



## Determinants of the labour market institutions in post-socialist economies



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### ABSTRACT

The aim of this study was to identify common determinants of the shape of labour market institutions in the group of 25 post-socialist countries during the transition period. The exclusion of countries' fixed effects (with the use of *least squares dummy variable* – LSDV model) showed that conducted market reforms (especially the privatisation of state-owned companies and enterprise restructuring) have determined the shape of labour market institutions in post-socialist countries. However, the levels of political liberty, protection of property rights, international trade freedom and government expenditures did not occur to have influenced the labour market institutions in these economies.

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### 1. Introduction

For the last three decades the economic literature has seen a lively and continuously growing discussion concerning the role of institutions in economic performance. Such a lively debate was also present in the labour economics literature where heterogeneity in labour market institutions among countries has been widely described and analysed, especially as a possible determinant of heterogeneity in labour market performance (Boeri and Van Ours, 2008; Layard et al., 2005, p. XIII–XXXIX; Blanchard, 2006; Eichhorst et al., 2008) and as a determinant of the labour market flexibility (Kwiatkowski et al., 2001; Cazes, 2002; OECD, 2004, p. 61–125). However, despite growing amount of studies in that field, the available evidences in the literature still remain inconclusive and often contradictory (Lehmann and Muravyev, 2012, p. 237). As it is stressed by Blanchard (2006, p. 43–46), there are rather no doubts that labour market institutions matter, but the question which ones and how is still current. Moreover, the question 'why labour market institutions are as they are, and to what extent the current configuration of labour market institutions might be desirable despite sometimes their unfavourable impact on labour market performance' (Arpaia and Mourre, 2005, p. 17–18) is also still open.

The analyses of labour market institutions presented in the literature focus predominantly on the OECD countries. In that context it worth taking notice of the post-socialist economies where labour market institutions were thoroughly rebuilt at the beginning of the transition period and significantly revised in later years. Also labour market outcomes were changing considerably and heterogeneously in these countries. Moreover, the economic transition was a period of deep reforms conducted in order to improve the macroeconomic performance and to transform economic and political institutions. Nowadays, after more than twenty years of transition, post-socialist countries can be seen as much more diversified in terms of the economic performance and the institutional framework than they were at the beginning of the transition process. In consequence, due to that significant diversification in time patterns of the conducted reforms, the transition countries can be perceived as a potentially fruitful 'laboratory' that allows to identify relationships among changes in different institutions, not only in the economic and political, but also in the labour market institutions.

Therefore, the goal of this study is to identify determinants of the changes in labour market institutions in the group of 25 post-socialist economies<sup>1</sup> during the transition period. The following hypothesis is stated: although one of the main characteristics of the changes in labour market institutions in post-socialist countries is the cross-country heterogeneity, the common determinants of the changes in these institutions include the conducted market reforms and the achieved degree of political freedom. Thus, it is conjectured that the conducted labour market reforms were a consequence of both economic and political aspect of the transformation process.

Although the analysis of the determinants of changes in the labour market institutions is present in the literature, it is conducted almost only for highly-developed countries where legislative processes are democratic and have not been so significantly changed in the last twenty years. Thus, the analysis of post-socialist countries is not only original, but can also shed some new light on the question concerning the determinants of labour market institutions. Moreover, thanks to the recent work of [Lehmann and Muravyev \(2012\)](#), who published the seminal dataset of labour market institutional indicators for transition countries, we will be able to identify these determinants empirically, which is the main novelty of the presented research.

The paper is organised as follows. Section 2 provides a synthetic description of the changes in the labour market institutions in post-socialist economies based on the critical review of the literature and analysis of the collected data. It presents also results of the cluster analysis that shows that one of the main characteristics of the changes in the labour market institutions in post-socialist economies is the cross-country heterogeneity. Section 3 reviews the literature concerning determinants of the labour market institutions in highly-developed countries and identifies theories that may be applied also for post-socialist countries. Section 4 presents a fixed effects model, estimated in order to identify common determinants of the changes in the labour market institutions in post-socialist countries. Section 5 gives a brief summary of the conducted analyses and suggests areas of further research.

## 2. Changes in the labour market institutions during the transition

### 2.1. Remarks from the literature

In the transition countries the processes of restructuring, privatisation and, what is characteristic for all post-socialist countries, the transformational recession ([Havrylyshyn, 2001](#)) caused significant changes on the labour markets during the transition period. It can be seen especially in the significant decreases in employment and economic activity levels, and also in the occurrence (almost all centrally planned economies were formally fully-employed) and rapid growth of unemployment and informal employment ([Cazes and Nesporova, 2003](#), p. 7–19). What is more, the transition economies were characterised by the strong excess supply of low-skilled workers (demanded in generally heavy-industry oriented socialist economies) and by a high demand for better skilled workers, with qualifications more suitable for service and consumer oriented market economy ([Winięcki, 2008](#)). Therefore, in order to adapt to these changes, governments in post-socialist countries had to reform the labour market institutional framework substantially.

However, due to the shortage of data, especially for the majority of CIS (*Commonwealth of Independent States*) countries, the labour market institutions analyses focused mainly on the transition countries that became EU members ([Cazes and Nesporova, 2003](#); [Boeri and Garibaldi, 2005](#); [Anspal and Vörk, 2007](#); [Fialova and Schneider, 2009](#); [Tonin, 2009](#)), on the selected groups of countries ([Eamets and Masso, 2005](#); [Gligorov et al., 2008](#)) or on particular countries ([Kajzer, 2007](#); [Micevska, 2008](#)). In that context it is worth mentioning the recent work of [Muravyev \(2010\)](#) where the values of Employment Protection Legislation (EPL) index<sup>2</sup> for former USSR countries for the years 1990–2009 are calculated. These results were further used in the work of [Lehmann and Muravyev \(2012\)](#) where labour market institutions were analysed as the determinants of labour market performance with the use of the new, hand-collected database of the labour market institutions indicators created for 27 post-socialist countries. Although their database allowed to include into the analysis also the CIS countries, the data in that study were collected only for four years: 1995, 1999, 2003 and 2007.

Based on the mentioned literature, three general conclusions concerning the labour market institutions in the post-socialist countries can be stated. Firstly, labour market institutions matter as a framework for economic activity on the labour market and as an important determinant of the flexibility of that market. Secondly, in the majority of the transition countries labour market institutions do not provide less flexibility than the institutions in the EU-15, and in many cases even more. And thirdly, despite some significant similarities among labour market institutions in many countries (for instance the general tendency to decrease the union density rate), the general characteristic of the labour market institutions in the transition economies is their heterogeneity, both in time and especially in space.

<sup>1</sup> The data were collected for the following countries: Albania, Armenia, Azerbaijan, Belarus, Bulgaria, Croatia, Czech Republic, Estonia, Georgia, Hungary, Kazakhstan, Kyrgyzstan, Latvia, Lithuania, Macedonia, Moldova, Poland, Romania, Russia, Slovakia, Slovenia, Tajikistan, Turkmenistan, Ukraine and Uzbekistan.

<sup>2</sup> The EPL index has been proposed by [OECD \(2014\)](#) in order to measure the strictness of employment protection legislation. It takes values from 0 to 6, the higher the value the more protective the labour law is.

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