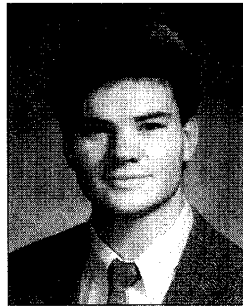


LABOR AND THE TRANSITION TO A FREE MARKET ECONOMY

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Introduction

Nobody wants to be unemployed. Unemployment involves physical hardship, since it makes paying bills and feeding children difficult. Unemployment also involves mental hardship, since it evokes feelings of inferiority and frustration. The unemployed begin to feel that they are not good enough to get a job, and they become frustrated after prolonged periods of unemployment.

In socialist economies, a job is guaranteed for every citizen. Socialist theorists and politicians claim that guaranteed employment is a major advantage of a socialist economy. In Czechoslovakia, however, the job guarantee was not an advantage. Rather, it led to misallocation of labor and hidden unemployment.

The hidden unemployment in Czechoslovakia is now being exposed as the country attempts the transition from a socialist economy to a market economy. What caused the misallocation of labor in Czechoslovakia before the transition? What problems is the transition causing in the labor market? How can the government solve these problems so that the tran-

sition can progress smoothly? These questions must be answered by the Czechoslovak government if the transition is to be successful.

Characteristics of Czechoslovak Labor Before Transition

Before the transition, labor in Czechoslovakia was characterized by an apparent contradiction: labor shortages occurring simultaneously with hidden unemployment. These two phenomena were caused by an inefficient allocation of labor and the maintenance of unprofitable enterprises by the state government.

Inefficient Allocation of Labor

The inefficient allocation of labor is a result of the development and goals of the Stalinist-type economic system. The system encouraged rapid industrialization with an emphasis on producer goods at the expense of consumer goods. Industry was concentrated in state hands, and production was centrally controlled. The important criterion for industries was the quantity of output. The central plan set

targets for the quantity of output, and enterprises were expected to fulfill the targets. Output growth was based on increasing the quantity of inputs rather than on increasing productivity.

The emphasis on output rather than efficiency caused distortions in the use of manpower by factories. Because factory managers received bonuses for plan fulfillment and over-fulfillment, they often behaved in irrational ways. They hired any workers that helped increase output, regardless of profitability. Often managers hired extra workers in order to ensure plan fulfillment in the event of an emergency (e.g. sickness or an increase in the output target). Because enterprises were not concerned with profitability, managers had no reason to economize on labor. Rather, they "hoarded" labor, hiring as many workers as the state allowed. Thus, labor was constantly in short supply in Czechoslovakia before the transition. But much of this labor was used inefficiently, resulting in underemployment or "hidden" unemployment.

Maintenance of Unprofitable Enterprises

Socialist governments believe in the rights of the working class. One of those rights is the right of every citizen to a job. The commitment of the old Czechoslovak government to job security was another cause of hidden unemployment.

In order to fulfill the commitment to job security, the state subsidized unprofitable enterprises. If the state did not subsidize unprofitable enterprises, many would have shut down, leaving workers unemployed and causing social disruption. Much of the funding used for the subsidies was taken from efficient enterprises, mostly in the form of taxes. Thus, the Czechoslovak system of subsidization transferred funds from efficient enterprises to inefficient enterprises. It allowed large unprofitable enterprises which employed many workers to remain in operation.

The guarantee of job security and the provision of subsidies to ailing enterprises removed many of the incentives for efficiency. There was no way to discipline firms and workers that did

not perform well. Inefficient firms were given funds, and workers were guaranteed a job regardless of the quality of their effort. (Vodopivec, p. 134) The removal of incentives for efficiency resulted in a large amount of hidden unemployment. Some workers were employed in unprofitable enterprises which would not be operating in a non-subsidized system. Other workers were underemployed with no real incentive to realize their skill potential (i.e. no threat of job loss). Officially, the socialist state declared that there was no unemployment. But the costs of maintaining (official) full employment were hidden unemployment and underemployment.

Problems Created by the Transition

Unemployment

Within the labor market, the biggest problem created by the transition has been unemployment. Unprofitable firms have shut down completely, releasing thousands of workers. Thousands more will be released as firms economize by shedding surplus workers. Newly developed, more productive technology will soon displace many other workers.

The greatest source of unemployment will be the closing of inefficient, unprofitable enterprises. Those enterprises that totally depend on state subsidies will be forced to close when subsidies are cut. Many other unprofitable firms which survive cuts in subsidies will not be able to survive and compete in a free market system. They will be forced out of business by profitable firms. Because of the number of people employed in unprofitable enterprises, their closing presents a major unemployment problem for the government.

Those enterprises that manage to survive will set targets for profitability, not output quantity. Decisions in these enterprises will be based on cutting costs and increasing productivity. One obvious cost is surplus labor. Releasing surplus labor will be beneficial to managers, since it will enable them to cut costs and increase the productivity of the remaining workers. The increase in productivity will compensate for the loss in manpower, and enterprises will be able to maintain or even increase

output with fewer workers. (Gamarnikow, p. 129)

Surplus workers and workers in unprofitable firms are not the only ones whose jobs will be endangered by the drive for efficiency. Remaining workers will be threatened by the advance of new technology. Many of the production techniques in Czechoslovakia are outdated. They are too labor-intensive and expensive. These old techniques will be supplanted by methods based on new technology which can perform the same tasks in a more reliable, less expensive manner. Many unskilled manual workers will be released in favor of new technology. For example, many assembly-line tasks will be automated, leaving thousands of assembly-line workers unemployed. This "technological unemployment" will contribute to unemployment during and after the transition to a free market system.

In the current stages of the transition, unemployment problems are more acute in the Slovakian region of the country. Many areas of Slovakia were over-industrialized during the period of communist rule. Over-industrialization resulted in the presence of large steel works and armaments plants in this region. These industries were over-subsidized in order to maintain both production and employment. Many of these industries have now shut down because of both inefficiency and dwindling demand. Because the people of Slovakia were heavily dependent on steel and armaments, plant closings have resulted in high unemployment rates. Industry in the Czech Republic, on the other hand, was more diversified. Consequently, the Czech Republic has not experienced as much unemployment. In the fall of 1991, the rate of unemployment was 9.5 percent in Slovakia but only 6.2 percent in the Czech Republic. (Chesnoff and Green, p. 62)

Skills Mismatch

The problem of unemployment will be compounded by the skills mismatch between released workers and industry. Many workers in Czechoslovakia are unskilled and capable of performing only manual tasks. After the transition, however, industry will demand more than just manual skills, and the skill level of the

released workers will not be adequate to satisfy the demand. Finding jobs for these released workers will be difficult once the new economic system is implemented.

An overall lack of mobility in the labor force will exacerbate the skills mismatch problem. The lack of mobility is caused both by a distorted housing market and a poor infrastructure within Czechoslovakia. The housing market suffers from a shortage of apartments and houses. Rent ceilings imposed by the government have created great demand for housing. This demand cannot be met, however, because the production costs of houses and apartments are extremely high. Labor mobility is also limited by the infrastructure of Czechoslovakia. Roads, highways, and bridges are of poor quality. Transportation systems within the country are outdated and unable to accommodate large numbers of people. Telecommunication systems are also antiquated, thus hindering effective communication among different regions of the country. The lack of mobility in the labor force restricts unemployed workers to seeking jobs in their own regions. If the labor force were more mobile, unemployed workers could seek jobs in areas where their skills were in demand. Thus, the lack of labor mobility constrains possible solutions to the skills mismatch problem.

Solving the Problems

Any solution to the problems of the labor market will involve finding employment for released workers. Czechoslovakia must generate employment opportunities by developing new industries (especially in the private sector). In order to capitalize on the employment opportunities, released workers must be retrained in the skills necessary for the new industries. Placement services must also be improved to help workers find jobs which match their skills.

In addition to finding employment for released workers, the solution to the labor market problems must protect the rights of the working class. Laws must be enacted to guarantee that workers will be treated fairly under the new economic system. The unemployment problems will not disappear overnight.

Consequently, the government must provide unemployed workers with temporary security in the form of unemployment benefits or compensation.

Unemployment Compensation

First-hand experience with unemployment has changed the general attitude toward unemployment compensation. Before the transition, unemployment compensation was seen as unnecessary because the guarantee of a job for every citizen took away the risk of unemployment. The new economic system does not guarantee employment for every citizen. Because of the risk of unemployment, methods for compensating the unemployed have become necessary.

There are two basic types of unemployment compensation: insurance and assistance. The two types differ in many ways. Qualification for unemployment insurance is based on employment history, and the amount of benefits paid is a proportion of past earnings. Payment of the benefit is limited in duration, but cannot be reduced if the family has other sources of income. Qualification for unemployment assistance, on the other hand, is not based on employment history, and the amount of benefits paid is not related to past earnings. Payment of this benefit is unlimited in duration, but can be reduced if the family has other sources of income. (Micklewright, p. 421)

Unemployment insurance has advantages when compared to unemployment assistance. Because it is contributory, insurance implies a redistribution of income from those with jobs to those without jobs. This signifies solidarity in the work force. Unemployment insurance also provides incentives to enter the work force. Because it is based on employment history and contributions, insurance can be considered a "right" (guarantee) for people who have worked. The guarantee of unemployment insurance will encourage people to take jobs and may replace the guarantee of a job. Another reason why insurance is preferred to assistance is that insurance does not punish a family with other sources of income. Insurance retains the incentive to work for other members of the family and thus encourages multiple-earner

households. (Micklewright, pp. 421-22)

Currently, the unemployment compensation plan for Czechoslovakia is still being developed. The goal of the new plan is to transfer responsibility for released workers from the enterprises to society. The temporary unemployment compensation plan calls for the enterprises to pay released employees two months salary. This plan resembles unemployment insurance because payment is both temporary and based on past earnings.

Developing Alternative Sources of Employment

Unemployment compensation is not the solution to the labor problems of the transition. Rather, it is a means of taking care of the needs of the unemployed. The solution to the labor problems lies mainly in the creation of jobs for released workers by expanding the private sector of the economy. Public works projects and new technology can also provide job opportunities for people with the appropriate skills.

The private sector has traditionally had little impact on the economy in Czechoslovakia. Propaganda has made entrepreneurship seem "socially inappropriate," and restrictive tax, credit, and investment laws have made entrepreneurship difficult. As a result, the private sector contributed only 0.7 percent to net material product in Czechoslovakia in 1983 compared to 95 percent produced by the socialist sector. (Mejstrik) As late as 1989, 90 percent of the labor force was employed in the socialist sector. (Prust, p. 52)

In order to create job opportunities, the government has undertaken various measures to encourage private sector development. The measures are intended to reduce the legal restrictions on establishing a private business. One such measure is the law on private enterprises which was passed in April, 1990. The law removes the legal limitations on the number of employees hired and the extent of property acquired by a private firm (Mejstrik). The private sector has expanded rapidly in response to the actions by the government. For example, the number of registered private entrepreneurs has risen from 87,000 in 1989 to 655,000 in the first quarter of 1991. (Federal Statistical Office,

1991) Despite the rapid growth of the private sector, however, problems which hinder private sector development still exist. For example, restrictive wage and tax laws increase the costs of maintaining a private business, and poorly functioning capital markets make it difficult to obtain credit.

In addition to the private sector, public works projects will provide employment. Public projects such as road building will also contribute to the transition by improving the infrastructure. However, newly elected local governments are inexperienced in initiating these programs. The programs also suffer from a lack of funds. Consequently, public works projects have not provided much employment help yet.

The introduction of new technology will displace some workers from their jobs (as discussed earlier), but it will also create job opportunities. Many new industries will form as a result of advanced technology, and these industries need workers. If the people can obtain the skills required by new industries, advanced technology will be beneficial in providing jobs.

Skills Development

The people of Czechoslovakia must develop new skills if they are to find employment in the expanding private sector. Skills development during the transition consists of two main components: retraining unemployed workers and reforming the education system.

Retraining programs face several obstacles. One obstacle is the inability of people to learn new skills. Ten percent of the work force in Czechoslovakia is above the normal retirement age. (Prust, p. 10) They are still employed but have few advanced skills. As the expression goes, "You can't teach an old dog new tricks."

Another obstacle to training programs is funding. Training and retraining programs require large amounts of money in order to operate, and the funds will be difficult to generate. One possible source of funds is enterprise contributions. Perhaps the major obstacle to training programs, though, is the difficulty of accurately determining which kinds of skills are needed by various occupations. This requires extensive research and communication between training centers and industries. A final obsta-

cle is the need to restructure the training programs themselves. Many of the training programs are outdated, and innovative methods must be developed which will provide people with current skills. (Samorodov, pp. 364-65)

Skills development entails not only retraining released workers, but also reforming the entire educational system. The educational system must be able to produce graduates with skills that are in demand. Educational facilities must be modernized, and curricula must be restructured. Czechoslovakia is currently looking both to the United States and Western Europe for assistance in restructuring its educational system. One way in which the United States has responded is by founding the U.S. Business School in Prague. Established jointly by Czech Technical University and Rochester Institute of Technology, the school is taught by a rotating group of U.S. professors. It is intended to teach managerial skills, and its graduates will have the equivalent of American MBAs. (Siler, May 13, 1991)

Placement Services

Along with skills development, the improvement of placement services is necessary to satisfy the potential labor demand in the expanding private sector. Placement services must be able to find jobs for those who have acquired new skills.

The nature of job placement services has changed because of the transition. Before the transition, placement services served merely as filters, rationing labor to industries. (Samorodov, p. 367) Because labor was in such high demand, placement services were essentially passive institutions. They did not need to actively seek employment opportunities. Now that labor is not in high demand, however, placement services must be active in finding job opportunities for people and in finding such opportunities quickly. The new active nature of placement services therefore makes it urgent that they improve in scope and efficiency.

In order to perform their expanded roles, placement services must communicate more closely with enterprises, local authorities, and workers. Placement services must communicate with enterprises and local authorities in

order to determine which skills each occupation requires. Placement services must then communicate with workers in order to identify workers who possess the required skills. The successful placement of workers in enterprises requires mutual agreement — the enterprise and the worker must both agree that a placement is suitable. (Samorodov, p. 368)

Improving Labor Mobility

Improved labor mobility will help job placement services perform their task by facilitating the movement of people to areas where their skills are in demand. Labor mobility can be improved by reforming the housing market.

Housing market reform is primarily aimed at reducing the shortage of apartments and houses. State-owned apartments will soon be privatized, and rent ceilings will be removed. These measures will reduce the demand for housing while improving the quality. The government also hopes to encourage competition in order to reduce the high costs of building houses. (Vodopivec, p. 146) Reduced construction costs and easier access to land would increase the supply of available housing. As the housing shortage is eliminated, more high quality homes and apartments will be available to workers who desire to move.

Labor Laws

A legal framework must be implemented in order to protect the rights of workers. Laws regarding minimum wages, protection from mass layoffs, and unemployment benefits will ensure that workers do not bear the entire burden of the economic transition. Trade unions will play an increased role in the formation and enforcement of these laws.

The role of trade unions will undergo a major change during and after the transition. Before the transition, trade unions functioned merely as “transmission belts,” implementing party directives in the economic sector. The trade unions were subordinate to the government and the central plan. Their main goal was to motivate workers to produce more goods. (Gamarnikow, p. 143) It was the state which

was responsible for safeguarding the interests of the workers, not the trade unions.

Because of the transition, however, the role of the trade unions is changing. Since control has shifted from the state to individual enterprises, workers now fear that their rights and interests will be violated. They are therefore looking increasingly to the trade unions to protect these interests. New functions of unions include the guarantee of favorable working conditions and the fight against violations of labor laws. Trade unions have also taken on more power because of their new functions and goals. Rather than merely obeying orders as before, they now negotiate and cooperate with policy makers. Currently, the trade unions are inexperienced and unorganized in their attempts to fulfill this new role. If they are to function well, they must develop better structure and organization. As they gain experience, however, they will gain power and will ultimately become the major protector of labor under the new economic system.

Conclusion

Much of the cost of the economic reforms in Czechoslovakia is being placed upon workers and their families. The physical and mental hardships of unemployment are large burdens for any family to bear. In Czechoslovakia, unemployment will be especially difficult since the people have never lived with the risk of losing a job. As unemployment worsens, the people may become restless. Many may desire to return to the old economic system, despite its inefficiency.

If the transition is to be successful, the government must therefore find a way to relieve the burdens of unemployment. It must develop alternative sources of employment, restructure training and placement programs, and improve labor mobility. The government must also protect workers by enacting labor legislation and providing unemployment benefits. The task will be difficult for the leaders of Czechoslovakia. But if they do not find ways to fight unemployment, they may soon be unemployed too.

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