Economics Department

LABOUR MARKET REVIEW

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MAIN DEVELOPMENTS IN THE FIRST HALF OF 2008

In the first half of 2008, the further development and duration of the economic cooling became the key issue. As Estonia has little experience with cyclical economic behaviour, the related forecasting is surrounded by a relatively large degree of uncertainty. The reaction of the labour market to the current cyclical deceleration is also important for future economic developments and may either help normalise the situation or aggravate it further.

The current decline of the Estonian economic cycle drastically differs from our earlier experience (which began after the so-called Russian crisis in 1998) and thus, it is difficult to draw any parallels between the developments of labour market indicators[1]. During the previous decline the rate of unemployment rose relatively fast – by 5 percentage points within three years (to 14.6% in the first quarter of 2000). The reaction of this indicator to the current cyclical economic downturn has not yet become apparent and, instead, in the second quarter of 2008 the unemployment rate reached its lowest level in recent years with 4.0% (see Figure 1). Nevertheless, in the near future unemployment is expected to increase, although considerably less than last time. As the experience of other countries has shown, the unemployment rate responds to the cooling of the economy with a 2 to 6 quarter lag.

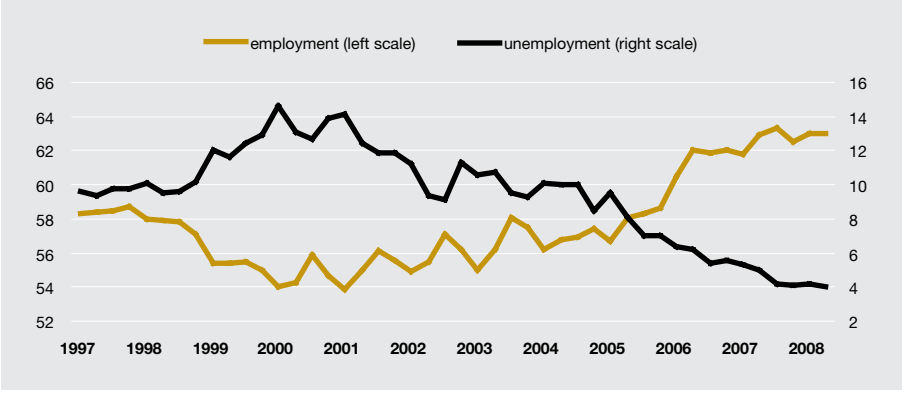

Figure 1. Employment and unemployment (%)

The number of employees and the employment rate should also be more in line with the decreasing demand. In the second quarter of 2008, the number of employees was only 0.3% lower than a year ago, whereas the economic decline posted -1.1%. The preceding hectic growth period was characterised by extensive labour shortage and plenty of vacancies in many companies. Thus, initially the slowdown in economic activity just entailed a decrease in vacant positions and alleviation of the labour shortage problem, not a drop in employment.

[1] Tairi Rõõm "Majandustsükli pöördumise mõju tööturule", Diplomaatia No 57, May 2008.

In the years of rapid growth in labour demand, Estonia's employment rate has increased considerably also on account of these residents for whom it would be more difficult to find a job if the demand for labour was smaller. For instance, in 2006-2007 employment grew by 48,000 people. 26% of them were in retirement age, 17% – young students, 15% – previously discouraged and 20% were long-term (more than two years) unemployed. In the second quarter of 2008, inactivity started growing again, mainly among people in retirement age.

The excessive wage growth that strongly surpassed productivity growth in the past two years raises serious concerns about the flexibility of labour costs. As the economic cycle turned, though, wage growth started to decelerate slightly in the middle of last year. Owing to the large inertia of wage growth, achieving balance with productivity growth should take 6–8 quarters. In Estonia, the pay rises of the public sector in the beginning of 2008 inhibit achieving accordance of these indicators, which from the perspective of the cyclical economic development did not happen at the most suitable time, but should not change the general situation in the long-term. In the second quarter, public sector wage growth slowed, decreasing to 12.2% in June, i.e. over 10 percentage points compared to the February indicator, for instance. In the private sector, wage growth decelerated even more distinctly.

The first half of 2008 witnessed further adjustment of real wage growth, which had started in the last quarter of 2007. The earlier robust growth in domestic demand had mainly been induced by the almost 15% growth in real wages. Later on, wage growth started to ease. Initially, the growth was inhibited only by the accelerating inflation, but in 2008 inflation was accompanied by a slowdown in nominal wage growth. In the second quarter, growth in real wages declined to as much as 3.4%.

At this stage, a further decrease in nominal wage growth is crucial for reducing Estonia's economic imbalances. As it is difficult for the labour market to react flexibly to the waning economic activity through employment and unemployment[2], a bigger adjustment should occur in wage growth. Companies do not rush to cut jobs, because they still remember their recent problems with filling the vacancies, but are restraining the rise in wage costs. Considering Estonia's relatively flexible wage formation (the relatively substantial share of bonuses), a reduction in wage payments cannot be excluded if the economic decline persists.

[2] This is caused by the decreasing number of the working age population, simplicity of migration and small labour reserves.

Table 1. Main labour market indicators

	Change y-o-y (%)						Change y-o-y (thousand)					
	2004	**2005**	**2006**	**2007**	**Q1 2008**	**Q2 2008**	**2004**	**2005**	**2006**	**2007**	**Q1 2008**	**Q2 2008**
Population (as at 1 January)	-0.4	-0.3	-0.2	-0.2			-5	-3.6	-2.3	-2.3		
Employment status (15 to 74 years old)	**2004**	**2005**	**2006**	**2007**	**Q1 2008**	**Q2 2008**	**2004**	**2005**	**2006**	**2007**	**Q1 2008**	**Q2 2008**
Workforce	-0.2	0.1	4.1	0.1	0.3	-1.4	-1.4	0.5	27.2	0.6	1.9	-9.6
Employed	0.2	2.0	6.4	1.4	1.5	-0.3	1.2	11.9	38.9	9.05	9.5	-2.0
Manufacturing	5.1	-0.9	-2.2	-1.2	-2.1	10.5	6.8	-1.4	-3.1	-1.6	-3.0	14.4
Unemployed	-3.9	-17.9	-22.4	-21.0	-20.9	-22.0	-2.6	-11.4	-12	-8.5	-7.6	-7.7
Less than 6 months	-17.2	-12.3	-15.6	-14.6	3.6	-16.8	-4.4	-2.6	-2.9	-2.3	0.5	-2.5
6 to 11 months	-9.8	-38.0	-7.0	-47.2	6.7	58.8	-1.0	-3.5	-0.4	-2.5	0.2	2.0
12 months or more	9.2	-16.0	-30.1	-19.0	-43.0	-42.8	2.8	-5.3	-8.4	-3.7	-8.3	-7.1
24 months or more	7.0	-15.3	-37.4	-21.9	-26.4	-32.2	1.4	-3.3	-6.8	-2.5	-2.8	-2.8
Inactive	0.3	0.1	-6.9	-0.9	-1.5	1.7	1.3	0.3	-27.0	-3.3	-5.5	6.1
Total	0.0	0.1	0.0	-0.3	-0.3	-0.3	0.0	0.8	0.5	-2.7	-3.6	-3.6
	Level (%)						**Change (percentage points)**					
Participation rate	62.9	62.9	65.5	65.7	65.7	65.6	-0.1	0.0	2.6	0.2	0.4	-0.7
Employment rate	56.8	57.9	61.6	62.6	63.0	63.0	0.1	1.1	3.7	1.0	1.2	0.1
Unemployment rate	9.7	7.9	5.9	4.7	4.2	4.0	-0.3	-1.8	-2.0	-1.2	-1.1	-1.0
Wages	**2004**	**2005**	**2006**	**2007**	**Q1 2008**	**Q2 2008**	**2004**	**2005**	**2006**	**2007**	**Q1 2008**	**Q2 2008**
	Level (EEK)						**Change (%)**					
Average gross monthly wages	7,287	8,073	9,350.5	11,260	12,337	13,306	8.4	10.8	16.2	20.4	19.5	15.2
Manufacturing	6,696	7,526	8,823	10,659	11,383	12,166	8.4	12.4	17.6	20.8	16.3	12.3
Average net monthly wages	5,675	6,411	7,524	9,038	10,034	10,711	9.6	13.0	17.4	20.1	20.3	15.6
Minimum wages	2,480	2,690	3,000	3,600	4,350	4,350	14.8	8.5	11.5	20.0	20.8	20.8

LABOUR SUPPLY AND DEMAND

Labour force participation and economic inactivity

In the first half of 2008, the dropping economic activity started to affect decisions regarding participation in the labour force. Although the employment rate remained relatively high (63% in the age group of 15 to 74), the number of the inactive[3] was on the upsurge: in the second quarter there were 359,000 inactive people; that is 6,000 more than a year ago. Inactivity grew mainly due to a rise in the number of the retired: in the second quarter 7,700 pensioners left the labour market. Other reasons for inactivity included health issues, pregnancy, maternity or parental leave (see Figure 2).

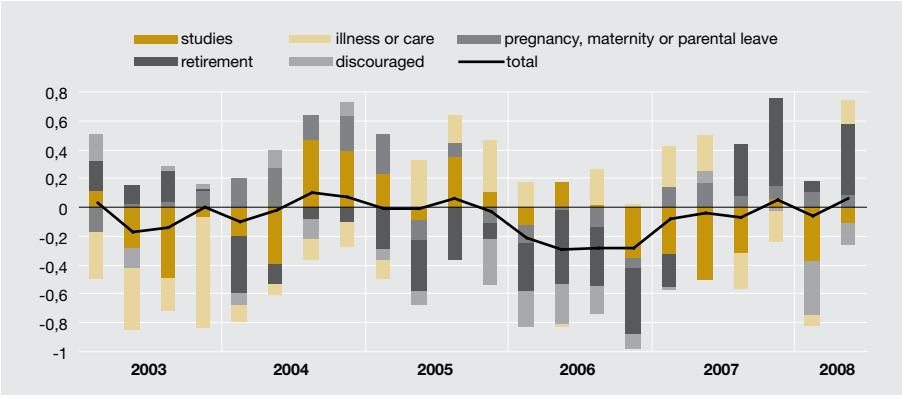

Figure 2. Change in the number of inactive and reasons for inactivity (y-o-y; thousand people)

By regions, the changes in the number of the inactive remained within the usual volatility range. In the second quarter, inactivity grew the most in North-Eastern and Northern Estonia (by 4,800 and 5,100, respectively year-on-year).

In the first half of 2008, the labour participation rate[4] fluctuated only slightly, remaining at the average of the previous year (65.7%), although the number of the working age population (aged 15 to 74) diminished by 3,600 over the year. As inactivity grew, the labour participation rate decreased by 0.7 percentage points year-on-year to 65.5% in the second quarter of 2008.

Year 2007 witnessed the trend of the labour force increasing on account of the young (aged 15 to 24) and the elderly (aged 50 to 74), whereas the number of people in the prime

[3] A person is inactive when he/she does not work and is not looking for work either (the retired, students, homemakers).

[4] The labour participation rate equals the weight of employees and the unemployed in the working age population.

working age dropped. The same trend continued also in the first quarter of 2008. In the second quarter, however, the situation changed and the labour force decreased almost equally in all age groups (see Figure 3).

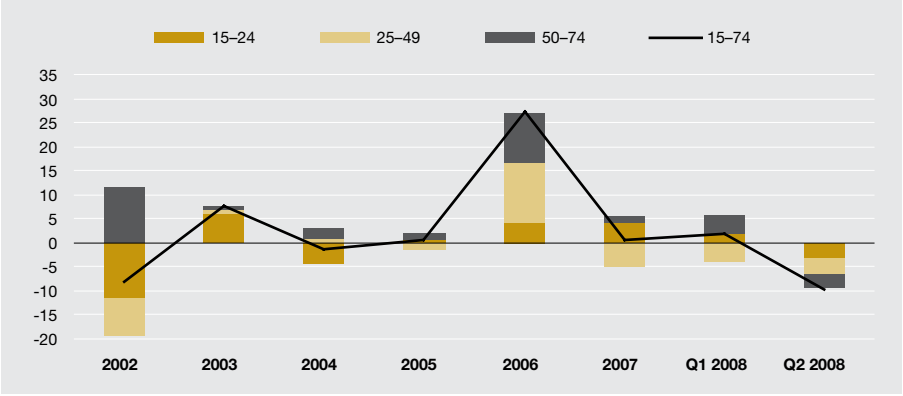

Figure 3. Contribution to employment growth by age groups (thousand people)

By regions, in the first half of 2008 activity increased in Southern and Central Estonia and decreased in North-Eastern and Northern Estonia. The activity rate has been historically the highest in Northern Estonia (almost 69–70%), but it has also fluctuated the most (see Figure 4).

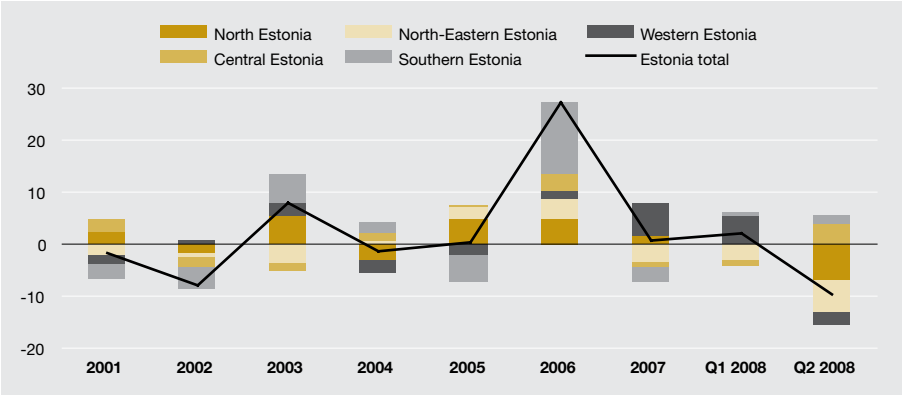

Figure 4. Contribution to employment growth by regions (thousand people)

Demographic changes

Estonia's population decreased also in 2008 and the population aged. The number of the working age population (aged 15 to 74) decreased by 3,600 over the year (excluding migration). According to indirect estimates, the outflow of workers from Estonia started to increase again in the second quarter. Therefore, labour shortage is still an issue. Moreover, finding work as well as workforce both raise problems.

According to a forecast of the Ministry of Economic Affairs and Communications concerning the workforce needs until 2015, labour demand may decrease temporarily due to the cooling of the economy. However, as regards the entire forecast horizon, demographic developments will be affecting the Estonian labour market to a large extent.

The introduction of new technologies calls for workers skilled in handling complex equipment and machinery, but they are currently difficult to find in the labour market. Various fields of activity with increased labour demand are facing the problem of low wage levels that do not attract potential workers, rather than lacking suitable workforce. In the future, labour supply is expected to decrease further, which puts companies under even more pressure.

According to demographic forecasts, in the following years the number of Estonian residents aged 15 to 74 will continue to decrease at an accelerating rate. It does not necessarily entail similar developments in the labour market, because only every tenth person aged 15 to 19 is currently working and among people over 60 years of age less than half of those who would like to work are actually employed or active. If employment or activity rates among women and men remain at their current levels in various age groups, the labour market situation may still be considered relatively stable in the next five years regardless of the general decrease in population.

In order to estimate the loss of labour force, i.e. the number of people leaving the labour market permanently, retirement (due to age as well as other reasons) and death rates have been analysed. In recent years, the mortality rate has decreased in almost every age group in Estonia. On the other hand, compared to developed countries the gap is still relatively large, especially among men. Compared to Finland, the likelihood of death is approximately twice higher in Estonia. The mortality rate might decrease also in the future, but the changes will probably take time.

The retirement figures were based on the data of the labour force survey for 2005–2007 concerning the share of the retired and the inactive owing to illnesses, injuries or disabilities by fields of activity (latest job), gender and age groups. In the case of women, the age of retirement extends every year by half a year.[5]

[5] In 2007 women retired at the age of 60, whereas by 2016 their age of retirement will be equal to that of men, that is 63 years of age (see the State Pension Insurance Act).

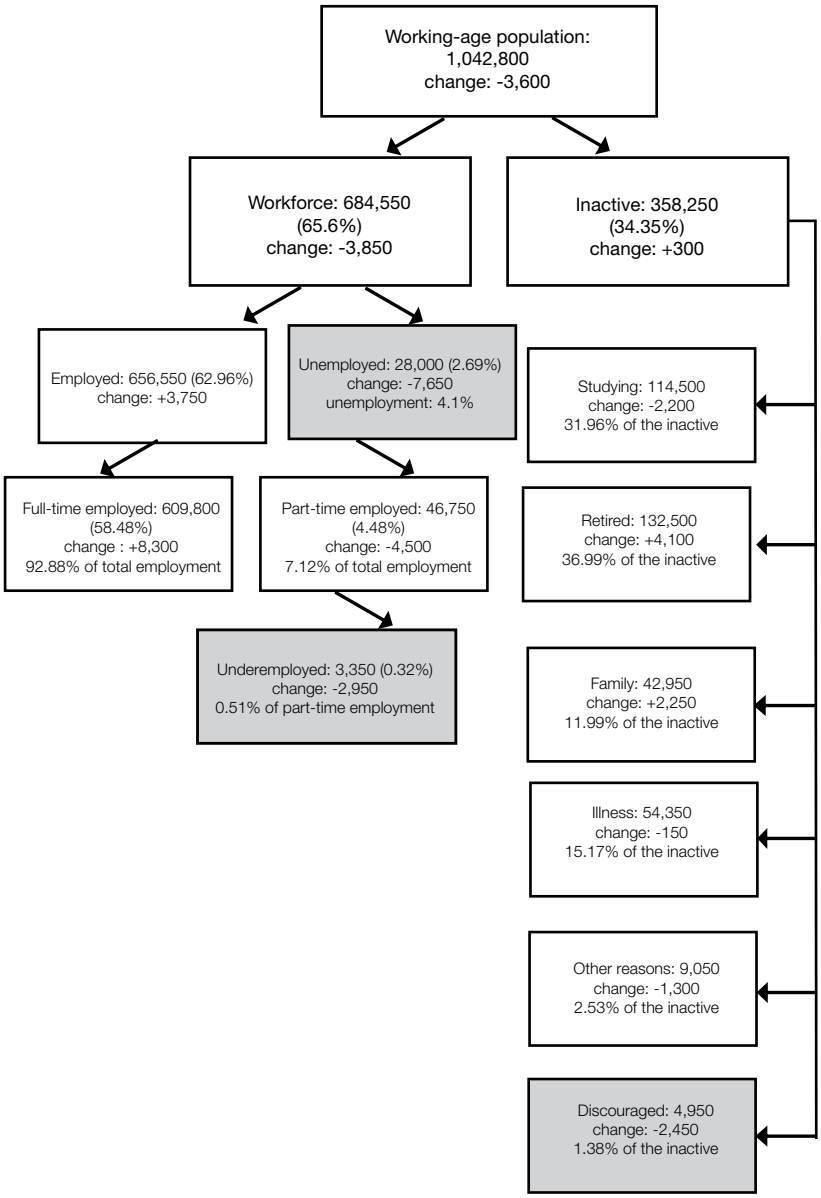

Figure 5. Estonian labour market in the first half of 2008 and change compared to the first half of 2007 (% of working-age population)

Migration in Estonia[6]

In January 2008, Eesti Pank conducted a survey to analyse migration in Estonia. The survey was undertaken due to the scarcity of such data. Unlike most other European countries, Statistics Estonia does not publish statistics on the demographic changes resulting from migration. The aim of this survey was to collect data that would enable to assess the extent of immigration and emigration as well as the structure of emigration.

The survey was based on enquiries conducted via the Internet. Responses were received from the managers of 592 enterprises. In total, these 592 companies have approximately 54,500 employees. Thus, the survey sample comprises about 9% of the Estonian labour force and covered the year 2007. The collected data give an overview of the cross-border movement of employees; that is, emigration from employment and immigration into employment. The survey does not reflect the cross-border movement of the unemployed and the inactive.

The results of the survey were somewhat surprising. Namely, in 2007 the number of foreigners employed in Estonian companies was higher than that of Estonians employed abroad. Nearly 6,400 people who had previously been employed abroad took up employment in Estonia (0.98% of all employees). Meanwhile, approximately 5,000 Estonian residents (0.77% of all employees) went to work abroad. The high figure for immigration partly stems from remigration. Approximately a third of those who came to work in Estonia also originate from Estonia. As the survey does not include the cross-border movement of the unemployed and the inactive, the data do not allow us to conclude that immigration in Estonia exceeded emigration in 2007.

Table 2 gives an overview of the extent of emigration from Estonia, Latvia and Lithuania in the years 2002–2007 to seven major target countries in the European Union (the United Kingdom, Ireland, Germany, Spain, Denmark, Finland and Sweden).

Table 2. Emigration from the Baltic States to seven EU countries

Share of emigrants in population (%)	2002	2003	2004	2005	2006	2007
Estonia	0.26	0.24	0.52	0.60	0.52	0.46
Latvia	0.20	0.19	0.79	1.12	0.90	0.62
Lithuania	0.29	0.27	1.20	1.51	1.24	1.01

Sources: Statistics Finland. Statistics Sweden. Accession Monitoring Report May 2004-June 2008. Department of Social and Family Affairs. Eurostat. Statistics Denmark.

Notes.

1) No data on Germany and Spain is available for 2007. The figures in the table are based on the assumption that emigration to Germany and Spain was as large as in 2006.

2) Data for 2002–2003 do not contain emigrants to the United Kingdom.

3) Data on the United Kingdom and Ireland are based on the number of registered work permits and do not reflect total emigration.

[6] The author of this chapter is Tairi Rõõm.

Emigration to these seven countries surged after the accession to the European Union in 2004 and peaked in 2005. In the following years, emigration gradually decreased. From among the Baltic States, Lithuania has experienced the largest outflow of workforce: since 2004 an average of 1.24% of residents have gone to work in one of the abovementioned target countries every year [7]. The respective indicator for Latvia is 0.86%. In Estonia, emigration has remained more modest compared to our southern neighbours. Namely 0.53% of our residents have taken up employment in the abovementioned countries as an annual average.

According to the migration survey, the majority of emigrants were young people. About three quarters of the emigrants were younger than 35 years of age (see Table 3). Meanwhile, people aged 15 to 34 accounted for 28.4% of Estonia's total employment. Thus, for an Estonian resident under the age of 35 the probability of emigrating to work abroad was about 9 times greater than for a person over that age.

Table 3. Emigrants by age group

Age	Number of emigrants in the sample	Share in total sample of emigrants (%)	Share in employment (%)
Up to 24	81	24.1	9.2
24–34	174	51.8	17.2
35–44	58	17.3	25.9
45–54	21	6.3	28.4
55 or more	2	0.6	19.4
Total	**336**	**100.0**	**100.0**

Among workers with basic education, the share of emigrants was approximately 3 times higher than among those with higher education. According to the survey, 17.3% of the emigrants in 2007 had basic education and 13.7% had higher education (see Table 4). At the same time, people with basic education accounted for 9.8% and those with higher education for 24.2% of Estonia's total employment.

Table 4. Emigrants by level of education

Level of education	Number of emigrants in the sample	Share in total sample of emigrants (%)	Share in employment (%)
Basic education (ISCED levels 0–2)	57	17.3	9.8
Secondary education (levels 3–4)	227	69.0	66.0
Higher education (levels 5–6)	45	13.7	24.2
Total	**329**	**100.0**	**100.0**

In 2007, the majority of emigrants were blue collar workers (86% of all emigrants). About 1.2% of unskilled workers and 1.1% of skilled workers emigrated last year. Among white collar workers the probability of emigration was three times lower: about 0.3% of office workers and 0.4% of top specialists emigrated. The survey results also indicated that emigrants primarily

[7] These data illustrate emigration, which is higher than migration in absolute value.

included private sector employees. Only 3.7% of the emigrants in 2007 had their latest position in a public sector enterprise (see Table 5).

Table 5. Emigrants by group of profession

Group of profession	Number of emigrants in the sample	Share in total sample of emigrants (%)	Share in employment (%)
Unskilled workers	115	34.6	1.2
Skilled workers, technical workers	169	50.9	1.1
Office clerks, public servants	15	4.5	0.3
Highly qualified specialists and managers	29	8.7	0.4
Other	4	1.2	0.1
Total	**332**	**100.0**	**0.7**

70% of the emigrants were men and 30% were women, while the share of men and women in Estonia's total employment is nearly equal. The share of Estonians among emigrants was 63.5% and that of Estonian residents of other nationalities was 36.5%. These percentages are similar to the shares of Estonians and non-Estonians in the employment rate (67.6% and 32.4%, respectively). In Southern Estonia the percentage of emigrants was slightly greater than in other regions.

The results of the survey indicated that in 2007, employment grew partly due to the fact that the immigration of workers exceeded emigration. This is probably an exception to both the previous years and the future. In the final years of the economic boom the Estonian labour market became overheated, which was reflected by a rise in unit labour costs. Overheating brought along workforce shortage: the demand for labour demand exceeded supply in several fields of activity owing to the existing wage levels. However, it is unlikely that the immigration of workers will exceed emigration also in the conditions of the current economic decline. Thus, in 2008 the outflow of workers from Estonia may again be stronger than inflow to Estonia.

The economic climate is not cooling only in Estonia but also elsewhere in Europe, which will probably inhibit emigration, as the demand for labour demand will also decrease in the potential target countries. At the same time, in the near future more Western European countries are going to abolish restrictions to the free movement of labour in the EU. This, in turn, will enhance cross-border labour mobility. By 2011, all EU member states (except Romania and Bulgaria) should provide for the free movement of labour.

Greater cross-border labour mobility will affect wage growth as well as unemployment developments. Regardless of the deceleration of economic growth, in the near future the emigration pressure will also be causing wage rise pressures. However, in the conditions

of an economic decline this is accompanied by the risk that wage growth will exceed productivity growth also in the forthcoming years. On the other hand, better opportunities for workers to find employment abroad mean that as the economic growth slows, the unemployment growth rate will be slightly lower. Domestic employment might decrease – and it probably will – but the loss of jobs will be offset by the fact that people can find work elsewhere.

The more open the European economy becomes, the more the economic cycles of the countries will converge. Thus, in the future this increases the probability that a cyclical downturn in Estonia will be preceded or accompanied by a decline elsewhere in Europe. This limits the opportunities of Estonian workers to go to work abroad if local economic conditions deteriorate. On the other hand, Estonian economic developments have been more volatile than in Western European countries. Although the timing of the cycles here and elsewhere increasingly overlaps, our economic fluctuations will be stronger than in our western neighbours with higher living standards. Consequently, Estonian residents will have relatively better opportunities to find work in Western Europe at the time of an economic decline and less options in an upward phase. Thus, the opportunity to emigrate operates as a stabilising factor for unemployment.

Employment

Estonia's employment witnessed significant changes in the first half of 2008. In the first quarter the number of employees still grew compared to the same period a year ago, although at a slowing rate, whereas in the second quarter the number of employees (656,000) was 2,000 smaller than last year. This means that employment growth was replaced by a decline, although initially it remained rather modest (0.3%). Meanwhile, the number of employees has ranged only marginally over the last four quarters, being quite stable in the first half of 2008. The labour market has responded very weakly to the changed economic situation. If growth remains negative, the number of employees might drop even further, but the extent of the decrease might be smaller than earlier expected.

By economic sectors, the structure of employment has somewhat changed, especially in manufacturing where employment grew by 14,400 in the second quarter. Although employment in construction – the sector with largest contribution to growth in earlier periods – continued to increase, the growth rate was considerably lower. In the first quarter of 2007 growth stood at 38.8%, whereas in the first quarter of 2008 it only posted 10.1%, reaching merely 2.2% in the second quarter and indicating a robust decline in activity in that sector.

In the first half of 2008, employment decreased mainly in transport, dropping 13.9% in the first and 9.7% in the second quarter. The number of employees shrank owing to a decrease in goods transport (including transit) and postal services as a result of the cooling economy. The number of employees also dropped in health care and social welfare. In health care the

employment rate was influenced by the falling number of foreign tourists at health centres and spas. In education the number of employees grew, primarily in the field of paid training.

The real estate market showed further weakening, also affecting employment in that field. Compared to the same period last year, unemployment has dropped mainly on account of the self-employed in the real estate business.

In conclusion, at the backdrop of the relatively minute changes in the general indicator the second quarter faced relatively large structural changes, as the number of employees decreased in the services sector and increased in the secondary sector[8], primarily in manufacturing (see Figure 6).

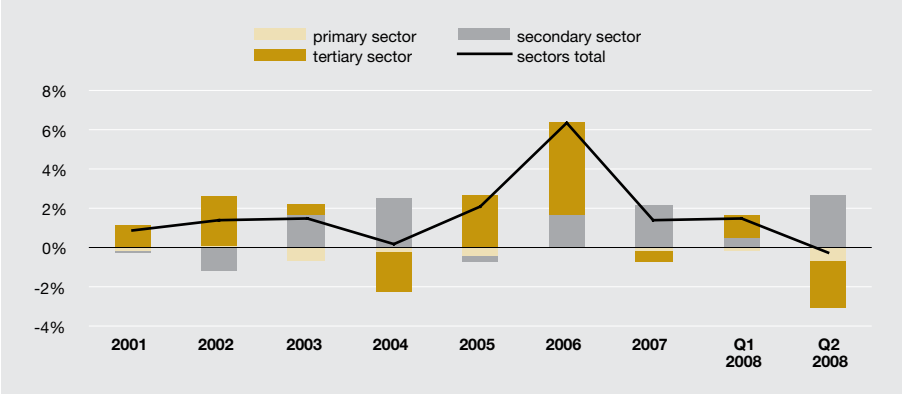

Figure 6. Employment growth and contributions by sectors

According to the new forecast of the Ministry of Economic Affairs and Communications, the total number of employees in 2008–2015 will be virtually similar to the levels recorded in 2005–2007. Additional jobs will be created in the services sector. In the primary sector[9] the employment rate will continue to decline, but at a slower rate. Employment is also expected to decrease slightly in the secondary sector. Employment will presumably grow primarily in the fields with higher labour productivity and fall in those sectors where the value added per employee is below average. However, there are a few exceptions. In several fields with high productivity, production will grow further also in the future, but mainly owing to increasing productivity rather than employment growth.

[8] The secondary sector includes manufacturing, construction, mining and quarrying, and electricity, gas and water supply.

[9] The primary sector includes agriculture and forestry.

By regions, employment changed unevenly. In North-Eastern Estonia employment dropped 6.4% (by 4,900) in the second quarter compared to the same period a year ago, whereas in Central and Southern Estonia it increased 8.3% and 2% (by 5,300 and 3,200) respectively. In other regions the employment rate declined 1–2%.

In the first half of 2008, the demographic structure of employment did not change compared to the previous year. In 2005-2006 employment grew most rapidly among Estonians, whereas in 2007 the number of non-Estonian workers climbed faster (3.6%). In the first quarter of 2008, the employment rate of Estonians increased 0.7% while that of non-Estonians grew 3%. The second-quarter fall in employment concerned only Estonians, whereas the employment rate of non-Estonians did not change.

The decreasing labour demand caused also changes in the structure of part-time or full-time employment. Generally, in Estonia part-time employment is used similarly to other new EU members: approximately 8% of the employees work part-time. In the entire European Union, the number of part-time workers is twice as high; that is about 18%. The share of part-time workers in total employment varies greatly across countries, ranging from 2–3% in Bulgaria and Slovakia to 25% in Sweden, the United Kingdom and Germany, and even to 46% in the Netherlands. However, these indicators are not always stable and may vary slightly along with the ups and downs of cyclical demand.

The strong demand for labour in Estonia in the past two years brought along plenty of new positions, including for part-time workers whose share in total employment increased to 8.2% in 2007. However, the second quarter of 2008 saw the start of a correction in total employment, which also denoted a considerable decline (by over 10,000) in the number of part-time workers. The number of full-time workers, on the other hand, continued growth: by 8,200 in the first and by 8,400 in the second quarter (see Figure 7).

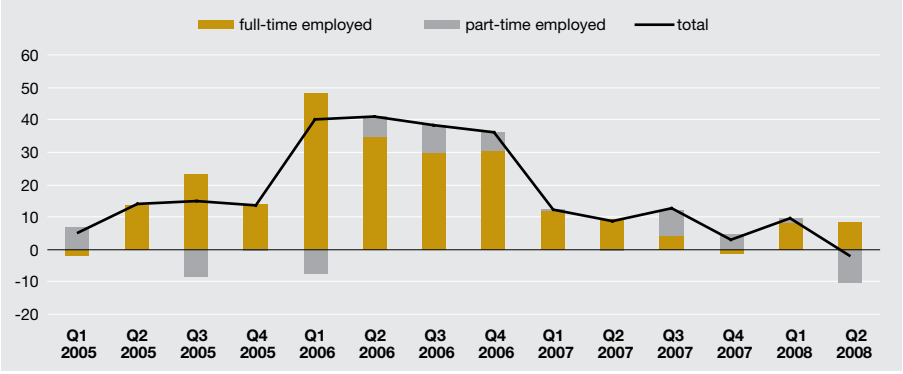

Figure 7. Change in the number of full-time and part-time employees (y-o-y; thousand people)

The comparison of these changes with employment changes across economic branches or sectors indicates that many jobs created in the services and construction sector in 2006–2007 were intended for part-time workers and the decrease in positions in this year's second quarter also concerned these jobs. At the same time, most of the newly employed in manufacturing are full-time workers. All in all, this should mean that all other conditions being equal, the number of average working hours per person employed may slightly increase, which may in turn influence other (deduced) indicators. For instance, the productivity indicator per person employed may increase.

According to the labour force survey, the deterioration of the economic situation only concerned the self-employed. Their number decreased in the first half of 2008, while the number of salaried employees increased (see Figure 8).

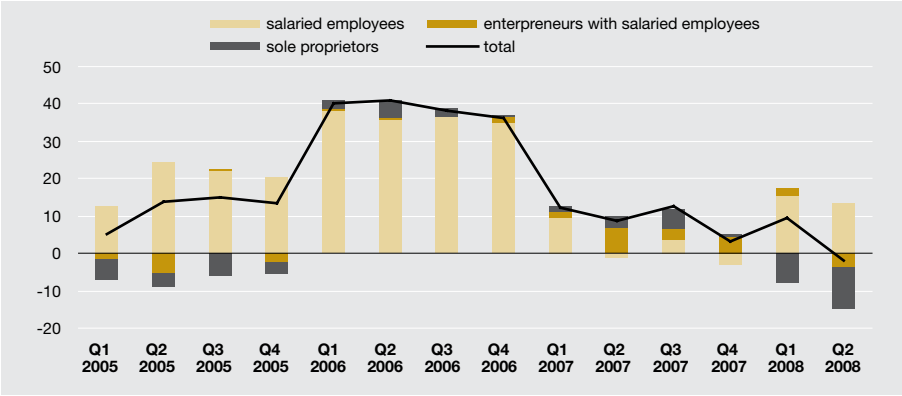

Figure 8. Change in the number of salaried employees and self-employed persons (y-o-y; thousand people)

However, the data of the labour force survey concerning the number of salaried employees do not coincide with the data provided by other databases. For instance, according to the Tax Board database, the number of salaried employees in Estonia is about 30,000 smaller than according to the data of Statistics Estonia (ESA), having decreased by 5,800 in the second quarter. The difference in this indicator between the two authorities, which could earlier have been explained by the so-called unofficial employment forms[10] and the increase in which in 2005–2006 and a decrease in 2007 pointed to either a boost or deceleration in labour migration, respectively, started surging again in 2008 (see Figure 9).

[10] The worker gets paid but does not declare it to the Tax Board.

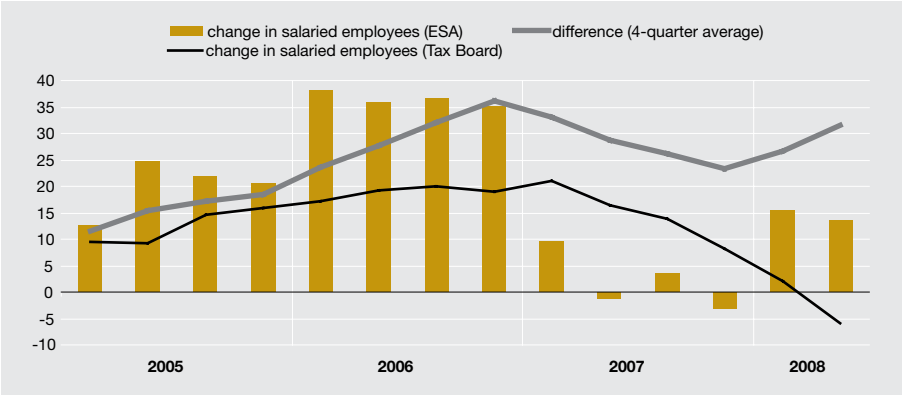

Figure 9. Salaried employees (thousand people)

The resurge of labour migration is also referred to by the employment data of the labour force survey, which differentiates between the concepts of domestic and total employment[11]. Their difference indicates net migration, i.e. the number of Estonian residents working abroad less the number of the residents of other countries working in Estonia (see Table 6).

Table 6. National and domestic employment

	National employment	Growth (%)	Domestic employment	Growth (%)	Difference
Q1 2004	592,000	2.2	587,000	2.3	5,000
Q2 2004	597,000	1.1	591,000	0.5	6,000
Q3 2004	600,000	-1.8	595,000	-1.9	5,000
Q4 2004	604,000	-0.4	596,000	-0.9	8,000
Q1 2005	597,000	0.8	590,000	0.5	7,000
Q2 2005	612,000	2.4	607,000	2.7	5,000
Q3 2005	614,000	2.4	609,000	2.3	5,000
Q4 2005	617,000	2.1	611,000	2.5	6,000
Q1 2006	636,000	6.6	627,000	6.2	9,000
Q2 2006	651,000	6.5	641,000	5.6	10,000
Q3 2006	651,000	6.0	640,000	5.1	11,000
Q4 2006	653,000	5.8	640,000	4.7	13,000
Q1 2007	649,000	2.0	632,000	0.8	17,000
Q2 2007	660,000	1.4	645,000	0.6	15,000
Q3 2007	663,000	1.8	648,000	1.3	15,000
Q4 2007	656,000	0.5	641,000	0.2	15,000
Q1 2008	659,000	1.5	645,000	2.1	14,000
Q2 2008	658,000	-0.3	641,000	-0.6	17,000

Source: Eurostat, authors' calculations

[11] Total employment includes domestic employment and also Estonian residents working abroad; it does not include non-resident foreigners working in Estonia.

In the first quarter of 2007, the negative balance of the net labour migration reached its first peak (17,000 people). Then it dropped to 14,000 persons in this year's first quarter. In the second quarter, total employment decreased by 0.3% year-on-year and domestic employment by 0.6%. This means that 3,000 more people found a job abroad.

At the same time, the labour demand forecast of the Ministry of Economic Affairs and Communications refers to the fact that whereas the labour force survey of 2007 speaks of approximately 15,000 people employed abroad, the data of other countries as well as various estimates indicate a figure two to three times higher (30,000–45,000). According to the labour force survey, over 40% of the people employed abroad were construction workers (almost every tenth construction worker was employed abroad), approximately 15% worked in the transport sector (land and maritime transport) and the share of other fields of activity remained below 10%. Other fields of activity attracting people to work abroad include agriculture, manufacturing transport vehicles (ship-building and repairs, manufacturing motor vehicles), the metallurgical industry, business services (computer software services, rented labour), hotels and restaurants, the trade sector and health care.

Seeking employment abroad is affected by various factors. In Estonia, the main motives to leave are still economic. According to a 2006 survey, 3.9% of Estonian residents aged 15–64% definitely wished to find work abroad and had made preparations for it. In 2007, the desire to work abroad had slightly diminished. The forecast of the Ministry of Economic Affairs and Communications expects the number of people working abroad to reach 20,000–25,000 (under 3% of people aged 15–64) in 2015, which means the figure may drop compared to today. The division of people working abroad by fields of activity is presumed to remain similar to recent years[12].

Vacancies

According to the Labour Market Board's statistics on vacancies[13], the growth rate of labour demand has shrunk remarkably in recent quarters. The number of new vacancy announcements remained lower compared to a year ago and the number of vacancies decreased even faster. In the first half of 2008, the number of valid job announcements submitted to the Labour Market Board was over 30% smaller year-on-year (see Figure 10).

[12] http://www.mkm.ee/failid/T__j_u_vajaduse_prognoos_aastani_2015.pdf (in Estonian only).

[13] The Labour Market Board's statistics on vacancies are not very representative. According to the Statistics Estonia, only 1% of those who found a job during the period under analysis found it through the Labour Market Board.

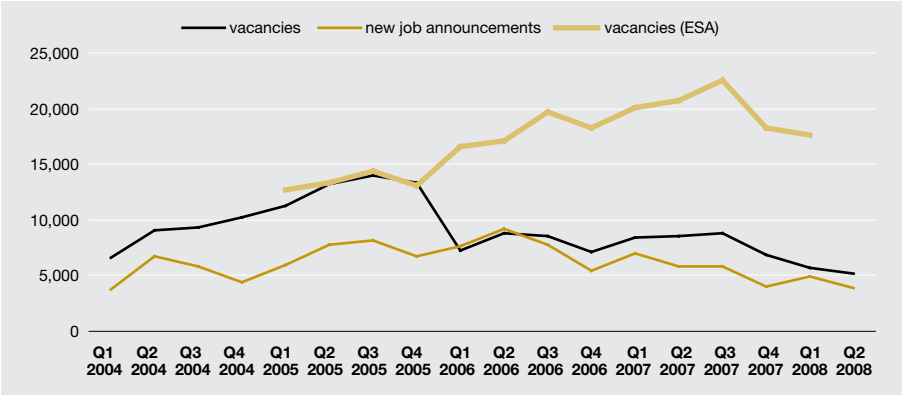

Figure 10. Job announcements submitted to the Labour Market Board

Also the data of Statistics Estonia on vacancies, which include all the vacancies[14] declared on the 15th day of a quarter's second month, refer to a decrease in vacancies.

After the period of economic upturn when the market suffered from extensive labour force shortage and a large number of companies had plenty of vacancies, the drop in activity was initially accompanied by a decrease in vacancies. In other words, this was an alleviation of labour shortage rather than a decrease in the employment rate. If the labour demand continues to drop, labour market indicators should start reflecting the decrease in the number of employees more clearly; meanwhile, the rise of unemployment is expected to remain modest also in the future.

Unemployment

In the second quarter of 2008, the unemployment rate dropped to a record 4.0% and the number of the unemployed fell to 27,300, which is the lowest level in 15 years. The number of the unemployed was 7,700 smaller year-on-year. The developments of the earlier quarters continued, because those who left unemployment did not become employed but economically inactive. Thus, this was not about decreasing available labour resources but giving up active job seeking. Since there occurred no simultaneous increase in discouragement and job migration, these people might return to the labour market when demand increases. In the second quarter, unemployment mainly decreased owing to the growing inactivity of pensioners.

[14] Vacancies resulting from freeing existing positions and new but unfilled positions awaiting a suitable candidate from outside the company (also takes into account part-time vacancies).

Generally, unemployment responds to changes in economic growth with a lag of 2 to 6 months. This time, however, the reaction evoked by unemployment may remain slightly weaker than usual, i.e. it is probable that this time the turn of the cycle will not entail a sharp rise in unemployment. This is avoided by the considerably increased cross-border labour mobility as well as by the decrease in the working age population. This means that in the forthcoming years labour supply will decrease – and not only in Estonia but also elsewhere in Europe. However, it should also be mentioned that if labour demand decreases sharply for a long time, an increase in unemployment will be unavoidable.

At the beginning of 2008, the number and share of the long-term unemployed continued to decline. The growth rate of long-term unemployment accelerated to 42–43% in the first and second quarter. While in the first quarter of 2007 the number of the long-term unemployed was 19,300, in the first quarter of 2008 it only amounted to 11,000 and to 9,500 in the second quarter. Their share in the structure of the unemployed also diminished rapidly (from 47.4% in the second quarter of last year to 35% in the second quarter of this year), because the number of the newly unemployed increased (see Figure 11).

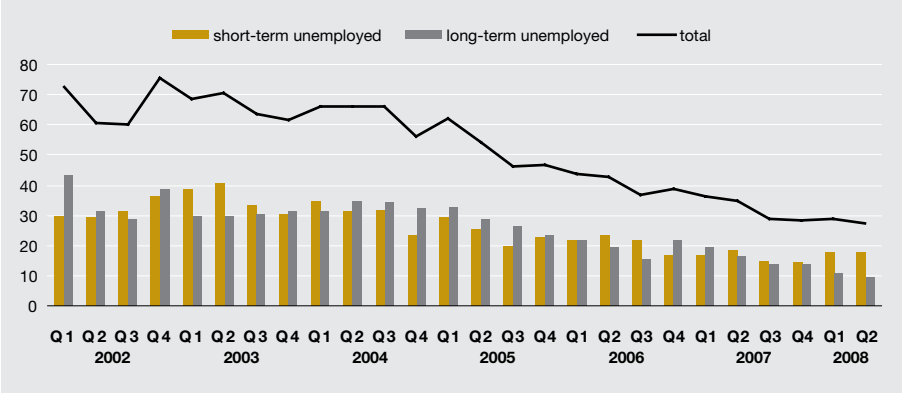

Figure 11. Short-term and long-term unemployed (thousand people)

In the first half of 2008, the number of the unemployed dropped among men as well as women. This time the deterioration of the labour market situation mostly affected the elderly; that is, people aged 50 to 74. Despite the robust drop in unemployment, the number of the elderly unemployed rose by 6.8% in the first quarter of 2008. In the second quarter, in this group the decline in the total number of the unemployed was the smallest – only 3.4% compared to other age groups; meanwhile, the number of the unemployed young shrank by 28% and the number of workers in their prime working age diminished by 24%. In other words, the decline in economic activity also affected the age structure of the labour market: the share of the young and persons in their prime working age grew in employment, whereas the share of the elderly increased among the unemployed and the inactive.

By regions, the unemployment rate decreased relatively evenly. In the second quarter the drop was the most extensive in Central Estonia, where it fell by 2.4 percentage points to 3.9%. The unemployment rate continued to be the lowest in Northern Estonia (2.9% in the first and 3% in the second quarter), and since the second quarter also in Western Estonia (2.4%). In North-Eastern Estonia, the area with the largest unemployment rate, unemployment declined by 1,500 on average in the first half of 2008. The unemployment rate in this area still remained over two times higher than the Estonian average (8.9% in the second quarter).

According to the consumer barometer of the Estonian Institute of Economic Research, households started estimating the likelihood of becoming unemployed to have increased in the final months of 2007. In 2008 this fear continued growing (see Figure 12). In 2006-2007, the fears of households largely remained in line with the changes in the number of the registered unemployed, whereas a large discrepancy appeared at the beginning of 2008. While concerns about unemployment kept surging, the number of the registered unemployed did not increase as dynamically as before.

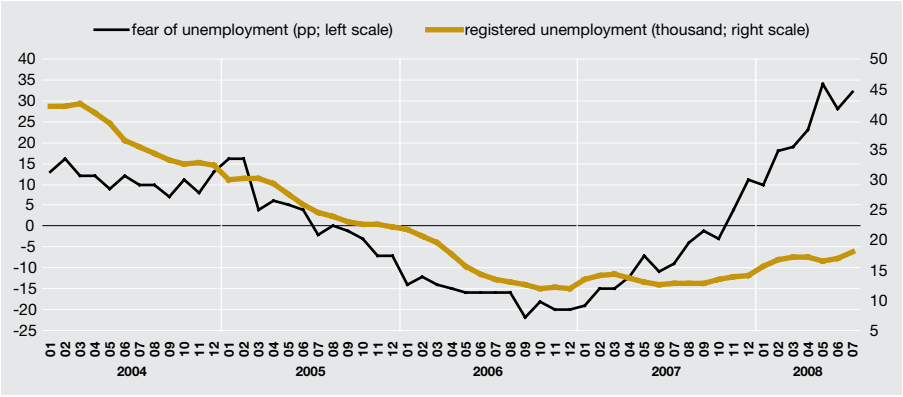

Figure 12. Fear of unemployment and registered unemployment

Source: Consumer Barometer of the Estonian Institute of Economic Research

The ratio between the registered unemployed and total unemployment began changing already in the second half of 2007, when the share of the registered unemployed in the total number of the unemployed started rising rapidly. The number of the registered unemployed increased, but total unemployment decreased. In other words, the fear of unemployment kept surging rapidly, while the number of the registered unemployed increased only slightly and the total official unemployment rate diminished. If finding work is considered more difficult, people also tend to register employment officially more often to obtain social guarantees (e.g. health insurance since 2007).

In Estonia, the number of people who are afraid of losing their job has grown also according to the EMOR survey commissioned by the news editorial department of the Estonian Public Broadcasting. The results of the survey showed that compared to half a year ago, the fear of losing one's job has increased and confidence in the rise of the living standard has decreased. According to the poll conducted in December 2007, 73% of the respondents were confident in keeping their job and 21% were afraid of losing theirs. The results of the survey conducted in June 2008 indicated that 24% of the respondents were afraid of losing their job, while 68% had maintained confidence in keeping theirs.

There was a remarkable difference in the results across the nationalities of the survey participants: 74% of Estonians were confident in keeping their job, whereas among non-Estonians the respective indicator was 59%. 17% of Estonians and 34% of non-Estonians were afraid of losing their job. Meanwhile, younger, more educated and better-paid people continued to feel more confident about keeping their job. 51% of the survey participants thought that they would find a new position fast, should they lose their current job; 44% believed that finding a new job might take longer and 1% would give up looking for a new job.

Disguised unemployment, which is not reflected in official statistics, has probably increased too. Disguised unemployment may occur if the marginal productivity of workers is zero or negative. In that case GDP would be greater if those workers were unemployed or employed in another field of activity where their marginal productivity would be positive. In case of disguised unemployment some people are underemployed and are working part-time, although they would like to work full-time. Working full-time, however, is impossible owing to the labour market situation (e.g. the company does not have enough orders or commodities).

Disguised unemployment also encompasses the inactive, including the discouraged. Since job offers are unfavourable – too few vacancies, low wages are offered – these people do not seek employment at all and generally do not even register themselves as unemployed with the Labour Market Board. However, in case of an attractive offer they are willing to start working immediately.

LABOUR COSTS AND PRICE PRESSURES

Average wages

The labour market began to adjust with the economic downturn through wage growth. In particular, this appeared in the second quarter of 2008, when average gross monthly wages amounted to 13,306 kroons, which is 15.2% more compared to the same quarter of the previous year. In June, wage growth abated to 12.2%. In the first quarter this tendency was not yet so clear and wage growth remained at nearly 20%, year-on-year (see Figure 13).

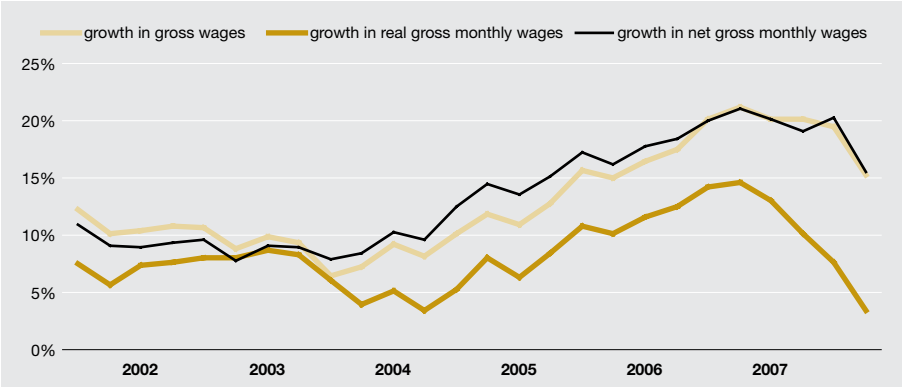

Figure 13. Average wage dynamics

The adjustment of the real wage growth was even more extensive. It began already in the second half of 2007, when compared to the hectic growth of the first half-year, the real wage growth rate decelerated by almost 5 percentage points to 10.1% in the fourth quarter. The drop was caused by a sudden acceleration of inflation (9.1% in the fourth quarter), not the deceleration of nominal wage growth. In the first half-year of 2008, real wage growth slowed further. Since consumer price growth was even more dynamic (over 11%) and nominal wage growth also started to shrink in the second quarter, the moderation of real wage growth was rather sudden: 7.6% in the first and 3.4% in the second quarter.

In the second quarter of 2008, average real wage growth still exceeded labour productivity growth. Even considering labour productivity changes not regarding only the employees or domestic employees, but, for instance, regarding workers transferred to full-time employment, the negative change in the labour productivity indicator was relatively robust and the decrease in the real wage growth followed only later (see Figure 14).

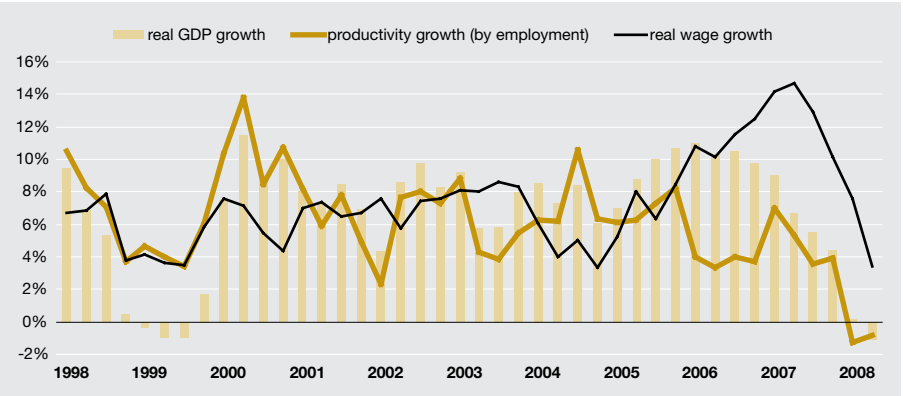

Figure 14. Wage and productivity growth (y-o-y)

Although a certain time lag in the reaction of wage developments to the changes in economic growth may be considered usual (this time it was relatively fast), the fact that wage changes are generally considered to be downwardly rigid raises concerns. This means that they usually react to cyclical declines less than it would be optimal. As wage growth exceeded productivity growth also during the previous economic boom, the decline may cause additional problems to companies whose profitability will decrease even further owing to the climbing costs (at least in the initial phase of the decline).

In the second quarter of 2008, average gross monthly wages increased the most in the primary sector, especially in fishing and forestry (by 51.7% and 29.2%, respectively). Wage growth was considerably faster than average also in education (21.4%). The deceleration of wage growth was mostly influenced by the transport, storage and communications, construction, real estate and financial intermediation sectors. In manufacturing, the growth of monthly wages dropped to 12.3% (see Table 7).

Table 7. Growth in average gross monthly wages by fields of activity (%)

	2002	2003	2004	2005	2006	2007	Q1 2008	Q2 2008
Average	**11.50**	**9.40**	**8.40**	**11.40**	**16.18**	**20.40**	**19.52**	**15.21**
Agriculture	18.30	8.90	13.10	18.00	20.75	26.40	20.93	18.64
Forestry	3.40	13.30	22.90	16.60	9.28	21.10	20.54	29.15
Fishery	19.40	-4.40	-1.40	4.50	54.19	16.80	42.22	51.68
Mining and quarrying	9.00	9.30	6.60	0.60	15.37	27.80	29.25	18.34
Manufacturing	10.00	9.00	8.40	12.80	17.59	20.90	16.34	12.27
Electricity, gas and water supply	8.80	9.30	6.00	13.60	7.78	20.60	21.30	18.72
Construction	12.60	13.50	11.70	14.60	19.10	28.40	19.54	12.23
Wholesale and retail trade	9.80	14.50	2.60	7.10	21.57	19.40	19.02	15.93
Hotels and restaurants	-5.80	17.70	8.50	22.10	12.70	18.00	20.59	17.61
Transport, storage and communications	9.40	4.10	9.30	10.70	13.70	24.00	10.67	12.12
Financial intermediation	8.20	9.80	3.00	9.80	2.41	26.30	17.52	9.79
Real estate, renting and business activities	28.90	-0.40	15.40	6.10	16.15	7.20	15.73	13.24
Public administration and defence	12.70	8.70	8.20	9.60	13.72	24.80	21.38	16.39
Education	12.50	9.40	10.30	11.40	10.26	18.20	23.87	21.44
Health care and social welfare	4.50	15.00	13.90	21.00	14.34	22.00	34.41	16.76
Other	7.40	8.30	14.30	12.20	12.31	22.10	19.25	15.69

In the first half of 2008, wage growth was relatively different across regions as well. Average gross monthly wages increased the most in Ida-Viru (by 30.4% in the first and 22.9% in the second quarter) and Võru Counties (by 33.5% and 21.2%). In Ida-Viru County, however, average gross monthly wages were again lower compared to other counties – only 10,171 kroons in the first half-year. Wages in Valga County also remain below the national average with 9,047 kroons in the first half of 2008. In Võru County, average wages rose to the average national level only in the last three quarters.

Average wages are still the highest in Tallinn and Harju County, reaching almost 15,000 kroons in the second quarter. However, wage growth in Harju County was relatively low in the first two quarters. Thus, the large wage differences between Harju County and other regions decreased even further. Wage growth was the slowest in Lääne County (9.6% in the second quarter).

The situation of economic sectors has also changed in terms of the employer's owner. Before 2007, wage growth was boosted by the private sector, and in 2007 wages increased dynamically in the private as well as the public sector. However, in the first half of 2008 the public sector and local governments took the lead in stimulating wage growth. Private sector wages responded more strongly to the easing in demand. For instance, in the second quarter of 2008 private-sector wages grew by 13.1%; within one quarter their growth slowed down by 4.3 percentage points (see Figure 15).

Wage growth in the public sector is generally more inert and thus responds more slowly to changes in the economic environment, but the differences are not expected to persist in the medium term.

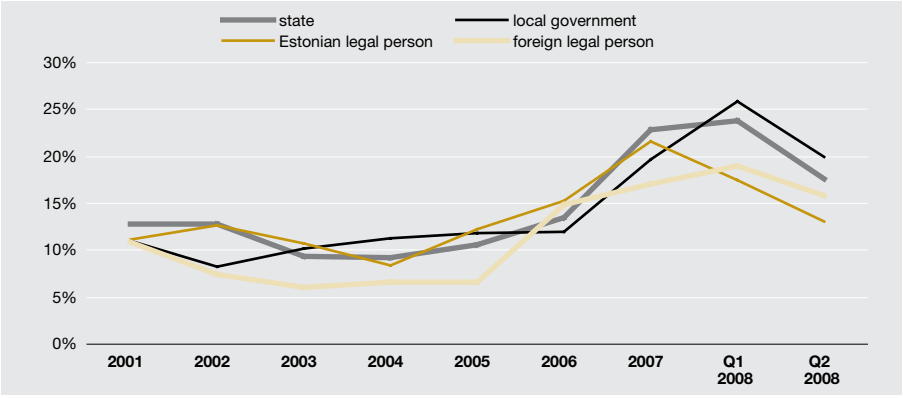

Figure 15. Average wage growth by employer's owner

Unit labour costs

As wage increase exceeded economic growth, the cost of human capital rose relatively rapidly and the share of profit in GDP continued to drop.

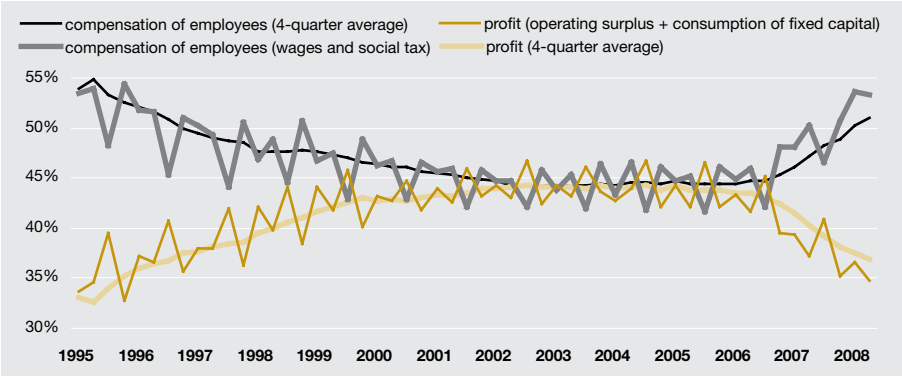

Figure 16. Share of labour cost and profit in GDP

The growth of real and nominal unit labour costs[15] also turned in the second quarter of 2008. In the second quarter, the growth of real unit labour costs decelerated to 5.3% (10.8% a year ago). As nominal productivity growth has not increased at the same time, but has moderated instead, the decrease in real unit labour cost growth was only related to the even faster slowdown in wage growth (see Figure 17).

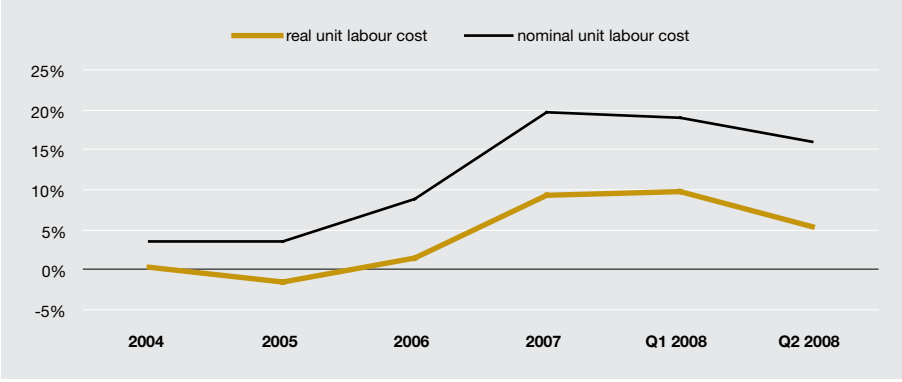

Figure 17. Unit labour cost growth

[15] The real unit labour cost indicator compares the amount of expenditure per employee (mostly wages and taxes on labour) and labour productivity (per employee) at current prices. Practically, the share of the value added spent on wages is calculated. The growth rate of unit labour costs is positive when labour costs per salaried employee grow faster than labour productivity in nominal terms. When real unit labour costs increase, it normally indicates a decrease in the employer's profit share in the value added (GDP).
Nominal unit labour costs compare labour costs per employee with real productivity, not with productivity calculated at current prices.

Nominal unit labour cost growth also decelerated in the second quarter, nearly as much as real unit labour cost growth; that is, by approximately 5 percentage points (from 21% in the second quarter of 2007 to 15.9% in the second quarter of 2008). Although unit labour cost growth is still rapid, the trend has turned and growth has slowed.

By economic sectors, in the first half of 2008 real unit labour costs grew faster than average in the fields of electricity, gas and water supply, transport, storage and communications, and real estate. Financial intermediation, on the other hand, recorded a decline in 2008, caused by the increased value added as well as the reduced benefits to employees (see Table 8).

Table 8. Unit labour cost growth by GDP statistics (%)

	2005	2006	2007	Q1 2008	Q2 2008
Real unit labour cost growth					
Total economy	-1.6	1.6	9.2	9.9	5.3
Primary sector	5.7	-0.2	26.4	-0.7	11.8
Secondary sector	-1.2	2.4	7.6	4.6	5.7
Private sector service providers	-2.5	4.8	14.1	8.0	5.8
Nominal unit labour cost growth					
Total economy	3.3	8.1	18.9	19.1	15.9
Primary sector	16.0	6.1	45.1	8.7	13.7
Secondary sector	3.4	10.0	17.2	12.5	12.3
Private sector service providers	0.0	9.9	20.9	20.1	17.6

Source: Statistics Estonia, authors' calculations

In manufacturing, real unit labour costs have grown quite modestly over the years. Maintaining the competitiveness of manufacturing companies is especially important for the economy since a large part of their production is exported. In the first half of 2008, real unit labour costs increased in manufacturing by 3.4% on average.

INSTITUTIONAL DEVELOPMENTS OF THE LABOUR MARKET

Owing to the poorer economic development outlook, several planned measures to further social benefits in 2009 have been cancelled. These include, for instance, raising the child allowance for the third and every next child and the planned increase in the child care allowance from the current 600 to 800 kroons, which is paid since the ending of the parental benefit until the child's third birthday.

Another measure cancelled is the rise of the unemployment benefit from the current 1,000 to 1,700 kroons. It used to be 400 kroons per month, but increased to nearly 1,000 kroons over the past two years. Unemployment benefits are provided for unemployed persons who, prior to registration as unemployed, have been employed or engaged in an activity equal to work for at least 180 days over the past 12 months and whose income is less than the amount of the unemployment allowance. Unemployment benefits are paid for a period up to 270 days. Since January 1, 2007, all the registered unemployed are also entitled to health insurance.

The school allowance, paid once a year, is also cancelled. This year it was 450 kroons.

Moreover, the government decided to freeze the income tax reform by postponing the reduction of the income tax rate and the rise in the non-taxable income threshold for a year. As of 2009, the VAT differences on periodicals, books and pharmaceuticals will be raised from the current 5% to 9% and the VAT on culture will be raised to 18%.

Pensions

Old-age pensions are provided for persons who have attained 63 years of age and whose pension qualified period is at least 15 years and has been earned in Estonia. The age limit provided by law applies to men since 2001; for women it will be fully applied by 2016, when women born in 1953 retire. The gradual equalisation of women's retirement age to men's takes place through a 6-month age cycle[16].

On January 1, 2008 Estonia had 381,121 pensioners with women comprising 63% of them. At the beginning of 2008, the retired accounted for 28.4% of the total population, whereas this number has been steadily growing over the years following the pension reform (27.6% in 2000). Over 75% of the retired are old-age pensioners, totalling 290,903 at the beginning of 2008 (677 less than a year ago).

[16] This means that while women born in 1947 were entitled to retire at the age of 60, women born in 1948 are entitled to retire at the age of 60.5, etc.

In the second quarter of 2008, the average calculated pension[17] stood at 4,100 kroons, having grown by 2.93 times in eight years. Last year witnessed the so-far strongest average pension growth – 29.8% in the second quarter, year-on-year. The old-age pension was 11% higher than the average pension, amounting to 4,555 kroons per month. In 2001, the difference between the two was 6.2%. Considering the deceleration of income and inflation growth, the rise in pensions will exceed income growth also in 2009.[18]

In 2009, the procedure for pension payments will change and pension as well as state allowance payments will be made to bank accounts. The possibility of home delivery on the expense of the state will be exceptional; otherwise the recipient will have to pay for home delivery.

On September 1, 2008 the Estonian-Latvian agreement regulating the payment of pensions for the Soviet period entered into force. In total, this agreement concerns about 1,000 people in Estonia and Latvia. Pursuant to the new agreement the person will receive pension from the country where the insurance period obtained by that person is longer. If the length of employment is equal in both states, the Soviet employment period will be paid for by the country where the person was insured the most recently. EU countries generally apply the principle that the retired person will receive pension from every country of his or her employment based on the period of employment in that country.

Parental benefits

As of 2009, parental benefits will increase for all beneficiaries including those receiving a benefit in the amount of minimum wage as well as those entitled to a maximum benefit.

55% of the beneficiaries receive benefits in the amount of their wages. If a parent did not work before, the benefit assigned in 2008 was 3,600 kroons. Next year it will be raised to 4,350 kroons. If a parent did work before, but his/her average wage remained below the minimum wage, he/she is entitled to a benefit equivalent to minimum wage.

Based on last year's data, the government established the average income subject to social tax in Estonia per calendar month at 10,234 kroons, which serves as a basis for calculating the maximum amount of the monthly parental benefit in 2009. The maximum amount of the benefit in 2009 will be three times the average income per calendar month; that is, 30,729 kroons. This is 5,520 kroons or 21.9% more than in 2008 (25,209 kroons). In July 2008, 4.9% of the beneficiaries were entitled to the maximum amount.

[17] The calculation encompasses all pension types.
[18] This calculation is based on the data of 2008 concerning social tax collection and inflation.

Minimum wages

In bilateral negotiations with the Estonian Employers' Confederation (ETKL), the Board of the Confederation of Estonian Trade Unions (EAKL) decided to propose raising the minimum wage in 2009 to 5,250 kroons per month (to 31,40 kroons per hour). Thus, minimum wages will be raised by 900 kroons (20.7%) from the current 4,350 kroons.

EAKL found it necessary to raise minimum wages faster compared to average wage growth. Their nearest goal is to raise the share of minimum wages to 37% of average wages instead of the current one-third. Additional reasons mentioned were the impending price increase of pharmaceuticals, the scheduled tax rises and also the abolishment of the school allowance. The fact that wage growth contributes to domestic demand and general improvement of the economic environment was also considered important. ETKL is yet to disclose their official figure, but comments suggested a wage rise in the amount of 100–150 kroons.

Comparison of labour market policies

According to the Eurostat, in comparison to other European Union Member States, three years ago Estonia spent the least on labour market policies measures in relative terms. In 2005 EU countries allocated 2.11% of GDP on average on measures targeted to help the unemployed and other disadvantaged residents return to the labour market, whereas Estonia's respective figure was 0.19%.

The highest expenditures on labour market policies were registered in Denmark (4.1% of GDP), Belgium (3.5%) and the Netherlands (3.4%). Latvia spent 0.54% and Lithuania 0.34% of GDP on labour market measures.

According to the methodology of the Eurostat, labour market policies involve three kinds of expenditures related to the labour market: services, measures and benefits. The EU average amounts allocated for the abovementioned expenditures were 0.23%, 0.53% and 1.36% of GDP, respectively. Estonia's respective indicators posted 0.02%, 0.05% and 0.12% of GDP.

SUMMARY

- In 2008, the further development and duration of the economic cooling has become the key issue. The reaction of the labour market is crucial for further developments.
- The unemployment rate has not yet responded to the current economic downturn and dropped to 4.0% in the second quarter of 2008 instead. In the near term, unemployment is expected to increase, although considerably less than before. The unemployment rate will respond to the cooling of the economy with a 2 to 6 quarter lag.
- The number of the unemployed and the employment rate should be more in line with the easing demand. In the second quarter the number of employees was only 0.3% lower than a year ago, whereas the economic decline posted -1.1%. It is also worth mentioning that the slowdown in economic activity just entailed a decrease in vacant positions and alleviation of the labour shortage problem, not a drop in employment.
- In the years of rapid growth in labour demand, Estonia's employment rate has increased considerably also owing to on account of these residents for whom it would be more difficult to find a job if the demand for labour was smaller. In the second quarter of 2008, inactivity started growing again, mainly among people in retirement age.
- The excessive wage growth that strongly surpassed productivity growth in the past two years raises serious concerns about the flexibility of labour costs. However, wage growth has started to slow after the turn of the economic cycle. Owing to the large inertia of wage growth, achieving balance with productivity growth should take 6 to 8 quarters. The deceleration of wage growth has been faster in the private sector.
- The first half of 2008 witnessed further adjustment of real wage growth. The earlier robust growth in domestic demand had mainly been induced by the almost 15% growth in real wages. Later on, wage growth started to ease. Initially, the growth was inhibited only by the accelerating inflation, but in 2008 inflation was accompanied by a slowdown in nominal wage growth. In June, real wage growth abated to 12.2%.
- Real unit labour cost growth also decelerated in the second quarter: to 5.3% from 10.8% a year ago. As nominal productivity growth has not increased at the same time, but has moderated instead, the decrease in real unit labour cost growth was only related to the even faster slowdown in wage growth.
- At this stage, a further decrease in nominal wage growth is crucial. As it is difficult for the labour market to react flexibly to the waning economic activity through employment and unemployment, a bigger adjustment should occur in wage growth.
- Rapid legislative proceeding with and entry into force of the new Labour Market Act is of high significance. Global price hikes and cyclical economic changes are inevitable. However, Estonia's economic potential should improve in order to respond flexibly to these changes. The most crucial aspect is the flexibility of the labour market so that labour resources would be employed more effectively. In the long run, this should stimulate economic activity and income growth.

Table 9. Estonian labour market

			2004	2005	2006	2007	Q1 2008	Q2 2008
Population (as at January 1)	thousand		1,351.1	1,347.0	1,344.7	1,342.4		
Employment status (15 to 74 year-olds)		**2003**	**2004**	**2005**	**2006**	**2007**	**Q1 2008**	**Q2 2008**
Workforce	thousand	660.5	659.1	659.6	686.8	687.4	685.2	683.9
Employed	thousand	594.3	595.5	607.4	646.3	655.3	656.5	656.6
Unemployed	thousand	66.2	63.6	52.2	40.5	32.0	28.7	27.3
Inactive	thousand	387.4	388.7	389	362.3	359	357.6	358.9
Total	thousand	1,047.8	1,047.8	1,048.6	1,049.1	1,046.4	1,042.8	1,042.8
Labour participation rate	%	63.0	62.9	62.9	65.5	65.7	65.7	65.6
Employment rate	%	56.7	56.8	57.9	61.6	62.6	63.0	63.0
Unemployment rate	%	10.0	9.7	7.9	5.9	4.7	4.2	4.0
Employed by fields of activity		**2003**	**2004**	**2005**	**2006**	**2007**	**Q1 2008**	**Q2 2008**
Agriculture, forestry and fishery	thousand	36.7	35.0	32.2	31.1	30.9	26.1	25.0
Mining and quarrying	thousand	5.7	8.0	5.9	5.2	5.5	5.8	6.8
Manufacturing	thousand	134.1	140.9	139.5	136.4	134.8	143.5	151.0
Electricity, gas and water supply	thousand	10.2	12.0	12.5	12.4	9.5	8.5	9.7
Construction	thousand	42.9	46.8	48.7	62.8	80.9	79.9	84.4
Wholesale and retail trade	thousand	80.8	80.0	80.6	88.7	88.1	94.8	85.7
Hotels and restaurants	thousand	17.4	16.2	22.1	22.3	22.8	21.7	25.7
Transport, storage and communications	thousand	56.2	51.5	54.6	61.5	58.4	50.8	56.6
Financial intermediation	thousand	7.6	7.9	6.9	7.3	9.4	9.7	8.7
Real estate, renting and business activities	thousand	44.4	39.4	46.4	48.1	49.5	48.5	45.5
Public administration and defence	thousand	34.5	36.9	37.2	39.0	39.2	38.8	36.7
Education	thousand	56.9	54.5	54.9	58.5	54.5	63.9	57.4
Health care	thousand	36.4	37.5	35.0	37.5	36.4	29.4	31.1
Other	thousand	30.4	28.8	31.1	34.3	35.6	35.2	32.4
Unemployed by duration of unemployment		**2003**	**2004**	**2005**	**2006**	**2007**	**Q1 2008**	**Q2 2008**
Less than 6 months	thousand	25.6	21.2	18.6	15.7	13.4	14.5	12.4
6 to 11 months	thousand	10.2	9.2	5.7	5.3	2.8	3.2	5.4
12 months or more	thousand	30.4	33.2	27.9	19.5	15.8	11.0	9.5
24 months or more	thousand	20.1	21.5	18.2	11.4	8.9	7.8	5.9

Inactive by reason of inactivity		2003	2004	2005	2006	2007	Q1 2008	Q2 2008
Studies	thousand	119.5	123.1	126.1	124.4	117.7	115.3	113.7
Illness or disability	thousand	44.9	43.3	47.0	51.3	51.8	54.6	54.1
Pregnancy, maternity or parental leave	thousand	22.7	27.2	27.1	23.8	26.5	27.9	28.3
Taking care of children or other family members	thousand	14.8	13.7	14.0	13.9	13.6	15.9	13.8
Retirement age	thousand	152.8	149.4	145.4	129.5	132.9	128.6	136.4
Discouraged people (lost hope to find work)	thousand	18.1	17.7	14.7	7.2	7.3	5.4	4.5
Other	thousand	14.5	14.4	14.6	12.2	9.2	10.0	8.1
Workforce by level of education		**2003**	**2004**	**2005**	**2006**	**2007**	**Q1 2008**	**Q2 2008**
First level and less	thousand	71.6	73.2	65.1	75.3	72.5		
Second level	thousand	383.7	375.6	367.4	376.4	383.4		
Third level	thousand	205.1	210.3	227.0	235.0	231.5		
Vocational secondary education	thousand	71.0	70.0	67.6	70.5	70.3		
Higher education	thousand	134.1	140.4	159.5	164.6	161.2		