Region. Cross-border movement is costly to the country of residence, which may lose the income tax revenue from the worker but has to finance the social expenditure and local infrastructure for the benefit of the workers' family. Labour migration from the Baltic States into the EU15 countries will not be significant in the near future.

On the basis of the experience gained from the previous stages of EU enlargement and the predictions that labour migration will not exceed 0.2% of the population, it is possible to estimate that during the first four or five years the migration figures for the Baltic States will be between 52 000–74 000. Over a long-term period (10 years) labour migration will decline.

In our future research we plan to concentrate on analyzing the impacts of different shocks and the influence of labour market institutions on the Baltic States' labour markets. It is interesting to see whether differences in labour market flexibility will lead to labour markets' differing reactions to shocks. This can be done by means of computable general equilibrium models of the Baltic States' economies. Also the issue of wage flexibility needs further investigation by including micro-level data in addition to the macro approach used in the present paper.

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KOKKUVÕTE

Tööturu paindlikkuse ja migratsiooni probleemid Balti riikides

Euroopa Liidu ittalaienemine ja Euroopa Rahaliidu kriteeriumid suurendavad survet tööturgude paindlikkusele nii praegustes Euroopa Liidu liikmesriikides kui ka kandidaatmaades. Kui tööturgude paindlikkus ei suurene, siis on põhjust mõlemas riikide grupis (kuid eriti kandidaatriikides) karta tööturu tasakaalutuse suurenemist. Käesoleva kirjutise eesmärgiks on anda ülevaade põhilistest muutustest Balti riikide tööturgudel perioodil 1995–2001 rõhuasetusega tööturu paindlikkuse ja migratsiooni probleemidele Euroopa Liidu ittalaienemise kontekstis. Mõlemad fenomenid mõjutavad oluliselt Euroopa tööturgu, samas konkreetne mõju varieerub üle riikide. Balti riikide puhul on tegemist erilise regionaalse klastriga, mis annab huvitava võimaluse siirde- ja integratsiooniprotsesside uurimiseks. Balti riikide tegelik mõju Euroopa ittalaienemise protsessile ei saa olla väga suur, tulenevalt nende riikide turgude väiksusest, võrreldes nii Euroopa Liidu praeguste liikmesmaadega kui ka kandidaatriikidega.

Käesoleva kirjutise esimene osa analüüsib tööturu paindlikkuse küsimusi, keskendades tähelepanu palkade paindlikkusele ning institutsionaalsele paindlikkusele (sh tööturu regulatsioonile, ametiühingute osale, tööturupoliitikale). Kirjutise teises osas uuritakse tööjõu migratsiooni probleeme rõhuasetusega migratsiooni tõuke- ja tõmbeteguritele ning Euroopa Liitu ittalaienemise seniste kogemuse analüüsile. Võib öelda, et tööturu paindlikkus on kõigis Balti riikides väga kõrge, olles samas mitmes mõttes (nt palkade paindlikkus) kõrgeim Eestis ja madalaim Leedus. Üleminekuprotsesside käigus on tööturu paindlikkus vähenenud. Ametiühingute nõrkus võrrelduna Euroopa Liidu maadega on aidanud suurendada palkade paindlikkust. Samuti on soovitav tulevikus keskenduda enam aktiivsetele tööturupoliitika meetmetele. Võttes arvesse Euroopa Liidu ittalaienemisest ja Euroopa rahaliidu nõuetest tulenevat survet

tööturgude paindlikkusele, on Balti riikides väga tõenäoline turu tasakaalutuse kasv juhul kui tööturu paindlikkus langeb. Viimane võib aset leida tulenevalt institutsioonide ning ametiühingute mõju suurenemisest ning riigi sekkumise suurenemisest läbi tööturupoliitikale eraldatavate vahendite kasvu. Kui ametiühingud kasvavad ja tugevnevad, on oodata ka palkade paindlikkuse langemist.

Tööjõu migratsioon Balti riikidest praegustesse Euroopa Liidu maadesse ei saa lähitulevikus olema olulise suurusega — hinnanguliselt võiks migratsioon tööjõu vaba liikumise esimesel 4–5 aastal olla Balti riikide peale kokku 10 kuni 18 tuhat inimest aastas. Samas avaldab Euroopa Liidu laienemisest tingitud tööjõu vaba liikumine tõsist survet Balti riikide tööturule seoses parema kvalifikatsiooniga ja paindlikuma tööjõu emigreerumisega — vananeva elanikkonnaga Balti riikides võib see kokkuvõttes suurendada kvalifitseeritud tööjõu defitsiiti. Suuremat mõju avaldavad tööjõu liikumised Balti mere regioonis.

Appendix 1

Calculation of the index measuring the restrictions on dismissals under regular contracts[a]

		Procedural inconveniences		**Notice and severance pay for no-fault individual dismissals by tenure categories**						**Difficulty of dismissal**			
		Proce-dures	Delay in starting notice	Notice period after			Severance pay after			Defini-tion of unfair dis-missal	Proba-tion period	Unfair dis-missal com-pensation at 20 years' tenure	Extent of reinstate-ment
				9 months	4 years	20 years	9 months	4 years	20 years				
Meas-ure in scale 0…6	Latvia	2	0	3	2	1	2	2	2	4	5	1	6
	Lithua-nia	2	0	6	4	2	6	6	2	2	5	2	6
	Estonia	4	0	6	4	2	4	3	2	4	4	1	6
Share in factor 1 (procedural inconveniences)		0.3	0.28	0.02	0.02	0.02	0	0	0	0.25	0.01	0.13	0.02
Share in factor 2 (direct firing costs)		0.02	0	0.02	0.02	0.02	0.41	0.41	0.41	0.01	0.06	0.11	0.37

[a] The measures are estimated on the scale 0…6. Thereafter they are weighted according to their weights in their factors ("procedural inconveniences", "direct costs of dismissal", "notice and probation period"). Finally all three factors are weighted and summed into an aggregate indicator measuring how strict the termination of unspecified term employment contracts is. The weights of individual measures in the factors are found by using factor analysis and data about OECD countries; see Nicoletti, 2000. The procedures for calculating the scales are given in the same source (Nicoletti *et al*., 2000).

	Procedural inconveniences		Notice and severance pay for no-fault individual dismissals by tenure categories						Difficulty of dismissal			
	Procedures	Delay in starting notice	Notice period after			Severance pay after			Definition of unfair dismissal	Probation period	Unfair dismissal compensation at 20 years' tenure	Extent of reinstatement
			9 months	4 years	20 years	9 months	4 years	20 years				
Share in factor 3 (notice and probation period)	0.02	0	0.44	0.44	0.44	0.01	0.01	0.01	0.05	0.4	0.08	0

	Latvia	Lithuania	Estonia	Share in aggregate measure
Factor1	1.94	1.61	2.57	0.44
Factor2	3.57	4.79	4.00	0.30
Factor3	3.22	4.11	3.75	0.26
Aggregate measure	2.76	3.21	3.31	

Appendix 2

Calculation of the index measuring the legal restrictions on using fixed-term employment contracts

		Fixed term contracts			**Temporary work agency (TWA) employment**		
		Valid cases other than the usual objective	Maximum number of successive contracts	Maximum cumulated duration	Type of work for which TWA is legal	Restrictions on number of renewals	Maximum cumulated duration
Measure in scale 0…6	Latvia	6	0	3	0	2	0
	Lithuania	4	0	1	0	2	0
	Estonia	4	0	1	0	2	0
Share in factor 1 (“procedures”)		0.24	0.22	0	0.24	0.22	0.07
Share in factor 2 (“maximum dura-tion”)		0.06	0.12	0.35	0.1	0.08	0.29

Measure	Country			Share in aggregate measure
	Latvia	Lithuania	Estonia	
Factor 1	1.88	1.57	1.76	0.6
Factor 2	1.4	0.75	1.14	0.4
Aggregate measure	1.4	0.75	1.14	

Index	Country								
	Latvia	Lithuania	Estonia	Average of the Baltic States	Average of the EU (1998)[c]	Germany	United Kingdom	France	Italy
Regular contracts	2.8	3.2	3.3	3.1	2.4	3.0	0.1	2.5	3.0
Fixed term contracts	1.8	1.1	1.1	1.3	2.3	2.5	0.3	3.7	3.6
Average[b]	2.3	2.2	2.2	2.2	2.4	2.8	0.2	3.1	3.3

[b] The average is here a simple average of the indexes for regular contracts and fixed-term contracts.

[c] See Nicoletti, 2000. The average of the European Union is the simple average of 14 member countries.

Appendix 3

Advance notice periods and severance pays in the Baltic States in case the employment contract is terminated on the employer's initiative

Table 1

Advance notice periods and severance pays in case of dismissals in Estonia

Length of record with present employer	**Dismissal**		**Liquidation of company, bankruptcy**		**Termination of contract due to employee's incapability to perform work**	
	Notice period	Severance pay	Notice period	Severance pay	Notice period	Severance pay
Up to 5 years	2 months	2 months' average pay	2 months	2 months' average pay	1 month	1 month's average pay
5–10 years	3 months	3 months' average pay	2 months	3 months' average pay	1 month	1 month's average pay
More than 10 years	4 months	4 months' average pay	2 months	4 months' average pay	1 month	1 month's average pay

Source: The Republic of Estonia Employment Contract Act.

Table 2

Advance notice periods and severance pays in case of dismissals in Latvia

Length of record with present employer	**Dismissal**		**Liquidation of company, bankruptcy**		**Termination of contract due to employee's incapability to perform work**	
	Notice period	Severance pay	Notice period	Severance pay	Notice period	Severance pay
Up to 5 years	1 month	1 month's average pay	1 month	1 month's average pay	1 month	1 month's average pay
5–10 years	1 month	2 months' average pay	1 month	2 months' average pay	1 month	2 months' average pay
10–20years	1 month	3 months' average pay	1 month	3 months' average pay	1 month	3 months' average pay
More than 20 years	1 month	4 months' average pay	1 month	4 months' average pay	1 month	1 month's average pay

Source: The Republic of Latvia Labour Law.

Table 3

Advance notice periods and severance pays in case of dismissals in Lithuania

Length of record with present employer	Dismissal		Liquidation of company, bankruptcy		Termination of contract due to employee's incapability to perform work	
	Notice period	Severance pay	Notice period	Severance pay	Notice period	Severance pay
Up to 5 years	2 months	2 (4) months' average pay	2 months	2 months' average pay	2 months	1 month's average pay
5-10 years	2 months	3 (6) months' average pay	2 months	3 months' average pay	2 months	1.5 months' average pay
10-20years	2 months	4 (8) months' average pay	2 months	4 months' average pay	2 months	2 months' average pay
More than 20 years	2 months	6 (12) months' average pay	2 months	6 months' average pay	2 months	3 months' average pay

Source: The Republic of Lithuania Law on the Employment Contract. In Lithuania the higher severance pays (numbers in parentheses) are applied in dismissals other than those due to reduction of the number of employees caused by changes in production or production organization.

Appendix 4

Number of participants in different Estonian, Latvian and Lithuanian labour market programmes

Table 1

Number of participants in different Estonian labour market programmes, 1995–2001

	1995	1996	1997	1998	1999	2000	2001
Registered job-seekers a year (total, in thousands)	**77 294**	**93 649**	**85 890**	**81 638**	**105782**	**120 921**	**136 831**
1. Passive measures	**39 789**	**44 421**	**46 679**	**48 428**	**63 610**	**67 412**	**70 438**
Recipients of unemployment benefit	39 789	44 421	46 679	48 428	63 610	67 412	70 438
As % of registered job-seekers	51.5	47.4	54.3	59.3	60.1	55.7	51.5
2. Active measures	**16 130**	**14 228**	**13 552**	**12 243**	**11 366**	**12 929**	**11 149**
Of them (in %):							
Participants in employment training	60.8	65.7	60.8	65.0	61.8	63.0	91.8
Employed with subsidies to employer	0.8	1.8	1.6	1.1	2.3	1.5	3.3
Employed with subsidies to start a business	2.8	3.2	3.2	3.1	3.8	3.2	3.8
Public works	35.6	28.7	34.4	30.8	32.3	32.3	1.1
Participants in active measures, % of registered job-seekers	**20.9**	**15.2**	**15.8**	**15.0**	**10.7**	**10.7**	**8.2**

Source: Estonian Labour Market Board.

Table 2

Number of participants in different labour market programmes in Lithuania, 1995–2001

	1995	1996	1997	1998	1999	2000	2001
Registered job-seekers per year (total, in thousands)	77 294	93 649	85 890	81 638	105 782	120 921	136 831
1. Passive measures							
Recipients of unemployment benefit (in thousands)	82.3	68.3	58.2	53.9	65.0	77.2	63.5
As % of registered job-seekers	38.5	37.2	30.1	26.4	26.6	30.0	25.4
2. Active measures (in thousands)	**32.7**	**40.9**	**52.3**	**71.4**	**76.1**	**86.3**	**106.6**
Of them (in %):							
Creation of new jobs	4.6	3.2	3.1	2.1	1.7	1.2	1.6
Participants in employment training	43.3	30.3	27.6	22.6	16.6	13.6	18.4
Job clubs	19.1	32.5	36.1	35.9	43.4	49.1	44.0
Public works	31.5	26.4	23.5	30.1	30.6	31.1	32.5
Supported works	–	6.0	9.3	7.6	5.6	2.9	3.6
Start own business	1.7	1.4	0.3	0.2	0.07	0.05	0.06
Participants in active measures, % of registered job-seekers	**15.3**	**22.3**	**27.0**	**35.0**	**31.1**	**33.5**	**42.6**

Source: Lithuanian Labour Exchange.

Table 3

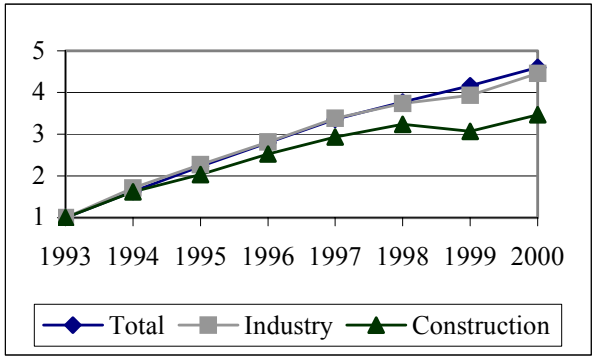
Number of participants in different labour market programmes in Latvia, 1995–2001

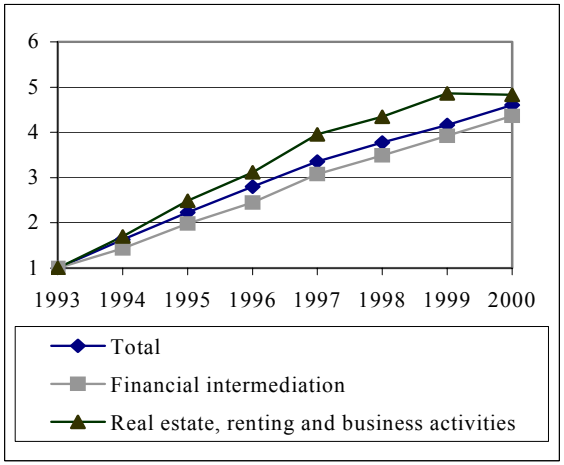
	1995	1996	1997	1998	1999	2000	2001
Registered job-seekers per year (total)	**82**	**81**	**109**	**81**	**119**	**100**	**93**
1. Passive measures							
Recipients of unemployment benefit (in thousands)	27.0	28.7	30.9	30.7	47.7	39.8	37.9
As % of registered job-seekers	32.9	35.6	28.4	37.9	40.1	40.0	40.6

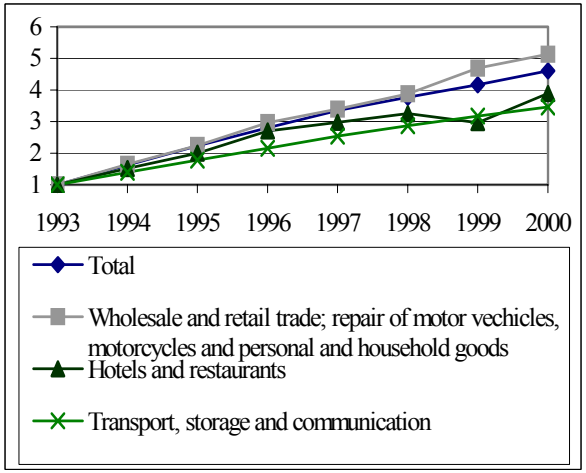
Source: State Employment Service; Ministry of Welfare (Social Report, 2001). Data on active measures were not available.

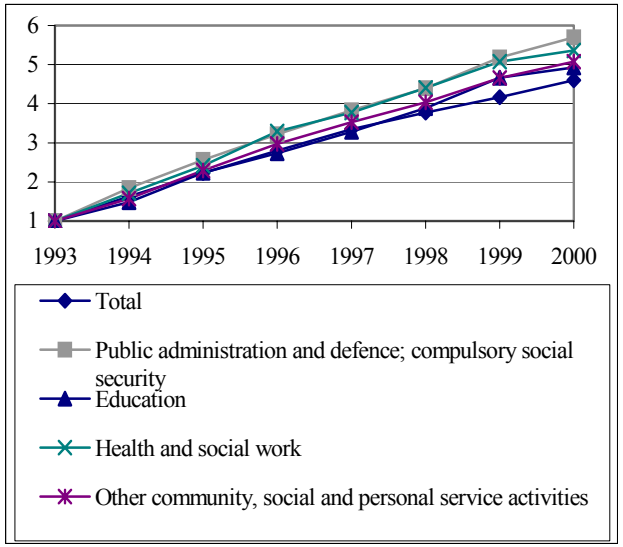
Appendix 5

Gross nominal wages by economic activities — Estonia



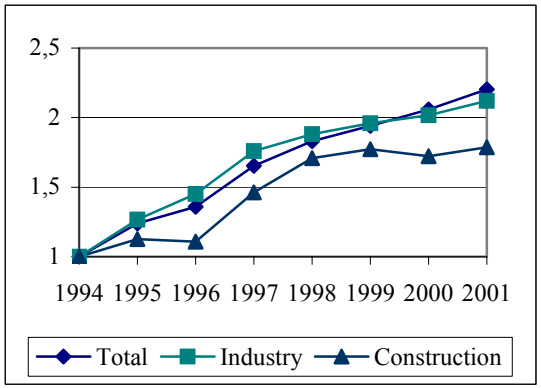


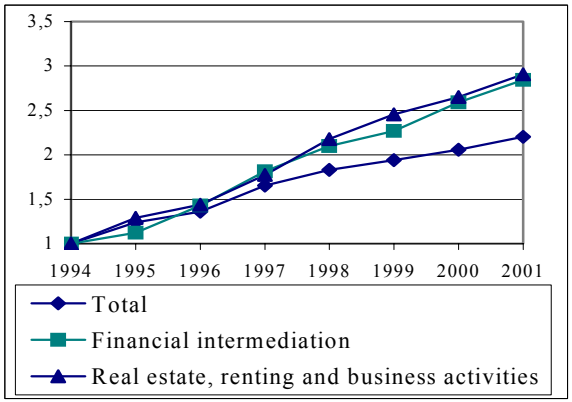

6
5
4
3
2
1
1993
1994
1995
1996
1997
1998
1999
2000
Total
Wholesale and retail trade; repair of motor vechicles, motorcycles and personal and household goods
Hotels and restaurants
Transport, storage and communication

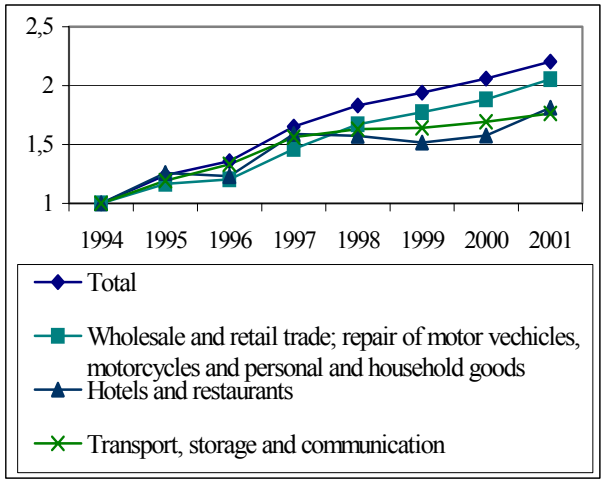

6
5
4
3
2
1
1993
1994
1995
1996
1997
1998
1999
2000
Total
Public administration and defence; compulsory social security
Education
Health and social work
Other community, social and personal service activities

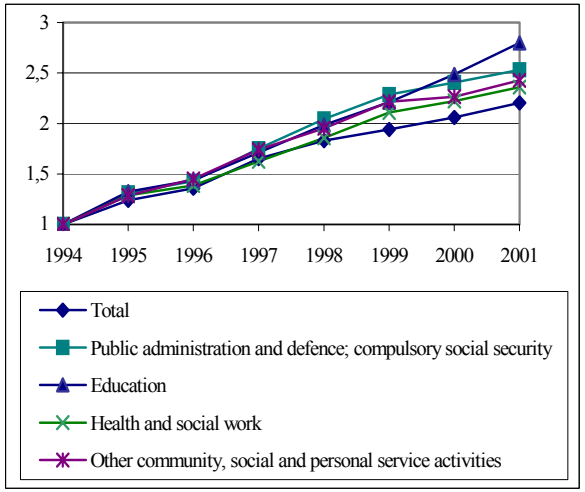
Appendix 6

Gross nominal wage indices by economic sectors — Latvia



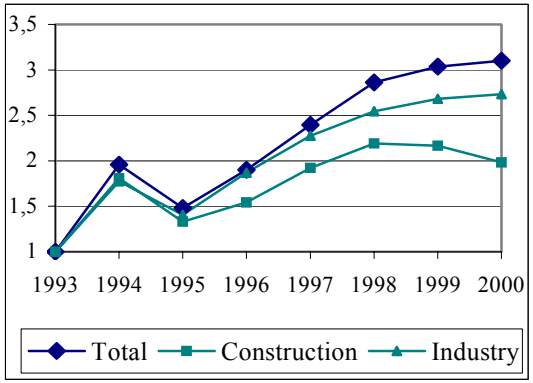


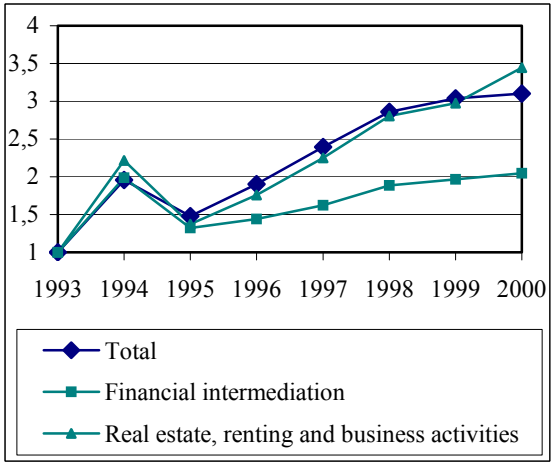

2,5
2
1,5
1
1994
1995
1996
1997
1998
1999
2000
2001
Total
Wholesale and retail trade; repair of motor vechicles, motorcycles and personal and household goods
Hotels and restaurants
Transport, storage and communication

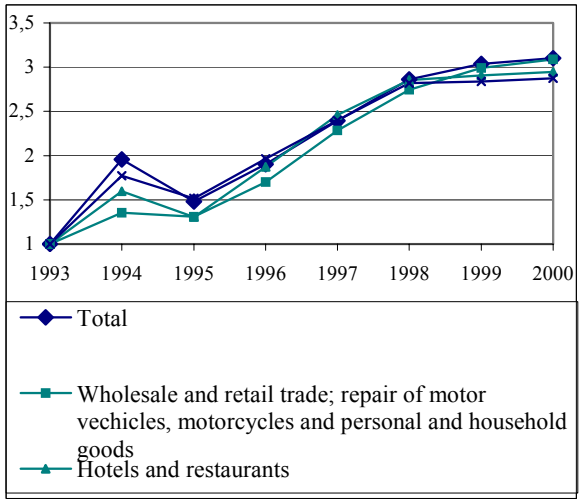

3
2,5
2
1,5
1
1994
1995
1996
1997
1998
1999
2000
2001
Total
Public administration and defence; compulsory social security
Education
Health and social work
Other community, social and personal service activities

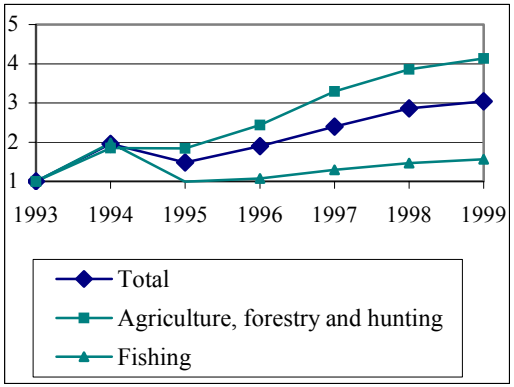
Appendix 7

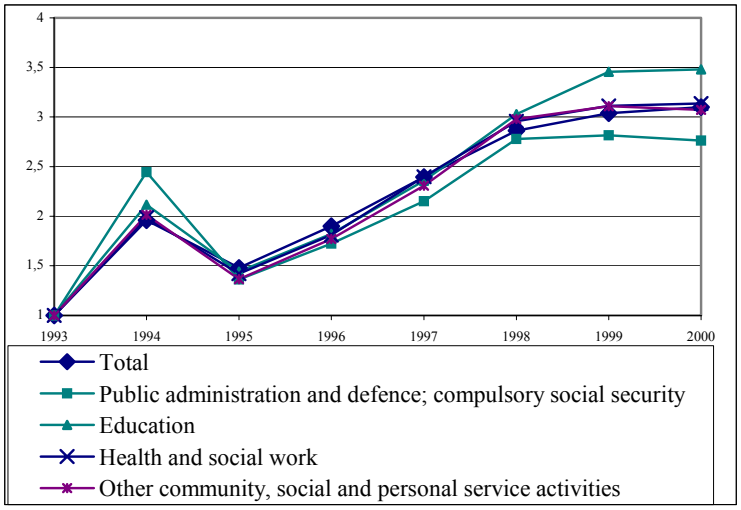
Gross nominal wage indexes by economic activities — Lithuania






3,5
3
2,5
2
1,5
1
1993
1994
1995
1996
1997
1998
1999
2000
Total
Wholesale and retail trade; repair of motor vechicles, motorcycles and personal and household goods
Hotels and restaurants


5
4
3
2
1
1993
1994
1995
1996
1997
1998
1999
Total
Agriculture, forestry and hunting
Fishing


4
3,5
3
2,5
2
1,5
1
1993
1994
1995
1996
1997
1998
1999
2000
Total
Public administration and defence; compulsory social security
Education
Health and social work
Other community, social and personal service activities