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Croatia: Paradise Lost

Abstract

Absolute poverty in Croatia is low, but this diagnosis is only deceptively consolatory. Poverty in Croatia is characterised by stagnation – those who become poor take a great deal of time to escape from indigence. In Croatia, many people are unemployed and/or have low employability and so are seriously exposed to economic poverty and social exclusion. For such people, unemployment becomes a wearisome constant companion. This is especially true in Croatia, where a large proportion of able-bodied welfare recipients are very long-term unemployed. The effects are damaging and costly. The task is to reduce both the flows into long-term unemployment and the stock of people already out of work for more than one year, primarily by improving their employability. The problems faced by many of the long-term jobless are often multi-dimensional and frequently include low levels of education and of motivation. Croatia has a range of active and passive measures to assist the unemployed. To be more effective, these measures should be adjusted and carefully targeted through social planning and the systematic analysis and evaluation of policy outcomes.

Keywords: *poverty, de-institutionalisation, unemployment, long-term unemployment, labour market flexibility, employment protection, active labour market policies, drop-out rates, youth training*

Introduction

Croatia is a relatively small country in south-eastern Europe, surrounded by Slovenia, Hungary, Serbia, Montenegro, Bosnia and Herzegovina, and (via a sea border) Italy. According to the 2001 Census, Croatia has about 4.4 million inhabitants with its capital in Zagreb, which has 780 000 inhabitants.

Recent Croatian history has been almost completely defined by three political factors: the fall of communism (the first free elections were held in 1990); the declaration of independence from Yugoslavia (1991); and the War of Independence (which started in 1991 and ended in 1995, when Croatia regained much of its occupied territories by military force).

Aggression towards Croatia in the early 1990s and the transition to a market economy have both strongly affected the economic, as well as the social, situation in the country. One-third of Croatian territory remained occupied until 1995, while Gross Domestic Product had shrunk by 1993 to lower than 60 per cent of the 1990 level. Living standards fell significantly due to hyperinflation, the destruction of household assets and growing unemployment; while transitional problems, coupled with war-related problems, meant that the country experienced a slower democratisation process than many other post-communist countries.

Croatia became a member of the Council of Europe in 1996 and established relations with the EU by signing a Stabilisation and Association Agreement in 2001. It was granted candidate status in 2004 and the negotiation process with the EU began in October 2005, after Croatia met all the preconditions. However, due to limited Croatian co-operation with the International Tribunal in Den Haag, negotiations for full EU membership have still not been finished and will probably not be completed until 2011.[1]

In the following note, we analyse the trade-offs between Croatian social policy, the labour market and education.

The case for a trade-off in social policy

It is almost unnecessary to recall that poverty is multidimensional. It is complex, institutionally embedded and also a gender- and location-specific phenomenon. Usually, in households, children and women suffer more than men. Poverty is the result of a complex interaction between policies and institutions in the economic and the political spheres.

Knowledge of the incidence and scope of poverty in Croatia was very limited until the analytical work on poverty and vulnerability carried out by the World Bank (2001), in collaboration with the government, became available. This analysis was based on the first post-war household expenditure survey in Croatia, carried out by the Croatian Bureau of Statistics in 1998. The results showed that poverty in Croatia was relatively low, i.e. lower than in most transition economies in the region (except for Slovenia). Only four per cent of the population lived on less than $ 4.30a day at purchasing power parity (an internationally comparable standard across transition economies), while around ten per cent lived on less than $ 5.30a day, which the study suggested was an appropriate absolute poverty line for Croatia.

Absolute poverty in Croatia may be low, but this diagnosis is only deceptively consolatory. Poverty in Croatia is characterised by a level of stagnation – those who become poor take a great deal of time to escape from indigence (World Bank, 2001).

There are several dominant groups of the poor: the unemployed and inactive people; the poorly educated; and the elderly. The group of unemployed and inactive people represent a relatively small share of the poor population in Croatia (2.9 % and 5.4 %, respectively), but they are the most exposed to poverty since employment provides fairly reliable protection. Almost three-quarters of the poor live in families whose head completed, at most, only primary education. These individuals are likely to have little prospect of finding work if they are not employed, or to have only low earnings if they are. The risk of poverty is particularly high when poor education is combined with unemployment. Those living in households with unemployed or inactive household heads are around three times more likely to be poor than the population as a whole. Thus, poverty in Croatia – having become much like poverty in western Europe – is highly correlated with the situation in the formal labour market and with the skills of individuals (Grootaert and Braithwaite, 1998). Finally, the elderly, especially those without pensions, also make up a significant part of the poor.

1 Editor's Note: accession negotiations were indeed completed on 30 June 2011.

In the last few years, poverty has mostly stagnated or, perhaps, has slightly increased. The at-risk-of-poverty rate in 2008 was identical to that in 2007 (17.4 %), but the relative at-risk-of-poverty gap increased from 21.9 % in 2007 to 24.9 % in 2008. Of all age groups, only the eldest (65+) had an at-risk-of-poverty rate higher than the national average and, in this age group, the difference between the rates of men and women was the biggest. In 2008, in comparison with 2007, the at-risk-of-poverty rates with the highest growth were those of single households and single-parent families (in other types of households, the at-risk-of-poverty rate was mostly reduced or else remained the same). Relative poverty data and indicators for 2009 are not yet available, although World Bank analyses and simulations show that poverty grew during 2009: it is estimated that the absolute poverty rate grew in 2009 by 35 %, or by three to four percentage points in comparison with 2008, when it was approximately 10 %.

There is currently a concern that social care services in Croatia are not necessarily targeted towards those most in need. Despite the high percentage of GDP taken up by social transfers (around 25 %), Croatia has achieved little redistribution. This is because most social spending programmes are relatively poorly targeted, while those programmes which are relatively well-targeted are fragmented and account for a small proportion of total social spending. The benefits of the programmes in which the majority of social expenditure is spent (primarily pensions and health insurance) are relatively badly targeted, while programmes that use a smaller part of social expenditure (such as rights in the welfare system and unemployment benefit) are better directed as regards the poor.

Furthermore, residential care is the predominant form of care provided by the Croatian social welfare system. Insufficient attention has been dedicated to de-institutionalisation and the development of half-day or day-care centres and the provision of services in the user's home. However, in the last few years, particularly in 2009, there has been some modest progress in terms of the de-institutionalisation of people who are already placed in institutions. Nevertheless, this is a longer-term process on which intense efforts are being concentrated. Thus, in 2009 as many as 70 % of social welfare homes surveyed, and 74 % of Centres for Social Welfare, had undertaken activities which were aimed at reducing the number of beneficiaries in permanent institutional accommodation; 61 % of homes (36/60) have organised the provision of non-institutional services; and 53 % have, in the last year, expanded the range of their services, with homes for children with disabilities, young people and adults taking the lead. One-fifth of the homes surveyed (12/60) have special posts for non-institutional services (Ministry of Health and Social Welfare, 2010).

The key obstacles to de-institutionalisation include, from the point of view of service providers (social welfare institutions), a lack of earmarked financing for the transformation; an insufficient degree of development of relevant services in the communities; a shortage of operational guidelines for the transformation of institutions; a lack of integration services in education institutions; and inadequate rules and standards for the modernisation of institutions. These five, most distinct obstacles can be removed relatively quickly through the development of a network of priority social services. That can be achieved by social planning and financial support for the provision of services in communities by the Ministry of Health and Social Welfare and the counties

in combination, as well as by the parallel, systemic promotion of the transformation of institutions on the basis of the action plan which is currently under preparation.

The perspective of the transformation of institutions into resource centres in their communities or regions, exclusively to provide non-institutional services, is a preferred option by the majority of stakeholders – both institutions, particularly homes for people with disabilities and adults with mental illnesses, as well as users. Some institutions have proposed another form of operation, with the focus on a combined provision (a mix) of institutional and non-institutional services, with accommodation services and permanent care targeting long-term or palliative solutions.

Succinctly, we might recall that the characteristics of the poor in Croatia are very similar to those of the deprived population in other transitional countries in central and south-east Europe, and are mostly determined by education, the number of income earners and employment status. There are several dominant groups among the poor, primarily the unemployed and inactive people as well as older people who have no pension rights. Economic growth in Croatia has failed to generate sufficient economic opportunities for the poor, and they are at a disadvantage with respect to benefiting from these opportunities.

From the standpoint of the trade-off between equity and efficiency, the impression is sometimes created that, if only more funds would become available for such measures, poverty could be eradicated in no time. We should regard it as much more appropriate for transition countries like Croatia to invest in the 'quality' of social policy rather than in its quantity. There is clearly a strong association between poverty, education, employability and long-term unemployment. Employment delivers the best protection against poverty and social exclusion. Additionally, paid jobs from home enable social integration and the realisation of full citizenship. People who are earning are able to participate more easily in social, political and even sporting activities. There is not enough work for all, to a certain extent because a part of the population does not have the knowledge and skills sought by employers.

Thus, this article turns its attention next to an analysis of the trade-off between equity and efficiency in employment policy.

The case for a trade-off in employment policy

Croatia, like many other central and east European countries, has been characterised in the past twenty years by U-shaped trends in GDP, strong and persistent declines in employment rates and a stagnation of the pool of unemployment, in spite of the rapid structural change that is taking place. There has been a remarkable increase in unemployment in Croatia (a more than threefold increase – from 123 000 in 1986 to 380 000 in 2001), and then subsequently a decline up to the second half of 2008. This has not been accompanied by adequate research-based or political attempts to understand the causes of the rise in unemployment that took place, or by proposals either for the reduction of unemployment or for improvements in the transition from unemployment to employment.

A relatively new and important area of research is the political economy of unemployment and employment policy (Calmfors and Holmlund, 2000). The key idea in this strand of research is that persistent unemployment may be explained by political mech-

anisms that inhibit labour market reforms. A successful strategy to fight unemployment must, according to this view, also recognise the prevailing political restrictions and offer proposals that may overcome them. Most of the time, the labour market is not perfect: unemployment and open demand co-exist. This implies that, particularly in countries like Croatia with high current levels of unemployment, there is room to improve the functioning of the labour market by bringing unemployment nearer to the minimum of labour demand and supply, thus reducing both unemployment and vacancies. Research on unemployment around the world has identified a number of plausible determinants of unemployment situations and rates. Among others, these factors include: employment protection regulation; unemployment insurance; active labour market policies; product market competition; taxation; systems of wage bargaining; working time; etc.

The inflexibility of the Croatian labour market is reflected in a high value for the composite index of the strictness of employment protection legislation (EPL), developed by the OECD. The EPL index is calculated as a weighted average of 22 indicators that quantify different procedures, costs, limitations and terms related to the cancellation of contracts of employment. Croatia has been assessed by some researchers (Biondić *et al*, 2002) as among the strictest in Europe. When compared to other countries, Croatia has the second highest value of the index (3.6), which is significantly higher than the OECD average (2.0) or that for EU countries (2.4); and is also much higher than that for those transition countries for which data exists (2.2).

All these factors led to the 2003 changes to the Labour Code. Current reform has detached Croatia from the group of countries with the most protective EPL index – yet, it remains among the most protected transitional labour markets (Matković and Biondić, 2003).

In the Croatian labour market, and in the regulation of labour relations, much greater attention is devoted to maintaining existing jobs than to creating new employment opportunities. Legislative solutions and political figures in Croatia have been more inclined to extend the lives of unprofitable firms instead of stimulating the creation of new and sound businesses. This persistent, and exaggerated, maintenance of current employment produces the diametrically opposite result from that desired, while the uncompetitiveness and inflexibility of the labour market have resulted in a reduction in the number of existing jobs and, at the same time, a restriction of the space for new employment. Thus, there has been a polarisation of society into a relatively safe (although, with respect to the cost of living, underpaid) employed core (the insiders); and an unemployed periphery (the outsiders). A very considerable number of the latter is found among the long-term unemployed with very slight chances and likelihood of finding work. This shows a total failure to understand (or even to know) the trends towards greater flexibility that mark both the global and the regional EU economy in which the emphasis is not upon saving jobs but on creating the conditions for employability.

Labour market data indicate that rising unemployment has mostly hit first-time job seekers, particularly those with secondary education. This suggests that unemployment is predominantly the result not of economic restructuring but, rather, of the country's inability to create jobs fast enough to accommodate new entrants to the labour force.

It may also reflect the willingness of educated young people to wait for jobs in the formal and public sectors to become available, and to register themselves as unemployed in the interim, as well as the failure of the education system to provide its students with the kinds of skills needed for private sector jobs.

A particular problem is long-term unemployment – more than one-half of the unemployed has been waiting for a job for longer than one year, while one-third has been waiting for more than two years – because, after an unsuccessful job search, long-term unemployed people tend to lose any prospect of finding a job. Partially, they lose the skills and knowledge gained through their education; other skills and knowledge become obsolete; and job-seekers' self-esteem and hope for the future disappears. Some of the young turn to crime, while older people become discouraged and apparently withdraw from the labour market.

An active labour market policy (ALMP) could redistribute job opportunities so that fewer people become recipients of long-term unemployment benefit and/of welfare assistance. When total employment and total labour supply are a given, this would imply a distribution of the burden of unemployment among a greater number of people (assuming that it is not the same people who are experiencing more unemployment periods as a result of the policy intervention). Clearly, an increase in total employment as a result of ALMP would be preferable to a redistribution of unemployment among a greater number of people. Economic theory states that ALMP scarcely affects total employment directly. However, if ALMP is successful in reintegrating long-term unemployed people or welfare recipients, the effective supply of labour increases. Therefore, reintegrating the long-term unemployed and preventing long-term unemployment are certainly worthwhile goals. There are other meaningful activities, in addition to paid employment, which can be a source of social integration and individual fulfilment. Nevertheless, the prevention of long-term and recurring unemployment would be a major contribution towards combating poverty and social exclusion and/or the prevalence of large numbers of social welfare recipients. This is especially important when the employability of the long-time unemployed is increased such that they become attractive to potential employers.

It would of course be helpful to all unemployed people if there were more jobs. However, there is clear international evidence, as well as examples in Croatia, that labour supply shortages can exist alongside high levels of long-term unemployment. Furthermore, each business cycle creates additional long-term unemployment which is not extinguished during the following business cycle. Until recently, long-term unemployment was ratcheted upwards and more and more unemployed people were dropping out of effective labour supply. That has negative influences on the efficiency of the labour market as well as on the material position of those made thereby vulnerable. It also increases the costs of the welfare system.

One should stress that, in Croatia, there is a range of active labour market measures. They are comparatively small-scale, and suffer from a funding mechanism that treats them as residual once the costs of passive measures are met. This has the perverse effect of diminishing funding for ALMP as unemployment rises. Active labour market measures in Croatia have been monitored, but not evaluated, for their net effect, i.e. what would have happened to the individuals had they not gone on active measures (such as

training). Only for the public works programme has there been this kind of evaluation; this showed that the public works projects examined had almost no effect in improving the subsequent success of participants in gaining jobs on the open labour market (Dorenbos *et al*, 2002). Babić (2003), using comparative analyses of expenditure on ALMP programmes, has shown that the structure of ALMP programmes is inappropriate for the Croatian labour market.

The lack of any real evaluation of outcomes (as opposed to monitoring the level of take-up and outputs) means that it is not possible to draw clear and firm conclusions as regards the value of individual active labour market measures. What is apparent is that the measures are not sufficiently integrated with the administration of unemployment compensation or the activation agenda. Nor are they targeted at those groups which are at risk of long-term joblessness or others which are likely to gain the most real benefit. The funding of active measures is too uncertain, while the mechanism is perverse in its effect: rising unemployment causes an increase in expenditure on unemployment benefits, which diminishes the scope for active measures. Consequently, there are problems related to the short duration and relatively low consistency of the measures put in place. Different programmes have been started, and have facilitated results that have been better than expected, but the implementation of the programmes has ceased (mostly because of insufficient financial possibilities or restrictions). This has a damaging impact on the infrastructure of the providers of active measures, as well as on the ability of the Croatian Employment Service to find ways of helping people out of unemployment.

The task is to reduce both the flows into long-term unemployment as well as the stock of people already out of work for more than one year. The problems faced by many long-term jobless people are often multi-dimensional and frequently include low levels of education and motivation. Croatia, nevertheless, has a number of active and passive measures to assist the unemployed. The employability of the long-term unemployed may be enhanced and social exclusion reduced through participation in work-related activities. However, there is a lack of timely evaluation to assess the true effectiveness of policy measures on the labour market. This could be addressed through the introduction of new techniques (such as tracking studies) for collecting up-to-date data on their impact. It is important to enhance the employability of such people – in particular to increase their human capital, improve their knowledge and skills, and enhance the attractiveness of work for them via the realisation of measures that make work pay.

Regarding a trade-off between equity and efficiency, active labour market measures are diverse and recognised as useful instruments of labour market policy. However, they are not yet sufficiently targeted to where most international evidence indicates they are most effective, i.e. towards disadvantaged people at risk of, or in, long-term unemployment. Their scale is small and their availability is made particularly uncertain by the funding arrangements. They are not yet integrated as closely as they might be with the benefits system (including the administration of unemployment compensation) and placement work.

Crucial also is the creation of an adequate entrepreneurial and investment climate. This means improved governance, incentives for economic openness to foreign direct

investment and foreign trade exchange, and the creation of an adequate organisational infrastructure that facilitates investment. Better availability of public services and employment will enable the social inclusion of the poor citizen, which is so important for full participation in society.

An important precondition for this is improved human capital, so we direct our attention next towards the 'trade-off' as regards education.

The case for a trade-off in education

Education is the most important determinant of employability – in Croatia, more highly-educated persons find jobs more easily and faster – but it also doubtlessly carries ancillary non-market effects (for example, easier access to information; greater care for personal health; and more active participation in social life which encourages responsible democratic civic behaviour, the election of democratic authorities and actualisation of the rule of law). Non-participation in education is especially precarious for the children of poor citizens. According to the World Bank (2001), the children of the poor in Croatia are very likely to drop out of the schooling system early, while differences in access to higher education are now very stark. The lack of access to levels of education that are highly valued on the market tends to lower employability and increase the danger of staying in poverty. These factors perpetuate the existing inequalities in the earning prospects of the poor and non-poor, and create the potential for the inter-generational persistence of poverty.

A considerable number of young people in Croatia are dropping out of secondary and higher education institutions. This is, among other reasons, caused by the serious lack of a network of 'second chance' schools aimed at young people who have either been excluded from education or who are on the verge of exclusion. High drop-out rates drive up the costs per graduate. The school drop-out rate should be reduced, and an apprenticeship system either created or the existing system improved.

Systematic prevention of the exclusion of young people from education could be realised by optimal flexibility and the passability of the education system at all levels.

Flexibility implies the sensitivity of the education system to changes in the needs of the environment and in the needs of pupils and adult learners. Flexibility in education can be accomplished by the re-certification of the existing competences of an individual as well as by the recognition of the results of non-formal education and self-education, i.e. by introducing a system of non-formally and formally-acquired qualifications (introducing passports for acquired knowledge and skills).

Passability implies avoiding 'dead ends'. Dead ends in education are those education streams (or types of programmes) which do not allow for transfer to a higher degree of education or to a different programme at the same educational level. Dead ends decrease the availability (or the democracy) of education and the utilisation of human resources. Passability, on the other hand, may be achieved by establishing a sufficient number of vertical and horizontal links between the different directions in the system which decreases selectivity and avoids the 'averaging' of pupils' achievements. The passability of the system depends, in particular, on the pathways that make transfers possible between general and vocational education at the higher secondary level, or

between higher secondary vocational education and tertiary education, in order to enable the continuation of education to a higher degree. The same requirement for passability also occurs between non-university and university forms of tertiary education as a means of facilitating transfers from one type of higher education to another.

With the goal in mind of lessening the number of drop-outs from the education system and preventing low employability and poverty, it is necessary to establish counsellors regarding the employment situation of young drop-outs and to provide measures for counsellors' continuing training. Counsellors should be able to assist in preparing young drop-outs for (re-)entering the labour market. To solve their employment problems, an additional network for collaboration should also be established comprising various state institutions as well as private and non-profit organisations involved in employment issues.

Regarding youth education and employment, measures that increase the returns from and participation in secondary and, particularly, in tertiary education could enhance employability, reduce unemployment and prevent (or reduce) long-term unemployment, poverty and social exclusion. In all EU member states and developed European countries, participation in education has increased in the last 25 years, but there remain huge differences between countries and particular regions of countries, as well as between particular socio-economic and ethnic groups.

The situation and causes of unemployment in Croatia differ from those in the EU; similarly, unemployment rates are lower for people with higher education and skills levels. The result of this is that it could be assumed that, as in France and Finland, Croatia would also profit from motivating young people towards further education; while, like in Spain and Italy, there would also be benefits from increasing the possibilities and programmes of vocational education and the participation of young people in them. The education aspect is crucial in increasing their employability which, in turn, is the most important determinant in evading poverty.

Due to many factors, it is difficult and complex to evaluate the trade-off between equity and efficiency in education. In the absence of domestic research and data, and according to the situation in many countries (Wolf, 2002), we can be relatively certain that education programmes do, in fact, increase existing social differences. This is because poor citizens profit relatively little from participating in education whereas children from richer social strata complete better and higher quality schools that provide entry to advantageous possibilities within further education, employment and professional promotion.

In most transition countries, existing education systems are expensive and ineffective with regard to their results. Students are forced to learn more data, but are weaker in their use of available knowledge and skills in non-standard circumstances. Thus, at all levels of education, it is necessary to emphasise the active participation of students and to improve efficiency and opportunities for modernisation, as well as to enhance teaching methods.

Conclusions

There is a strong and permanent link between social policy, the labour market and education. Undoubtedly, many long-term unemployed and poor people have complet-

ed, at best, only a low level of education and/or have knowledge and skills that are not sought on the labour market. It would be reasonable to assume that many do not have basic literacy and numeracy skills; while some have had no formal education whatsoever. There are many indicators and reports that stress the insufficient incentives for lower-paid workers to find jobs and to leave behind the system of protection during unemployment or welfare.

Employers complain of the difficulty of finding an adequate workforce even in regions with high unemployment rates. Long-term unemployed people are in a further adverse position as a result of the depreciation of their knowledge and skills during the period of their unemployment, as well as of negative attitudes from employers. Therefore, it is necessary, in a co-ordinated way, to improve the basic knowledge and skills of long-term unemployed people, develop new programmes so that these people will acquire work experience, and expand re-orientation programmes (courses).

Apart from a better convergence of labour supply and demand, the focus should be on making labour relationships cheaper and more flexible in order to increase the likelihood that more labour will be taken on. It is not necessary to deregulate, in a hit-or-miss manner, the system of employment and work relationships but rather to attempt to find the optimum ratio between the desired level of labour market flexibility and the required amount of social protection. Flexibility needs to be considered in such a way as not to lower the standards of labour law, but as an expansion of the far-reaching consequences of the regulatory approach to labour and social law. The point of making employment relations cheaper and more flexible is in getting labour and social legislation (establishing medical and retirement insurance) to work in the same direction and in harmony, and in the procedures for the handling of labour conflicts.

For the sake of reducing tax pressure, as well as the broadening of the tax base and the cheapening of labour – which are the conditions for greater employment – it is necessary to bring as many of the economic activities of the working population as possible within the limits of labour legislation, and to carry out the legalisation of those activities in the grey or underground economy which should be brought within the purview of the law.

In terms of employment and social policy, we could say that Croatia is, on the whole, moving in the direction of those policies that are currently in vogue in Europe. These policies are marked by a narrowing of rights through the implementation of more stringent conditions and a stronger emphasis on active measures in employment policy, with unemployment benefits being linked increasingly to participation in training and requalification programmes. What remains is the rather fraught task of encouraging a more flexible labour legislation and the removal of organisational and administrative barriers to the foundation of new small and medium-sized enterprises. This should be of the most help in the mitigation of unemployment in Croatia. Within the context of the level of Croatian association with, and ultimate membership of, the EU, constant attention is required in the consideration of the labour market and the labour legislation.

Activities related to professional orientation, lifelong learning and qualifications, professional development and the increase in the total stock of knowledge in society ought to be enhanced, since this would increase the adaptability of the labour force to the requirements of the labour market. Active labour market policy measures must be

more strongly directed at people between the ages of 15 and 24, among whom rates of unemployment are the highest (while, for this group, the return on investment in human resources is probably also the highest), with the emphasis on training and further qualifications. Training programmes should be matched, as far as possible, to the demand for given occupations and capacities that will be sought in the future; that is, emphasis should be placed on qualifying for a *known* employer.

The labour market, social and education policy must be monitored continually and measures should ensure that men and women obtain equal opportunities and responsibilities. It is important constantly to evaluate the effects and influences of the different measures and of social and education policies on the labour market. This implies a need to determine improvements in the possibilities of employing people who have come out of educational programmes. It is also necessary to consider the costs of obtaining these results, or otherwise the cost-effectiveness of particular given programmes.

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