

2.3. Employment, Unemployment and Wages

- **Unemployment was affected by cyclical as well as structural factors**

Rising since 1997, the unemployment rate hit double-digit figures in the last period becoming one of the major concerns over the unbalanced trends in the economy. A wide range of macroeconomic circumstances and structural factors shapes the labour market. The most important ones in this respect are the current stage of the business cycle, which the domestic or European economy finds itself in, the extent to which the supply of and demand for labour coincide, the cost of labour and whether the spatial and professional mobility of labour force is sufficient. The aspects influencing the rate of unemployment that are of no lower significance include the relation between wages and productivity, the process of substitution of labour for capital or alternatively for advanced technologies, and the magnitude of preference for leisure.

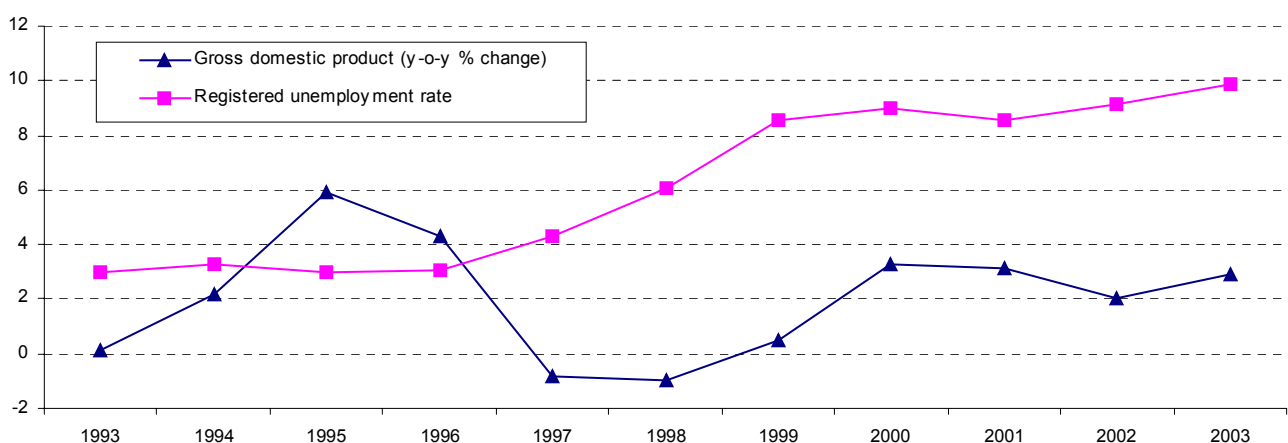
- **Unemployment soared during the 1997-1999 recession**

Throughout the 90's the labour market was heavily impacted by the business cycle. During the expansion in 1994-1996 the unemployment rate was staying close to a very low 3 % level coupled with an increase in employment in excess of 1 % p.a. This was due to delays in restructuring on the one hand, and the ability of the undersized services sector to absorb the existing excess labour supply on the other.

In the midst of the downturn that occurred in 1997-1999, the consolidation of the business sector that was underway resulted in the registered unemployment rate climbing up as high as 8.5 % in 1999. Down by 1 p. p. compared with the average rate recorded in the previous period, a rather lower GDP growth led to a 1.9 p. p. increase in the unemployment rate. At the same time employment was on the decline, with the reduction topping 2 % year-on-year in the final year of the recession (1999). Tight macroeconomic policy, both monetary and fiscal, had a major effect on the course of unemployment by impacting on the creation of new jobs.

The expansionary stage of the business cycle over 2000-2003 can be thought of as encompassing two sub-periods. In the years 2000 and 2001 with GDP growth surpassing 3 %, the unemployment rate was still on the rise in the former year due to a time lag, but in the latter dropped to the 1999-year level. The labour market responded to the economic slowdown in 2002 and 2003's first half by pushing the average unemployment rate up to 9.9 %, followed by 10.3 % at year-end of 2003, and 10.8 % in January of 2004. The development was influenced by both cyclical development, i.e. EU's sluggish performance, and structural factors.

Graph 1 Unemployment and GDP Developments



- **The tertiary sector's ability to absorb idle labour force came to a halt**

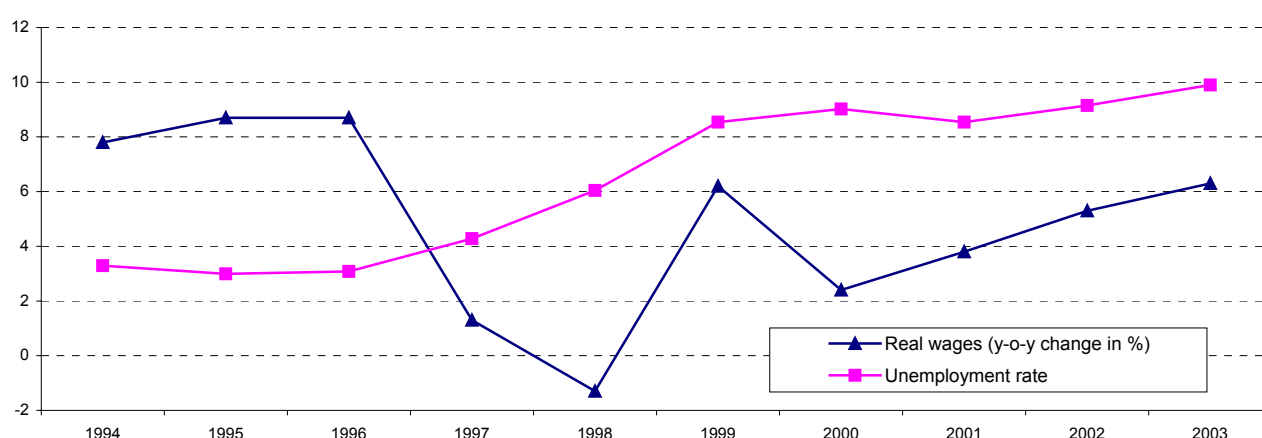
The pronounced long-term structural inter-sector changes, i.e. agriculture, industry and services, have a significant effect on the development of unemployment and employment. With the structure of demand undertaking changes and labour-intensive industries having exhausted their growth potential, labour force is shifting towards services. Throughout the period of 1990 to 2004, the number of workers in agriculture and industry has dropped by 337 thousand (implying a two thirds decrease) and 464 thousand (one quarter decrease), respectively. The reduction in the number of

workers employed in industry has been felt in particular in light and heavy industry, that is, in market segments characterized by both overcapacity and the shift of production in favour of low-income countries with a closer proximity to raw material resources and countries with lower labour costs. Against this backdrop, new jobs, some 756 thousand, have been created in the services sector. The current issue for concern is however the fact that the ability of the tertiary sector to absorb labour force seems to have ceased. According to the CZSO 2004's first quarter survey, new jobs have been generated only in transportation services, warehousing, real estate and health services sectors, and these gains have been rather moderate. In a number of other services branches the number of workers has been in fact falling.

- **Discord between the wages and labour productivity development**

The real wage and unemployment rate time series indicate, that as soon as the growth of wages considerably departed from the time series in 1999 – 2003 and significantly overtook the growth of labour productivity, specifically in 1999, 2002 and 2003, the growth of unemployment rate increased simultaneously.

Graph 2 Real Wages and Unemployment Developments



In the course of 1993-2003 the real wages grew on average by 5.0 % p.a., while the growth of labour productivity reached only 2.3 % p.a. The growth of labour productivity was faster only in 1998 and 2000. Interestingly, the substantial, typically more than double lead of growth of wages to productivity transpired in the expansionary phases of the business cycle, i.e. in 1994-1996 period and in 2000-2003 period, as well as in contracting phases, i.e. in 1997-1999 period.

Table 6 Real Wages and Labour Productivity Developments

	year-on-year % change												
	1994	1995	1996	1994-1996	1997	1998	1999	1997-1999	2000	2001	2002	2003	2000-2003
Average real wage	7.8	8.7	8.7	8.4	1.3	-1.4	6.2	8.0	2.4	3.8	5.3	6.7	4.6
Labour productivity	1.0	4.2	3.2	2.8	0.0	0.9	3.3	1.4	4.0	2.6	1.3	3.6	2.8

Source: CZSO

- **Growing importance of incentives**

It is important for the development of labour market supply and demand relations to provide adequate incentives for employers to create and maintain jobs and for population to work.

The tax burden of work is relatively high here. Especially large differential compared to most western European countries is found in the part paid in the form of transfer by the employer. This part is in high-income countries roughly half to the level of this tax rate set here. Shrinking number of employees in the past years evokes a question, whether it is due to the growth of labour productivity, shift of some assets from the industrial firm to services sector (outsourcing), or a reaction to the excessive taxation of labour.

Intentions of population to enter the working process is being mapped out by a new category of CZSO Labour Force Sample Survey, which is related to persons who are not working, are not actively looking for a job, however wish to work. Their number was 291 thousand in Q1 this year. This relatively large group of people with the biggest share being the youth (91 thousand) forms in essence certain stock of labour. More accurate interpretation of reasons why people are not looking for a job is difficult, however for some parts of population certain hypotheses can be expressed. For instance some middle age women might prefer longer maternity leave.

The expanding number of long term unemployed (1 year and more) represents the biggest labour market problem; this number increased in Q1 2004 by 35 thousand people year-on-year and arrived at total of 228 thousand people. These persons constitute nearly two thirds of total addition to unemployment. These alarming numbers present a challenge to seek more intensively new ways and means to stop this trend. Inspiration can be searched for in particular in those countries boasting the lowest rate of unemployment.