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AZERBAIJAN

Enterprise Restructuring and Labor Redeployment

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FISCAL YEAR

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ABBREVIATIONS AND ACRONYMS

ALMPs	Active Labor Market Programs
CIS	Commonwealth of Independent States
CPI	Consumer Price Index
EBRD	European Bank for Reconstruction and Development
FDI	Foreign Direct Investments
FSU	Former Soviet Union
GDP	Gross Domestic Product
IDPs	Internally Displaced People
ILO	International Labor Organization
IMF	International Monetary Fund
LFPR	Labor Force Participation Rate
LRP	Labor Redeployment Program
NES	National Employment Service
PES	Public Employment Services
SME	Small and Medium Enterprises
SOEs	State-Owned Enterprises
SSP	Social Support Program
UNDP	United Nations Development Program
VET	Vocational Education and Training

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Lyaki
Sumqayıt
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Kürdämir
ARMENIA
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(Stepanakert)
Karabakh
Naxçivan
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ACKNOWLEDGEMENTS

The Azerbaijan report was written by Arvo Kuddo (Task Team Leader), with Jan Rutkowski, Pablo Saavedra and Hjalte Sederlof (ECSHD).

Surveys of employees, displaced workers, and focus group survey of key stakeholders in the city of Mingachevir, Azerbaijan were conducted by a team of researchers from the Institute of Labor and Social Problems of Azerbaijan headed by Masuma Mamedova, and included Nigar Giliyeva, Matlab Mahmudov, and Savindzh Bayramova. The job and vacancy survey as well as the survey of local employers were conducted by the Caspian Business Consultants, whose team was headed by Hafiz Qayibov, and included Rufat Garagezli.

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AZERBAIJAN

Enterprise Restructuring and Labor Redeployment

Executive Summary

As Azerbaijan undertakes restructuring and privatization of its public enterprise sector, it faces the challenge of redeploying large numbers of workers who become redundant in the process: facilitating their reentry into the workforce or moving them into retirement. This will require labor-intensive economic growth, a competitive business environment that boosts labor productivity, and a flexible labor market and labor market institutions that promote labor mobility toward more productive and better paying jobs. It also will require sufficient public resources to provide a safety-net that offers adequate protection against temporary and permanent reduction in income of laid-off workers and their families.

The process of reducing extensive labor hoarding in big state owned enterprises (SOEs) has started. Many enterprises, especially in industry and construction, have gone through downsizing and restructuring, and, while productivity in the economy still is low (in part reflecting the effects of overstaffing and a large informal market), such reforms are reflected in improved productivity and higher wages. In part, also, wage growth reflects the appearance of skills shortages in some factor markets, raising the concern that rapidly rising wages may well risk diluting the competitive edge that Azerbaijan currently may have in terms of relatively moderate unit labor costs.

The particular challenges that Azerbaijan faces involve continued restructuring and improving productivity of the enterprise sector, with a special focus on facilitating a diversification of the industrial base. This entails improving the investment climate by removing the constraints to firm formation and growth and developing a competitive environment that promotes innovation and productivity. This in turn will involve shaping the legal and regulatory environment in a way that promotes business development and labor market mobility (the movement of labor from low productivity jobs towards high productivity jobs); the promotion of small and medium size enterprises, as these tend to be a major catalyst for job creation; and removing skills bottlenecks.

The main objective of this report is, first, to examine changes in the welfare and labor market status of workers in Azerbaijan, with concentration on large state-owned enterprises (SOEs) already displaced or which may be displaced because of enterprise restructuring and privatization; and, second, to study the dynamics of labor demand and patterns of job creation and job destruction, as well as any barriers to firm entry and growth. The ultimate objective of the analysis is to advise policymakers regarding effective labor redeployment policies and measures to foster job creation.

The report is based on the findings of a detailed survey of key stakeholders--employers, employees and displaced workers--in the city of Mingachevir--population approximately 95,000, which is one of the principal and typical industrial centers of Azerbaijan, and the fourth city in the country, by number of population. While generalizations from a single-city survey should be treated with caution, the findings do offer insights that can reasonably be assumed to have general relevance for the Azerbaijan labor market.

Labor redeployment programs

There are economic, social and political objectives for providing social support packages to workers displaced by restructured and privatized state-owned enterprises. (See Fretwell 2004 for the details).

From an **economic standpoint**, the objective is to reduce excess labor costs and overstaffing so enterprises can be competitive, and to facilitate the rapid return of workers to productive employment and thus reduce the duration of state supported income support payments.

From a **social standpoint**, the objective is to provide transitional income support while displaced workers are finding alternate employment and, for those who have difficulty finding employment, providing extended income support to prevent these workers and their families from slipping into poverty.

From a **political standpoint**, labor redeployment programs (LRPs) are intended to build public support for restructuring by signaling to citizens, communities, and labor representatives that those responsible for restructuring are turned to the needs of affected workers and that they are ready and willing to assist those that need and want help.

While providing income support to displaced workers, LRP is helping redundant workers to cope with their new status and to reintegrate into the labor market by providing information, counseling and assisting workers to undertake self-employment, and reduce the short-term negative impact of labor restructuring on affected workers and communities.

The design and use of LRPs varies considerably between countries and is greatly influenced by the economic environment, including the level of unemployment, and type of general social support programs in-place in the country where economic restructuring is occurring.

The primary strategic decision in labor redeployment is whether it should be carried out by the Government, or if in the case of privatization, it should be left to the private sector. There is no single approach, and countries have followed different paths. Among them are three options: (a) let the new investor deal with them; (b) have the government assist prior to sale; or (c) combine both approaches. All have their advantages and disadvantages, both in terms of the financial gains to the Government and in terms of the process of labor shedding and its social mitigation. Each approach needs to be carefully evaluated before a decision is taken.

Investor driven layoffs assume that the new investor will restructure the enterprise and address related labor requirements. This is the preferred option as the new investor is in the best position to know and plan the labor requirements of the enterprise he is buying.

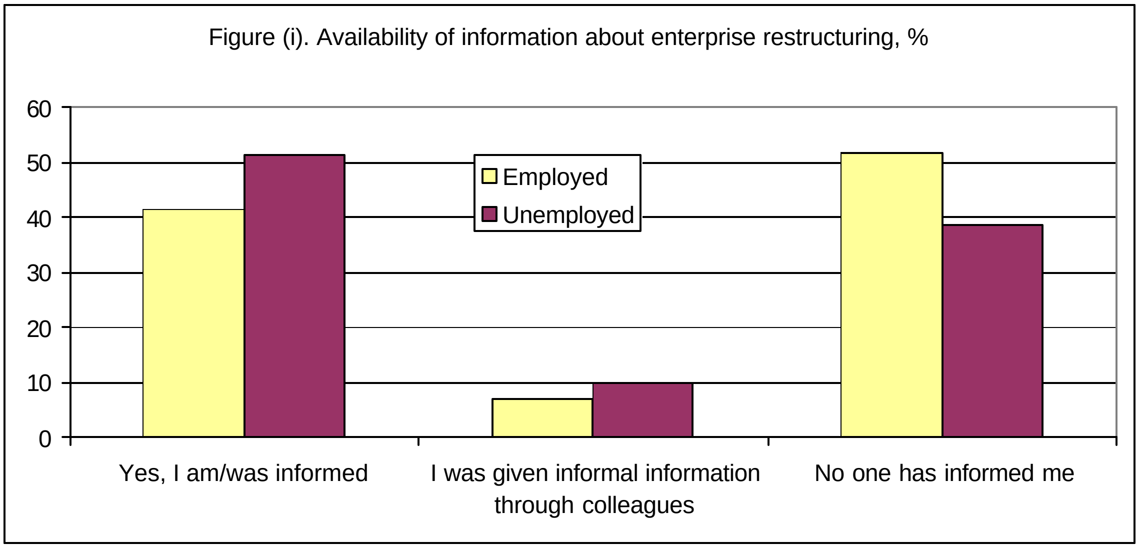
Some SOEs are very unattractive to buyers, because of large excess numbers of workers. Therefore, the government may become involved in designing, financing, and administering the divestiture process prior to and during privatization and restructuring. The costs of the programs provided prior to sale would be recaptured by gaining a higher cost from the sale.

Main findings of the report

Employment surveys can provide a good understanding of the labor market that workers will enter. These surveys provide an analytical framework that can be used to discuss policy alternatives to enhance labor market dynamism and promote business growth. The following are some of the main findings of the study.

Industrial cities, such as Mingachevir, are much more vulnerable to economic downturns and transitional shocks than other regions. A vast majority of the unemployed in the city have become redundant because of external economic shocks and lack of demand for the products produced, and inevitably leading to production stoppage, bankruptcy or liquidation, or enterprise restructuring or privatization. Only 3 percent of the unemployed left their job voluntary. The survey of workers indicates that labor hoarding in SOEs is still significant, and labor retrenchments may continue.

A large percentage of workers were not informed about their legal rights, pursuant to the Labor Law, Law on Bankruptcy and the Law on Privatization, when they were declared redundant. (Figure (i)). Among the workers already declared redundant, 51 percent responded that they were officially informed about the transformation of their company, and another 10 percent were given information by colleagues. However, 30 percent of redundant workers were not informed, even about the grounds on which they would receive severance pay. These data indicate workers generally are not provided with information concerning their legal rights if and when declared redundant by either management or their trade unions.



Source: World Bank/Institute of Labor and Social Protection (2004). Social monitoring of the displaced workers in Mingachevir city.

Worker participation in the company can be enhanced by setting up consultation mechanisms aimed at soliciting workers' opinion on issues affecting the enterprise. However, both employees and employers rated unions poorly in terms of their performance in representing the interests of workers in the restructuring process. Workers generally did not participate in the process of enterprise restructuring.

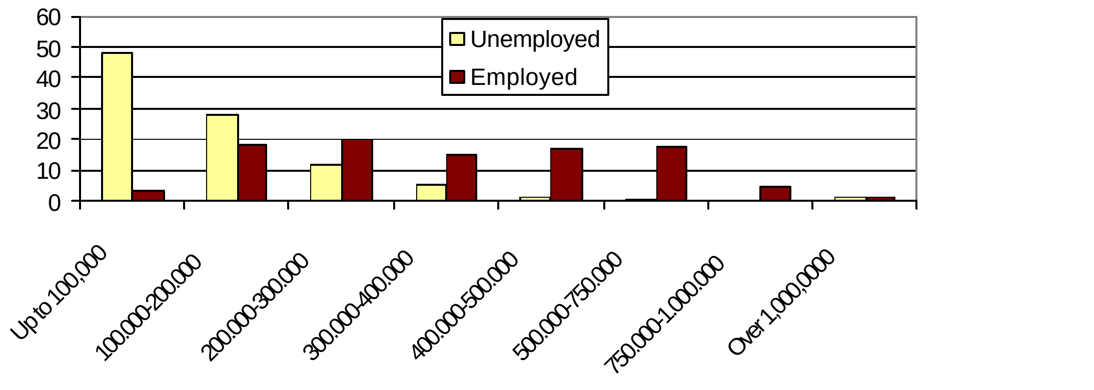
Survey results indicate that to hold to their jobs, workers themselves have "agreed' to significant real wage cuts to maintain high employment rates. Wage levels in large SOEs in Mingachevir appear to be much below the average for the country. Wage arrears are common and some groups of workers are not being paid at all. Living standards of the unemployed population are much worse. Around 48 percent of the families of the unemployed had total incomes (salary, pension, social benefits, and income from agriculture) below AZM 100,000, and another 28 percent between AZM 100,000 and 200,000 (See Figure (ii)).

The main reasons for this were the following:

1. In 78 percent of the families of the unemployed no one is employed on a permanent basis; moreover, only one family member is employed in 20 percent of the households of the unemployed.

2. In the majority of cases of unemployed workers, social benefits were the only source of family income, reflecting (i) their importance for the well-being of many families; (ii) their inadequate levels; and (iii) the long-term nature of the unemployment, as 87 percent of the unemployed had been out of work for more than 24 months, by far exhausting their right to unemployment benefits.
3. Employed workers were often limited to wage and work-time adjustments that limited their labor income.

Figure (ii). Average monthly income of the family in AZM in Mingachevir (manat), %

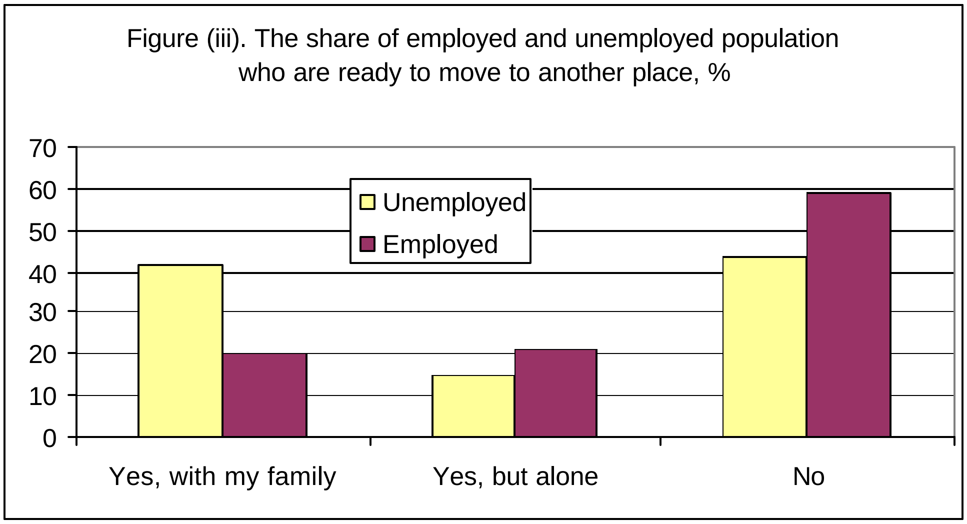


Source: World Bank/Institute of Labor and Social Protection (2004). Social monitoring of the displaced workers in Mingachevir city.

Interviewed workers resorted to a number of coping strategies, including in particular home production from private plots, private transfers from family and friends, and migration, both external and internal. External migration, although initially high cost and therefore more accessible to better-off families, appears to have been a significant outlet for surplus labor, while internal migration in search of work is hampered by a rigid housing market and by a reluctance to leave familiar surroundings, even in search of more remunerative work. This may at least in part explain the low job mobility of the interviewed workers, and it should be of particular concern when seeking to increase domestic labor mobility.

The surveys confirm that a significant share of both the employed and unemployed population is ready to move out of Mingachevir. Around 42 percent of the unemployed and 20 percent of the employed are ready to move out of the city with their entire family (Figure (iii)). This is further evidence that job prospects in the city are slim. Whether these intentions are ever acted on depends on many factors. Generally, the economic constraints alluded to above prevent people from moving out immediately.

Low labor mobility may in part also explain the extended job search period (as well as the long term nature of unemployment). While workers tend to start looking for a new job immediately after dismissal, the job search period averages two years, job search is concentrated in Mingachevir and often limited to the enterprise in which the job seeker was employed. At the same time, a significant minority of interviewees did look for work beyond Mingachevir, but were constrained by migration, including housing costs.



Source: World Bank/Institute of Labor and Social Protection (2004). Social monitoring of the displaced workers in Mingachevir city.

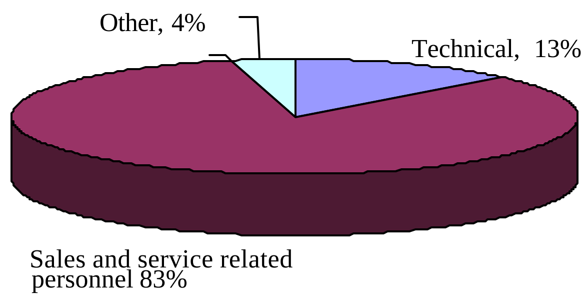
Surveys also confirmed that violations of workers' rights are common, e.g., delays in wage payments and severance pay. Especially vulnerable are workers declared redundant many years ago and who did not have written labor contracts. They may never recover the wages or severance owed to them by their former employer, i.e., state-owned enterprises which may have no funds or be bankrupt or liquidated.

A significant portion of the able-bodied population, including some of the workers still on the active list of enterprises, no longer receive any earnings, and thus become much more dependent on social transfers from the state or private transfers from relatives. Simultaneously, as reliance on social transfers from the state grows, dependency ratios worsen. Unfortunately, surveys confirmed that state social assistance is limited, and most unemployed individuals receive no social or humanitarian assistance and do not even know where to apply for it. This signals that state-provided social safety nets are weak.

One important constraint to job creation is a mismatch between the skills of available workers and the skill requirements of firms. The analysis revealed that in Mingachevir, vacancies are mostly in sales and service positions and that firms have difficulty filling these job openings due to a shortage of workers with relevant skills. (Figure iv). More critically, the manufacturing and service industries, which are creating new employment opportunities, are the sectors with most difficulty finding suitably skilled personnel. In fact, lack of skilled personnel ranks as one of the top of reasons for not hiring new personnel. This visible mismatch between the skill profile of labor supply and labor demand may be an important input for policy makers in reforming the education system and shaping active labor market programs. The finding points to the importance of equipping workers with broad and transferable skills as a means of supporting job creation.

Also only a minority of unemployed job seekers recognized that the biggest obstacle to finding a job might be lack of qualifications or skills. Almost half of the interviewees expected to find a job similar to the one they had been laid off from. Self-employment is only marginally seen as an alternative to paid work, in part reflecting perceived regulatory difficulties, as well as limited access to seed money.

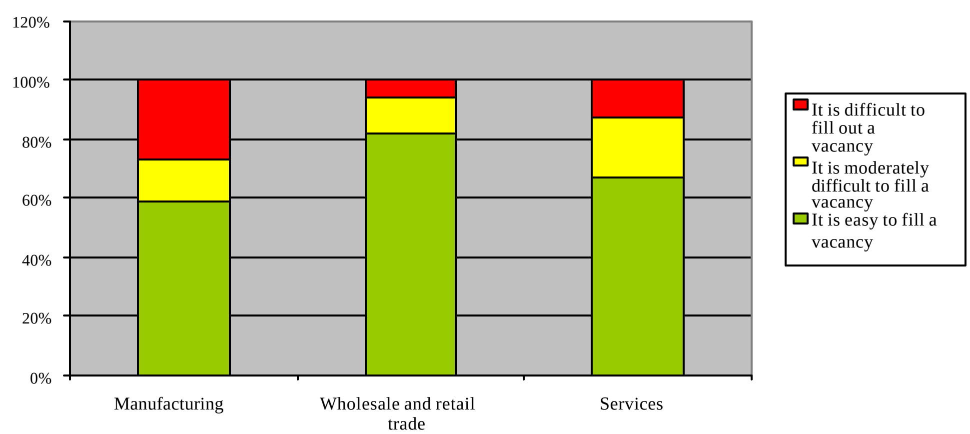
Figure (i v): Type of vacancies available



Source: World Bank/Caspian Business Consultants (2004). Employment and job vacancy survey in Mingachevir.

A policy geared to promote small and medium enterprises is key for job creation. It was found that most of the new jobs were created by small and medium enterprises; in fact, 9 out of 10 jobs were created by firms with less than 30 employees. (Figure (v)). Additionally, small business creation could be a way out from unemployment for job seekers.

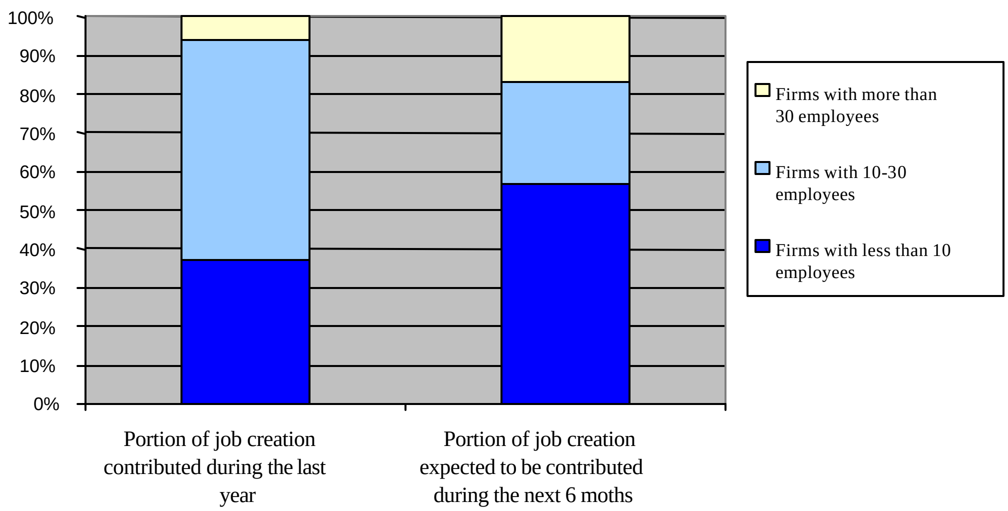
Figure (v): Degree of difficulty finding new personnel to fill out vacancies



Source: World Bank/Caspian Business Consultants (2004). Employment and job vacancy survey in Mingachevir.

Younger firms are not creating employment, which points to a constraint in the business environment. The survey revealed that firms established after year 2000 were not contributing to job creation as much as older firms. In fact, employment growth was negative in younger firms last year. This struggle to grow should also send a signal to policy-makers working in the business environment of the country. The constraint cited as the most important impediment for growth was the lack of access to financial resources on favorable terms. This obstacle may be affecting younger firms more severely as they have yet to establish a "name" in the market.

Figure (vi): Percentage of contribution to job creation by firm size (firm size in terms of number of employees)



Source: World Bank/Caspian Business Consultants (2004). Employment and job vacancy survey in Mingachevir.

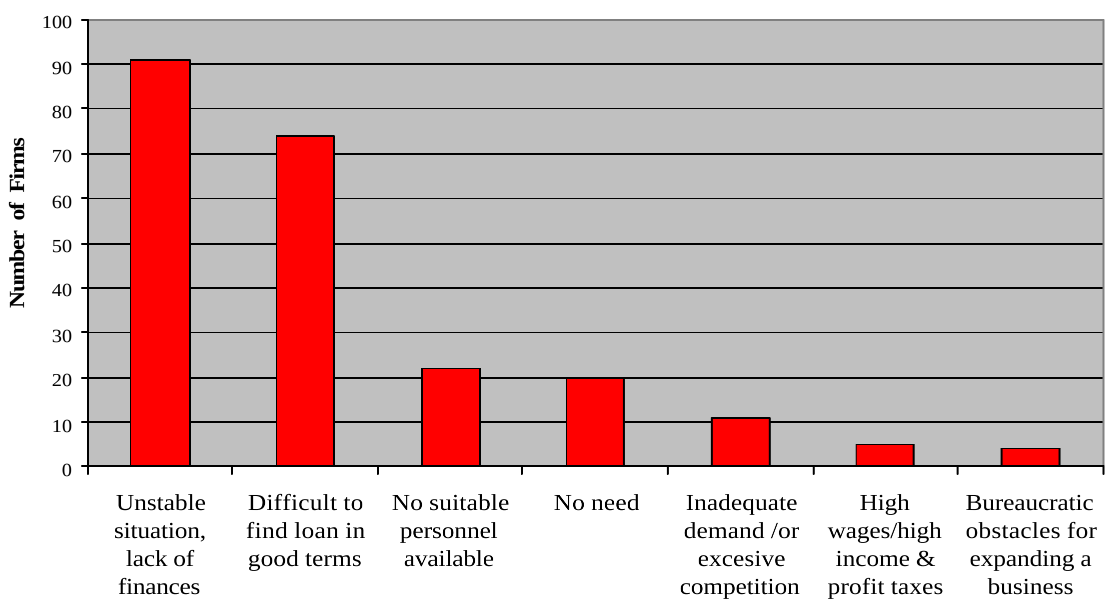
Potential constraints to expansion. While the survey results showed a positive trend in labor demand, many firms were cautious about the future: some 57 percent of firms did not change the level of employment over the previous year, and some 61 percent either were not considering hiring staff during the subsequent six-month period, or simply "did not know" if they would do so. A number of factors seem to be particularly influential in determining business decisions on expansion. They relate to difficulty in finding appropriate staff, and institutional factors in the business environment:

1. **Skills bottlenecks.** Skills bottlenecks are beginning to constrain recruitment and business expansion, especially in larger companies and in the manufacturing sector. Thus, some 20 percent of surveyed firms reported difficulties in finding appropriately skilled staff, and shortages of skilled labor was ranked as the third most important constraint on expansion.

2. **The business environment**. While the survey does indicate an increasingly dynamic business environment with more enterprise establishment, job creation and labor mobility, it still has features that aggravate business establishment and growth. These pertain in particular to the regulatory framework, governance, and access to finance:

   a. **The legal and regulatory framework makes business establishment difficult**. Over 40 percent of the surveyed firms claim that it is difficult to establish a new business in Azerbaijan and 60 percent claim that it is moderately difficult. This is confirmed by international surveys that indicate that it takes an average of 123 days to register a business in Azerbaijan, compared to an average of 35 days in the EU (including new accession countries).[1] Some of the major features that current business owners indicate as deterrents to business creation are burdensome licensing procedures (although these are improving), obtaining land and construction permits, and formalization of real state transactions. As business start-ups internationally account for a large portion (from 25 to 50 percent) of new job creation, excessive obstacles to entry risk translating into lower employment growth.

Figure (vii): Main constrains for not hiring new personnel



Source: World Bank/Caspian Business Consultants (2004). Employment and job vacancy survey in Mingachevir.

   b. **Weak governance creates an uncertain environment for business investment and expansion.** Survey participants raised concerns about public governance and regulatory and supervisory practice that have adverse effects on doing business:

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[1] Source: World Bank, Doing Business 2005

rules and regulations are unnecessarily complex and sometimes contradictory, and subject to frequent changes; the court system is perceived as being biased in favor of the State; and regulations are selectively and arbitrarily enforced by state officials.

c. **Access to external financing on reasonable terms is viewed as the major constraint on business growth and increased employment**. While the situation is improving, survey participants still raised stringent conditions on the financial markets as the major constraint to expansion: maturities on commercial loans are short; interest rates are rising; and other financial instruments, i.e. micro-credit and small-business financing institutions, leasing, etc., are not available. As a consequence, some 70 percent of surveyed firms do not finance their operations and investments in the financial markets, but rather from their own resources and through informal networks.

Policy responses

Labor redeployment is rarely the objective when undertaking enterprise restructuring. It should be defined in the context of the economic and social goals that are being sought. Economic goals are usually described as more efficient operations, possibly linked to privatization. On the social side, labor redeployment takes up considerations of how to mitigate adverse social costs.

Notwithstanding the approach taken, the process of divestiture of labor, and related social assets, has three major elements, as follows:

- **Enterprise Analysis**. To identify existing enterprise personnel to be affected by privatization and restructuring decisions and social infrastructure to be divested;

- **Pre-Layoff Assistance**. To develop and implement labor adjustment plans for workers prior to dismissal in order to help "assist and push" displaced workers back into the productive employment.; and

- **Post-Layoff Assistance**. To provide temporary income support and labor redeployment services to individual displaced workers and support regional development efforts.

In addition, **evaluation and monitoring of labor redeployment activities** is needed as an integral part of any social mitigation activity related to privatization and restructuring. This is critical to ensure that displaced workers get their entitled benefits in a timely manner, that they are not re-hired via a "back door", and that those who have difficulty in re-entering the labor market are identified early, and given targeted assistance to ensure they do not slip into poverty.

A strategy for enterprise restructuring and labor redeployment has to take into account the current deficiencies in the market place: (i) high unemployment; (ii) low job creation;

and (iii) inadequate social mitigation schemes. Their existence has three consequences: (i) labor shedding will be costlier; (ii) a high proportion of laid-off workers may find themselves dependent on informal work or welfare; and (iii) labor redeployment may have high financial and economic costs. A useful strategy may have to be gradual and should focus on the following:

- Elimination of obstacles to private sector development;
- The development of the public employment services, with a special focus on (i) the information base for demand and supply of skilled and semi-skilled jobs; accompanied by (ii) carefully targeted training programs, delivered either by public modular training services, or sub-contracted to private training institutions;
- The development of a capacity for advisory services to administer large-scale lay-off schemes, including partnerships with local authorities and stakeholders

Labor redeployment typically combines a set of social mitigation measures: (i) *income support*, and (ii) *labor redeployment services*. Income support usually includes one or more of the following: severance payments, unemployment benefits, social assistance, early retirement, and retirement. Labor redeployment involves retraining and redeployment support (job search assistance, counseling). The design of the social mitigation package will take into account fiscal and financial considerations, the situation in the labor market, the demography of the workforce, prevailing wages and wage levels, the dynamics between labor, state, and enterprise management, and the importance of the enterprise in the surrounding community and the country.

While a social mitigation package may be developed exclusively by the Government, the nature of the restructuring--which is likely to involve significant redundancy and temporary income support plus retooling of the workforce--and the importance of the enterprise in the economy, including consultation with labor and union representatives, as well as local authorities and other stakeholders, who should be identified early in the process. Partnerships are often created to draw on the collective local knowledge of opportunities – existing or potential – in the surrounding economy that could be developed and absorb some of the laid-off workers.

While labor redeployment services – usually retraining, counseling, and job search assistance – are a central feature of most labor redeployment programs, their success often has been modest, especially in circumstances where labor demand is low. Azerbaijan needs to be particularly cautious in this sense, where labor redeployment services are weak or non-existent, and the information base on the demand for skilled and semi-skilled labor is absent.

Early analysis of the costs of labor redeployment services is critical in assessing the feasible options for labor redeployment and social mitigation packages and the scope of the resource envelope for which funding is required. Labor redeployment programs involve spending considerable resources in the short run to reap gains in the longer term. Consequently, enterprise restructuring and labor redeployment decisions should consider the financial and economic returns involved, much the same as in an investment decision. Here, cost-benefit analyses provide insights into the financial sustainability of the overall program.

Given the situation in Azerbaijan, where little social infrastructure that could adequately serve labor restructuring currently exists, the financial and economic costs are likely to be quite high: high financial costs because more reliance must be placed on compensation payments to workers; and high economic costs, because adjustment in the workforce as a whole may take longer. This does not mean, however, that the costs will outweigh the benefits; it does however point to the close attention that must be given to the financial and economic analysis of costs and benefits.

The parties to labor restructuring. The main stakeholders, i.e., groups and institutions that may be affected by or influence the design, implementation, and outcomes of labor restructuring and privatization, involve the central government and authorities in the locality where the restructuring is to take place, as well as workers' representatives (trade unions and enterprise-level employees representatives). Other directly affected parties may also be involved, as necessary. The process should be initiated as early as possible according to a well-defined strategy that might take the following form:

(1) Set up a working group consisting of Government entities that should have direct involvement in the restructuring. This working group should, in collaboration with enterprise management have the following responsibilities:

   a. Agree on a consistent policy for SOE restructuring, including in particular to what extent "exceptional" safety net initiatives beyond the current provisions of social safety net programs, should be recognized;

   b. Clarify the respective responsibilities of the Government and management in developing and implementing a labor restructuring strategy;

   c. Assess the capacity of the Government to carry out labor restructuring strategies – the carrying capacity of income support and labor redeployment schemes in their current configurations, and taking into account any modifications to them that may come about as a result of negotiations with workers and trade unions;

   d. Develop a consistent communications strategy for labor restructuring, based on stakeholder analysis (i.e. employee surveys, surveys of focus groups); a communications strategy should include the following elements:

      (i) The need for labor restructuring;
      (ii) Assurances that the Government is working towards developing a labor mitigation strategy that takes workers' interests into account, attempts to compensate them for their

losses, and be fair and transparent in the treatment of the workers;

(iii) Assurances on consultation with all parties concerned on restructuring approaches, including income support and redeployment schemes.

e. The communications strategy should support and continuously be shaped by consultations with stakeholders (management, unions, workers, municipalities) on the labor restructuring strategy and financial/social packages to be extended to redundant workers; in order to facilitate shaping packages and reaching consensus on approaches to be adopted, and further shape the communications strategy, the consultation process should include enterprise employee surveys;

f. Review (private and) fiscal costs of the strategies and social packages being developed and ensure that the necessary resources will be available.

A synthesis of a labor redeployment strategy, based on the experience of transition countries, is provided in the following policy matrix. (Table (i)).

Table (i). Summary of main labor redeployment interventions and impact evaluations of active labor market programs

Intervention/Action	Comments and/or expected overall impact
1. Enterprise analysis	
1.1. Identify SOEs and stakeholders involved	Usually the measure also includes determining options for divesting of non-core functions and to spin-off these units into separate entities, and determining stakeholders, including enterprise management (investor-driven adjustment; government assisted adjustment), labor representatives, community leaders, government (national, regional, local), non-governmental organizations (NGOs); private sector.
1.2. Conduct an analysis of local labor markets	An activity to determine the capacity of local labor markets to absorb workers made redundant, and ability of public employment services (PES) and other agencies to mitigate the impact of group redundancies.
1.3. Conduct enterprise analysis to identify labor and social assets to be divested, and staffing profile	An activity to determine the likely impact, both type and magnitude, of the labor restructuring being undertaken, including potential level of layoffs.
1.4. Determine staff reduction procedures and contractual obligations towards employees	An activity to identify external and internal labor regulations that affect divestiture, and determine statutory wage costs and other contractual obligations towards employees.
1.5. Determine financing plan for pre-layoff	An activity to determine funds available,

services package	including enterprise own funds (including investor financing), revenues from privatization, PES funds, budgetary support, borrowed funds, outside donor support, trade unions funds, etc., and to develop an estimate of take-up and cost for each type of program.
1.6. Identify administrative structure for a LRP	The organizational structure for the personnel retrenchment program may include the staff of personnel department, local employment centers, consultants, representatives of administration, trade unions, and employees.
2. Pre-layoff services (on-site employment services)	
2.1. Consultation process involving employees, trade union, administration, representatives of local government and employment services	It provides the parties involved, as early as possible, an opportunity for consultation on measures to be taken to avert or to minimize the impact of terminations on the workers concerned.
2.2. Public and internal information on retrenchment and labor redeployment program	This is an essential foundation for effective labor redeployment and employment services. Early communication and consultation with labor is important to ensure fairness and transparency of the process.
2.3. Assistance to management in structuring the dismissal of employees and in preparing a retrenchment plan; training for management on redundancy criteria	This activity provides management with personnel tools to do their job effectively, including policies on a formalized system of performance evaluation, and provides support to operational unit heads by developing a formal communication strategy on restructuring.
2.4. Counseling programs for individual employees on the options and the sources of assistance available; the legal rights of employees; provision of information on training and retraining opportunities available; career guidance, job search, screening and referral to other redeployment assistance; individual coaching and advising; workshops to teach job search skills; health assessment, counseling and referral of persons with diminished work capacity, etc.	This activity examines how to increase employability of redundant workers and introduce them to the type of measures they can use to find a new job.
2.5. Voluntary redundancy arrangements (prior to final dismissal) including voluntary departure schemes, early retirement schemes and compensation payments on redundancy	These arrangements and benefits can reduce workers' resistance to restructuring and facilitate transition.
2.6. Provision of on-site training, retraining, and adjustment courses	Very little evidence for transition countries. Often no positive impact on employment and earnings but there are exceptions. Better results

	may be achieved with integrated training and employment services
2.7. Assistance in self-employment and in other job creation programs; workshops on starting small businesses, cooperative ventures of becoming self-employed; reallocation of funds allocated for severance to be placed in a revolving fund for self-employment creation measures; support in business plan preparation, assistance with business registration procedures and other support through business advisory services that may include legal, financial, and business advisory services	Take-up is usually very low (see below para 3.9).
3. Post-layoff services	
3.1. Temporary income support programs (unemployment benefits, unemployment assistance, social assistance, early retirement schemes for registered unemployed at pre-retirement age).	These programs have income and consumption-smoothing impact and provide resources to conduct a job search. If the benefits are too generous and of long duration, it may have adverse work incentive effects and negative effects on probability of exit from unemployment.
3.2. Employment services (provision of information on the local labor market; job counseling and job search assistance; provision of information on training and retraining opportunities available; career guidance, screening and referral to other assistance; vocational guidance, including providing information, vocational consulting services and psychological support to the unemployed, etc.).	Generally positive impacts on employment and earnings. This assistance is relatively inexpensive and by providing job seekers with better information on jobs, it can also help in shortening unemployment spells. On the negative side, these interventions usually have "deadweight losses" – i.e., individuals who find jobs through these services are generally more qualified than most job-seekers and many likely would have found jobs even in the absence of these services. Programs have most positive impacts when economy is good.
3.3. Provision of training and retraining; adjustment courses	Positive impacts on employment but no overall effect on earnings. Program effectiveness benefits from on-the-job training and employer involvement. Women often seem to benefit more than men. Programs have most success when economy is good.
3.4. Relocation grants (mobility assistance)	Effective when jobs are available elsewhere but take-up is usually low.
3.5. Employer contact services to promote and improve local employment services by gaining better knowledge of, and improve relationships with local employers	These services are inexpensive and help meet employer needs and promote continual use of employment services.
3.6. Job and vacancy fairs	These fairs are cost-effective and are designed to assist local employment agencies in matching supply and demand on labor market by presenting unemployed and other job

	seekers with specific professions, skills, abilities, etc., and employers with needs to employ new workers.
3.7. Specially designed and targeted programs and placement services for the youth, women, disabled, and long-term unemployed	Youth employment problems are more effectively addressed through earlier, education-related interventions. Training most effective when combined with other employment, basic education, and social services. Successful programs require intensive services, and thus are costly
3.8. Temporary community employment schemes (public works)	Overall negative impacts on employment and earnings. Public works can be arranged when the intention is well-defined, for example, to improve local infrastructure Can be effective as a short-term safety net for the poor but generally not as program to improve future labor market prospects
3.9. Assistance in self-employment and in other job creation programs; micro credit programs and start-up loans or grants	Although take-up is usually very low, some of the programs are relatively inexpensive and can be proposed to carefully selected job seekers, including small business advisory services or even small-scale micro credit programs. Some evidence of positive impacts for older, better-educated individuals. Results likely better when technical and advisory services accompany financial aid.
3.10. Job clubs	One of the cost-effective ways for job search assistance, and are recommended especially for those with low self-confidence, who have been unemployed for extended periods of time, or who are displaced.
3.11. Small business incubators	Incubation services are rather costly but can contribute significantly to job creation and redevelopment in economically depressed areas.
3.12. Employment creation schemes, including wage/employment subsidies	Overall negative impacts on employment and earnings. These programs typically are targeted to the long-term unemployed, areas/sectors with high unemployment, and special groups of workers (e.g., youth).
3.13. Local economic development planning studies	These studies help strengthen capacities, especially of poor communities and municipalities, to develop the local economy and generate new employment by identifying and marketing regional resources and opportunities to potential investors and finding local solutions, including sources of funding.
4. Social monitoring and evaluation	
4.1. Evaluation and monitoring of pre-layoff and post-layoff activities	Monitoring of LRPs is critical to ensure that displaced workers get their entitled benefits in

	a timely manner, that they are not rehired via a "back door," and that workers who have difficulty in reentering the labor market are identified early and given targeted assistance to ensure they do not slip into poverty.

Sources: Betcherman et al. (2004); Dar and Tzannatos (1999); Kuddo (2004).

Introduction

One of the preconditions for successful labor redeployment programs associated with enterprise restructuring and privatization is a good understanding of the labor market that workers will enter. This requires a labor market survey, which should be done in tandem with the initial phase of enterprise rationalization. Proper labor market information is critical for setting up training and employment support programs that are targeted to workers' opportunities and needs. Such surveys facilitate development of an overall strategy that includes restructuring options for dealing with labor issues as an integral part of the overall privatization strategy.

The main objective of this report is, first, to examine changes in the welfare and labor market status of workers in Azerbaijan, with concentration on large state-owned enterprises (SOEs) already displaced or which may be displaced because of enterprise restructuring and privatization. This includes identifying: a) dominant patterns in labor market behavior, b) changes in worker socioeconomic status in the wake of redundancy; and c) assistance received under enterprise social programs and other government social safety nets. Second, the study also explores patterns of job creation and job destruction, and the dynamics of labor demand, including any barriers to firm entry and growth.

The goal of the study is to design, implement, and analyze a series of surveys, including a tracer (follow-up) survey of displaced workers; a survey of workers in SOEs undergoing restructuring and associated downsizing; a survey of local employers to identify the potential for labor demand; and focus groups surveys of local employers and main stakeholders. The objective is to: (i) analyze the link between enterprise restructuring and poverty and social impacts, (ii) help to design mitigating measures and risk management systems, and (iii) build country ownership and analytical capacity to assess the impact of labor conversion and staff reductions associated with enterprise privatization and restructuring.

A pilot study was conducted in the city of Mingachevir, population approximately 95,000, which is one of the principal and typical industrial centers of Azerbaijan, and the fourth city in the country, by number of population. The following main industrial enterprises are represented in this city: a hydroelectric power station, textile factory, a technical rubber factory; a glass factory, and Azerkabel, among others.[2]

Mingachevir city belongs to the Aran economic region of Azerbaijan, which has a total population of 1.667 million, or 20.5 percent of the republican population, and covers 21.4 thousand sq. km. The power industry is one of the region's most developed and specialized sectors. The electricity generated by the power stations in Mingachevir city is about 60 percent of all electricity generated in the republic. The main underground natural resources of the Aran economic region are oil, natural gas, mineral water with iodine and bromide, and different construction materials. The region also has an

[2] Mingachevir was suggested as a pilot city undergoing major restructuring of SOEs, by the Ministry of Labor and Social Protection of Population and the National Employment Service.

extensive stock of land suitable for agriculture. Over 90 percent of the cotton produced in Azerbaijan is from this region. There are over 2,000 small-, medium-small, and medium-sized enterprises in the Aran region, or 10 percent of the total in the country (State Program 2004).

From the *supply side*, the study seeks to describe the characteristics of workers being declared or who already are redundant; their coping strategies; the impact of the changes on their lives; their potential for redeployment, and the number of surplus workers in general. These issues are discussed in detail in the first chapter of the study. From the *demand side*, the analysis focuses on the capacity of local labor markets to absorb workers made redundant; their strategies regarding future expansion/reduction; and their capacities for mitigating the impact of the redundancy. The dynamics of labor market demand is the main topic of the second chapter.

Some of the survey data gathered in Mingachevir are compared with data from the 2003 household-based survey on economic activity of the population (hereinafter the "labor force survey"), as well as other available surveys.

The outlook for unemployment and employment in Azerbaijan currently is for an increase in unemployment caused by enterprise reform. A great number of public enterprises in the machinery, oil, chemical, and food sectors are to be privatized, which may lead to significant layoffs and related social tensions. The Government also is embarking on a utilities restructuring and related privatization program in the energy sector as part of its effort to eliminate the root causes of fiscal deficits and the operational inefficiencies in the energy and utility sectors. Some of the enterprises will be restructured, others downsized, and still others closed.

Particularly at a time of growth in unemployment, coupled with job-shedding by firms, privatization typically becomes associated with reduction and reorganization of the labor force, either as preparation for privatization or in its aftermath. Labor adjustments are intended to lead to improvements in labor productivity, particularly in such sectors and State-Owned Enterprises (SOEs) where surplus employment is significant. Labor restructuring thus is understood as necessary to improve the effectiveness and competitiveness of state enterprises.

Whether restructuring should take place before or after a change of ownership is also an important aspect of strategic planning and is best resolved through a participatory approach with all stakeholders. Much of the labor restructuring that has taken place to date in Azerbaijan occurred well before privatization, when state enterprises themselves adjusted their labor force to improve performance.

In most Eastern European countries privatization--accompanied by redundancies and the introduction of hard budget constraints on enterprises--has resulted in large-scale job losses. This created a pool of unemployed workers that often cannot be absorbed by other privatized firms or new firms.

In Azerbaijan, the social effect of enterprise restructuring and privatization has been neglected for several years. This has led to increasingly volatile social pressure building up, especially in some industrial conglomerate areas. There is a strong possibility of social unrest if those who have been most affected by transformation begin to believe they will be among the long-term unemployed lacking any other employment alternatives.

Moreover, the delayed restructuring may have led to the departure of the best workers and thereby a loss of critical skills. The most skilled and capable employees tend to leave first, since they are able to find alternative employment elsewhere in the economy—even though the restructured enterprise would most likely want to retain them. This phenomenon was confirmed during the focus group survey of local employers in Mingachevir, who observed there already is a shortage of highly qualified workers--even in SOEs that generally remain overstaffed.

While large state-owned enterprise struggle to survive, a more vibrant and dynamic sector of the labor market exists in which new jobs are being created but there is a shortage of skilled labor. In Mingachevir as many as 30 percent of the firms surveyed for this study reported hiring new employees during the past year, and that over 90 percent of the jobs created were in firms with 30 employees or less. Importantly, over 20 percent of the firms indicated that lack of skilled labor is an important constraint for hiring new personnel.

The Government now wishes to design a model Social Support Program (SSP), or labor redeployment program (LRP), aimed at social protection and employment of persons displaced from privatized state-owned enterprises (SOE). The overall goal of a labor redeployment program is to facilitate enterprise restructuring by providing resources to affected workers, enterprises, and localities to: a) enable workers to remain in the workforce and contribute to economic growth in current or new localities, and shorten the duration of frictional and structural unemployment by ensuring worker access to active labor programs and services; and b) strengthen the economic base of regions affected by privatization through the design of local and/or regional economic development plans to create new job opportunities based on market principles (see Beck, Johansson and Fretwell, 1995).

The lack of experience on the part of authorities responsible for labor issues has hampered the coordination of an overall labor redeployment model in terms of design, costing, financing, delivering, and evaluating a labor redeployment program that is fiscally sustainability and contributes to improved performance of the social protection system.

For this reason, the study focuses largely on identifying informational and institutional gaps in elaborating a general labor redeployment program suitable for conditions in Azerbaijan. Suggestions for the introduction of labor redeployment activities and enterprise social plans are provided that would enable authorities to design relevant mitigating measures.

Chapter I. Labor Restructuring In Enterprises

1.1. Macroeconomic background of labor redeployment surveys

By all macroeconomic indicators, Azerbaijan enjoys one of the highest rates of economic growth in the region. The economy began to recover in 1996, and in the last six years, GDP growth rates are close to or expressed in double-digits (Table 1). During the last 5 years, GDP grew by 60 percent, capital investment increased 2.8-fold, and average wages increased 2.2-fold. During this period, the annual budget deficit was no more than 2 percent and inflation not exceeding 2.5 percent. The private sector share of GDP also increased significantly from 60 percent in 1998 to 73 percent in 2003, including a jump from 26 percent to 54 percent in the industrial sector (Decree November 24, 2003; World Bank 2003).

The economic growth is concentrated only in a very few sectors of the economy, especially in oil and gas, and in recent years also in metallurgy, construction, building materials, and agriculture. (See Annex I, Table 14 for growth rates in industries.) The mono-structural nature of the economy is illustrated by the fact that in 2002, the oil sector accounted for about a 30 percent of GDP, but only one percent of employment. [3] Even FDI inflows into Azerbaijan have been driven almost entirely by its oil and gas endowments. The largest individual non-oil investments are in construction, building materials, mobile telecommunications, and brewing. Developing the non-oil sector is Azerbaijan is important for macroeconomic stability, as dependence on oil makes Azerbaijan vulnerable to oil price volatility and Dutch Disease.[4] This is also the key to achieving broad-based growth and reducing poverty.

Table 1. Azerbaijan: Key social and macroeconomic indicators

	1998	1999	2000	2001	2002	2003
Population, millions: as of 1 July	7.763	7.983	8.049	8.111	8.172	8.234
Urban population, % of total	51.8	51.0	51.0	50.8	50.7	50.6
Employed (1000’)	3702	3703	3705	3715	3727	3747
Agriculture	1140	1567	1519	1484	1498	1499
Industry	251	259	249	247	252	252
Others	2311	1877	1937	1984	1977	1996
Unemployment rate *	1.1	1.2	1.2	1.3	1.3	1.4
Labor force participation rate, % **	84.4	82.1	80.0	76.9	77.2	77.4
Real GDP growth, % ***	10.0	7.4	11.1	9.0	10.6	11.2
Structure of output, % of GDP						
Agriculture	18.7	19.0	17.0	15.9	15.2	14.1
Industry	36.5	40.7	45.3	47.2	49.5	53.7
Services	44.8	40.3	37.7	36.9	35.3	32.2

[3] The broader effects, through the supply chain, have also been limited because most inputs for the oil and gas sector are imported rather than supplied domestically. (See FIAS 2002).

[4] Dutch Disease – an economic condition where sharp currency appreciation, fuelled by revenues from natural resources, makes a country’s economy uncompetitive.

Price Indexes, annual change, %						
CPI	-0.2	-8.5	1.9	1.5	2.8	2.2
Food price index	0.0	-11.0	2.3	2.7	3.7	3.2

* - registered unemployment;
** - ratio of economically active population to total employed and inactive population;
*** - IMF estimate.
Source: Asian Development Bank (www.adb.org); IMF.

While the economy has displayed robust growth during the past few years, job creation has remained flat: GDP growth has averaged close to 10 percent per year during the 1998-2003 period, while net employment creation has been one percent over the same period. The limited capacity of the economy to absorb new workers is aggravated by a fast-growing working population and by industrial downsizing and restructuring. While this should have increased unemployment rolls, it has not been the case: instead, potential new entrants onto the labor market have ended up as informal sector workers or joined the inactive population. The latter has been the case in particular for urban women.

Neither a large informal sector, nor extensive labor hoarding, are desirable features of a competitive economy – both issues point to significant inefficiencies in the use of national resources and need to be tackled as Azerbaijan moves forward into the international marketplace.

The recently approved State Program of Poverty Reduction and Economic Development (SPRED) has identified six strategic medium-term objectives: (i) enabling income-generating opportunities and jobs in the non-oil sector: (ii) macroeconomic stability; (iii) equity in health and education; (iv) improved infrastructure; (v) better targeted social protection; and (vi) better conditions for refugees and IDPs. These objectives can be achieved, among other tasks, though continued transformation of economic activity from the public to the private sector, and reducing administrative barriers to private investment and SME development. (See Republic of Azerbaijan (2002); World Bank 2003.) [5]

Paid employment is the main way of protecting the population from poverty. In the last few years, employment in absolute terms slowly began to increase: by the data of the State Statistical Committee of Azerbaijan, in 2000, 3.705 million people were employed in the national economy, with 3.747 million employed in 2003. Earnings from employment remain the main source of household income, accounting for 40 percent of total income, with the share being higher in urban areas (55 percent). Income from agriculture and self-employment is particularly important in rural areas, accounting for 59 percent of total household income (Republic of Azerbaijan 2002).

[5] A comprehensive diagnostic of the investment environment and administrative barriers analysis has been undertaken by the Business Environment and Enterprise Performance Survey (BEEPS) of the World Bank and EBRD, and by the Foreign Investment Advisory Survey (FIAS) of the International Finance Corporation and the World Bank. (See World Bank 2003 and FIAS 2002.) Surveys conducted under this study largely confirm the earlier findings.

Generally it is easier to undertake enterprise restructuring and privatization when the economy is improving, investment increasing, and unemployment going down. The worse the economic situation, the more political commitment is needed and the more carefully designed the social package--including temporary income support--must be.

The privatization process began with small enterprises, primarily in the service sector, such as retail, catering, personal services, and construction. Employee and management buyouts were the primary method of converting small enterprises. Privatization of large enterprises generally is proceeding in two stages. First, state-owned enterprises are converted into joint-stock companies, a process often referred to as “corporatization” or “commercialization.” Second, ownership shares are transferred by sale or some form of voucher distribution.

The privatization of small companies was successfully executed until 2001 within the scope of the first privatization program. In 2001 and 2002, three production enterprises were privatized per year (together with three sports stadiums in 2001). Six state enterprises were privatized in 2003 through investment competition, while over 1,500 medium and large enterprises have been turned into joint stock companies in recent years.

The majority of SOEs are completely deteriorated: plant equipment is worn out or is at least 30 years old and in need of replacement, so what remains can only be used in the context of targeted restructuring, privatization, or liquidation. With few exceptions, the products of SOEs are the same as in former socialist times without any major innovations and of poor quality and design. Moreover, the former markets no longer exist for several reasons: i) there is no demand for locally produced products since much cheaper and competitive imports dominate; ii) end-users are not known to local companies importing their products because third parties in Russia and elsewhere, as distributors of their own products, took over selling activities; iii) raw materials must be imported but no cash is available; and iv) specialists left the companies which led to a lack of know-how. (See ABU Consult 2003).

It is unlikely that a national or international investor would invest in many of these enterprises and purchase them within the scope of the announced investment tender, basically as markets for the products these companies once produced no longer exist.

The primary strategic decision is whether labor restructuring should be carried out by the government prior to privatization, or whether such restructuring should be left to the private sector. There are three options: (a) let the new investor deal with them; (b) have the government assist prior to sale; or (c) combine both approaches. All have their advantages and disadvantages, both in terms of the financial gains to the Government and in terms of the process of labor shedding and its social mitigation. Each approach needs to be carefully evaluated before a decision is taken.

Investor driven layoffs assume that the new investor will restructure the enterprise and address related labor requirements. This is the preferred option as the new investor is in the best position to know and plan the labor requirements of the enterprise he is buying.

Countries have followed different paths, depending on timetables, the nature of labor issues at the enterprise level, and the existing legal framework.[6] In Azerbaijan, many large state-owned enterprises are left alone to deal with their overstaffing and redundancy problems.

The employees of SOEs, who are still on the wage lists were for years left with the impression that there was still hope for these enterprises as soon as investors appeared. Slow privatization resulted partially from lack of appropriate social mitigation policy instruments.

As this problem has been neglected for several years now, an increasingly threatening social pressure has built up, especially in certain industrial areas. The longer the privatization of these enterprises is delayed, the more employees of these enterprises will be forced to look for an alternative source of income–which they often find in the black economy. There is a real danger of social unrest once those affected become aware of their long-term unemployed status without alternatives.

By its very nature, privatization is a political process. At the same time, it has important economic and social implications affecting not only economic and enterprise performance but also social welfare and stability. The social dimension of privatization must be viewed as an integral part of the privatization process. Thus, a balance must be sought between the economic objectives of privatization and the need for workers to have equitable and adequate protection.

To counteract negative social developments, measures must be initiated to prepare enterprises that have already been privatized as well as those still to be privatized of the demands of a system of free enterprise. This includes such factors as reducing the existing company’s size to obtain greater economies of scale, including physical facilities, land, production space, and plants, often looking to outsourcing as an alternative. An integral part of this process includes, as a priority, seeking ways to deal with the social impact of mass redundancies and unemployment.

1.2. General labor market situation

Labor market developments in Azerbaijan are affected by many demographic factors, including still relatively high fertility rates. The country belongs to the group of CIS states with fast-growing populations. Population age structure in Azerbaijan is also very favorable for population growth. In the coming years, the increased number of

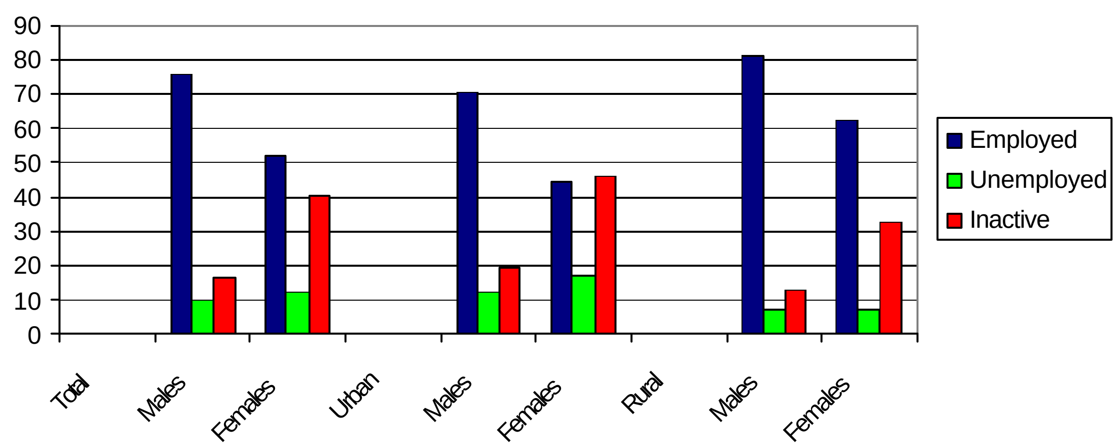
[6] The most comprehensive study of factors determining privatization prices, based on 236 privatizations in Mexico, found that a 20 percent reduction in the labor force prior to privatization would lead to a 24 percent increase in price (Lopez-de-Silanes 1997).

new labor market entrants will have a significant impact on labor supply. This growth in new entrants reflects the high birthrates of the 1980s. The country also has one of the lowest old-age dependency burdens among CIS states: the population share of those 65 years and older is only around 6 percent of the total population.

Despite a substantial drop in GDP in early 1990s, aggregate employment has been rather stable indicating that adjustment in employment has been less common in Azerbaijan. Data show 3.7 million people were employed in 1990, with the lowest level registered in 1995 at 3.6 million, or a drop of 4.2 percent. Real GDP shrunk 42.1 percent over the same period. The enterprises made corrections mainly by reducing real wages, cutting back on working hours, and placing workers on unpaid leave.

Higher growth rates provide greater opportunities for creating jobs. By 2003, the number of employed increased to 3.747 million. Employment elasticity (which shows the responsiveness of employment to economic growth) can be calculated by dividing the net new-job growth rate by the economic growth rate. In the last three years elasticity ranged between 0.03 and 0.05 annually, indicating that the job market has not responded adequately to economic growth.

Figure 1. Economically active and inactive population at able-bodied age (males 15-61, females 15-56), %



Source: STATCOM of Azerbaijan 2004.

In Azerbaijan, agriculture is the only sector with significant growth in employment during the transition period. This is directly related to a land reform which resulted in the allocation of farm lands and the issuance of land titles to new farm families. This process began in 1996 on 1,745 former state and collective farms the Government decided to privatize. The cultivable land on those farms was allocated to farm members. By 2002, some 838,000 land titles had been issued to rural families, with 1.3 million hectares of agricultural land distributed to rural residents. Essentially, growth in agricultural employment affected only the rural population, which typically has much higher employment rates and unemployment rates two times lower than the rates in urban areas (Figure 1). As a result of the land reform, the number of employed in agriculture (including hunting and forestry) increased from 1.140 million in 1998 to 1.515 million in 2001 (STATCOM of Azerbaijan 2001). Agriculture contributes about 18 percent of GDP and provides income and employment for 40 percent of households. In 1990, the total number of employed in agriculture and forestry equaled 1.144 million. In the last few years, the employment in agriculture has begun to decline, mainly due to productivity improvements in the sector.

After a decline of 72 percent between 1990 and 1995, the construction sector has played a dominant role in the economic recovery. Although the growth rate moderated during 1999-2001, construction accelerated again in 2002 and it is expected to receive another sizeable boost as a result of the rapid oil and gas sector development.

The services sector plays an important role for job creation, as it accounts for more than 40 percent of total employment. Services (including commerce, social services, transport, and communication) have grown steadily since 1995, registering strong growth of 9.2 percent on an annual basis (World Bank 2003).

In May-June 2003, with the support of the ILO and UNDP, the State Statistical Committee of the Republic of Azerbaijan for the first time conducted a nationally representative household-based survey on the economic activity of the population (i.e., a labor force survey). The survey captured baseline information on the size and structure of the economically active population. Findings included: nationally there were 3.378 million employed and 404,700 unemployed ages 15 and older, including 3.287 million males and 403,700 females of "able-bodied" age: males 15-61, females 15-56. The National Employment Service (NES) data showed 55,945 registered unemployed by end 2004; thus, only one in seven unemployed persons registered at the NES. [7]

In fact, the 1999 population census revealed much higher numbers of unemployed, at 552,600 (ILO definition), including 518,900 people of working age.

Indicators of unemployment are generally recognized as acceptable indicators of overall economic activity and its economic stability. There seems to be a trend for unemployment to decline and aggregate employment to increase. Labor force survey data in mid-2003 indicate an unemployment rate below 11 percent, which is near the average for transition economies. Compared to 1999 population census data, there has been a significant drop in unemployment in early 1999 from 14.2 percent among males and 18.6 percent among females age 16 and over to 9.6 percent among males and 12.2 percent among females at age 15 and over in mid-2003. By the end of 1990s, unemployment affected significant numbers of people; however, the unemployment rate did not increase proportionally due to substantial labor hoarding and an increase in small-scale agricultural self-employment and other informal activities. By 2003 the size of the economically active population had increased by 382,000 persons, or 11.2 percent,

[7] In 2003, only 3,111 of unemployed out of 54,365 registered by the National Employment Service received unemployment benefits.

compared to 1999 data. [8] A significant number of employees (32.2 percent) were temporary and casual workers in 2003, as captured by labor force survey data.

With regard to the education status of the population, Azerbaijan enjoys impressive educational outcomes for a country with its income level. It shows high enrollment rates at all levels of education regardless of gender, poverty level, or geographic location. At present, however, Azerbaijan has been struggling to sustain previously achieved education outcomes due to decreasing fiscal resources and increasing competition for limited funds, while reorienting its education system to the needs of a market economy and an independent country. Much of the Azeri workforce is quickly losing its skills and the existing skills are becoming obsolete, as reflected in the unemployment statistics.

Importantly, there is a clear correlation between the level of education, work experience, and unemployment. From 2003 survey data, 62.5 percent of respondents were unemployed and lacked employment experience, of which 72 percent were secondary school graduates. The survey showed that the percentage of unemployed among graduates of secondary general schools was 14.0 percent; among graduates of secondary vocational schools, 7.2 percent; among graduates of primary vocational schools, 6.5 percent, and among graduates of higher educational establishments, 4.9 percent respectively. (STATCOM of Azerbaijan 2004).

By international standards, compared to developed countries, Azerbaijan's labor force participation rate (LFPR) of 62.9 percent for those ages 15 and older can be considered high. In the USA, Australia, Canada, Japan, Netherlands, UK and Sweden, the labor force participation rate in 2000 stood at between 62 and 67 percent, in France, 56 percent, in Germany, 55 percent, and in Italy, 47 percent. [9]

There are however distinctive urban-rural and gender-related patterns of employment and unemployment in the country. In particular, labor force survey data show the employment rate of rural population at working age is 14.8 percent higher than for urban population, at 72 percent and 57.2 percent, respectively, and the unemployment rate of the rural able-bodied population is two times lower than the urban population, at 7.1 and 14.3 percent, respectively. Especially low is the employment rate for females of able-bodied age (15-56) in urban areas, at 44.2 percent. There are more inactive females of working age in cities than employed, and the unemployment rate among women in urban areas is also the highest, at 17.3 percent. (STATCOM of Azerbaijan 2004).

There is a significant and widening gap in employment rates for males and females. During the Soviet era, using 1989 population census data, male employment rates at age

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[8] The 1999 population census was conducted in January-February, i.e., off-season, which may have had an impact on employment and unemployment rates.

[9] Working age population – USA, France, Sweden and United Kingdom – ages 16 and older; Australia, Japan, Netherlands, Germany and Italy – 15 years, and Italy in 1990, 14 years.

In US Department of Commerce (2001), Statistical Abstract of the United States 2001. Washington, DC.

16-59 (including in subsidiary household plots) was 82 percent and females' employment rate at ages 16-54 stood at 66.2 percent. (GOSKOMSTAT SSSR 1991). Although the working age changed during the transition years because of an increase in retirement age, the employment rate for females has dropped 8 percent more than for males. This indicates that economic reforms, and especially enterprise restructuring, has hit the female labor force harder than males, especially in urban areas.

It formerly appeared rational for enterprises to maintain employment at high levels because returns did not depend on worker productivity or firm profitability but rather on access to state resources. Most extant industries have experienced job losses: first because of the decline in demand, and then to maintain or reinforce productivity by reducing the considerable over-staffing. Many enterprises may still have to go through a period of downsizing and restructuring, with further effects on employment and unemployment rates.

Labor hoarding in industrial enterprises is still significant. This was confirmed by the data of the Labor Flexibility Policy Survey in Industrial Enterprises of Azerbaijan, conducted in 2001. Although only 42 percent of the estimated production capacity was used, 25.6 percent of the respondents (managers of enterprises) confirmed that they could produce the same output with fewer workers, but 64.5 percent responded that the number of employees cannot be reduced to produce the same amount of production (STATCOM of Azerbaijan 2002). According to the recent Business Environment and Enterprise Performance Survey (BEEPS),[10] firms are operating substantially below capacity, with close to 50 percent of firms surveyed operating at below 40 percent capacity. This is reflected in the decline in labor productivity (as measured by output per worker), which remains well below 1990 levels. Thus substantial capacity remains in place.

Wage adjustments also have been noteworthy. In Azerbaijan in the 1990s, the dynamics of real wages has two distinct phases: the first half of the 1990s, and the period starting from the mid-1990s. The period of rapid inflation in Azerbaijan occurred in the early 1990s. In 1992, consumer prices increased by 10.1 times compared to the previous year, followed by a price hike of 12.3 times in 1993 and 17.6-fold increase in 1994. Between 1991 and 1995, a dramatic erosion in real wages also occurred, as wage growth lagged far behind employment and output growth. By 1995, real wages had dropped 17 percent compared to 1991. The decline in real wages in absolute terms (and relative to output declines) was sharper in Azerbaijan than in any other CIS countries (except Tajikistan) (CIS STAT 2001).

Since the mid-1990s, real wages have responded to economic growth, though the response was much ahead with respect to output. Especially in the last four years (2001-2004), the nominal growth of wages much outpaced the growth in GDP. For example, in 2001 the average reported wages in the national economy were AZM 260,000 while in January 2005, the average monthly wage was already AZM 532,100, or

[10] EBRD and World Bank, Business Environment and Enterprise Performance Survey, 2002. Approximately 200 firms in Azerbaijan were surveyed in this comprehensive survey covering private sector perceptions of the business environment and firm performance.

around US$110, which is 21.1 percent higher than in January 2004. According to data of the National Bank of Azerbaijan, nominal GDP increased for the same period by 7 percent. Such an unbalanced increase in nominal wages compared to enhancements in labor productivity may hamper the competitiveness of Azerbaijan's products and services in internal and external markets in the long run.

However, despite the recent turnaround, the level of real wages in Azerbaijan remains low. The relatively cheap and well-qualified workforce may be one of the main competitive advantages of industries in Azerbaijan. There is a concern, however, that in sectors other than oil, competitiveness is relying far too heavily on low labor costs, and that Azerbaijan may be locking into unskilled labor-intensive activities and low-productivity patterns of specialization. Productivity of the economy in Azerbaijan remains low by international standards, thus to a large extent offsetting the competitive advantages of low wages. Also given that real wages and labor productivity are increasing from a very low base, considerable growth is needed for Azerbaijan to close its wage and labor productivity gap with fast-reforming transition countries.

1.3 Selection and characteristics of survey sample frames

Official labor market statistics do not reveal the true unemployment situation. Although the local employment bureau in Mingachevir shows 1,715 registered unemployed on their roster (end-2004), the actual number might be several times higher. In the late 1980s, when big state-owned enterprises (SOEs) worked at full capacity, they employed more than 30,000 workers. Currently, on average SOEs use about 10 percent of total capacity, and some are completely idle. In addition, thousands of refugees and IDPs have moved to the city in the last decade.

The sample of unemployed was built on the database of the local employment bureau, and reflected the randomly selected redundant workers, mainly from 11 big SOEs that have undergone restructuring in recent years. These include former employees of the textile factory, glass factory, factory of technical rubber, two construction companies, and similar enterprises (Volume II Annex 2). Around 30 percent of the unemployed who were surveyed said they previously worked in other firms and organizations. An initial sample of 1,000 people was selected from the roster of the employment bureau. The actual survey sample was reduced to 831 individuals, after culling vacant residences, incorrect addresses, and respondent refusals.

The sample of enterprises from which the surveyed workers were selected was determined based on meetings with the city administration and staff of the local employment bureau. As a result, seven large SOEs were selected that were undergoing restructuring, and 10 percent of the randomly selected workers, or 477 people, ultimately comprised the survey population (Volume II Annex 3).

The sampling frame for the employment and job vacancy survey was selected from a list of approximately 2,000 entrepreneurs and small, medium and large business

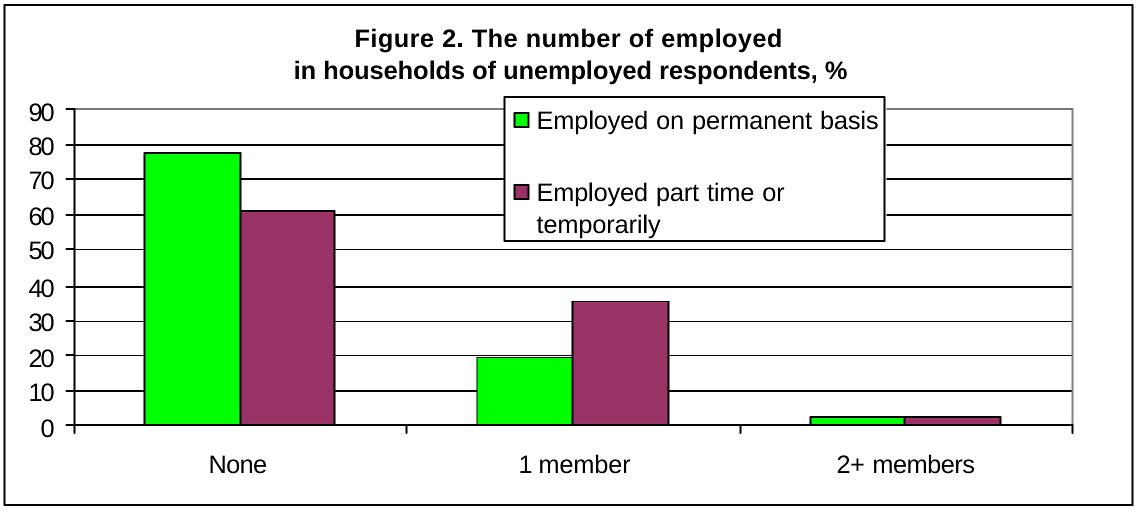
owners in the city of Mingachevir, registered by the Mingachevir Charter of the National Employer Association (MC-NEC). A stratified random sample of 100 respondents was selected by industry type. Sample representation by industry was determined based on MC-NEC data: 45 percent for wholesale and retail trade, 30 percent for services, transport and communication, and 25 percent for manufacturing and construction.

Selection of the focus group for the survey of business owners was not random and was based on reference. Of 21 business owners invited, 15 took part. A geographically diverse group, with 10 out of the 15 members from outside of Baku (i.e., Ganja, Sumgayit, Mingachevir, Barda, Imishli, Xachmaz, Gusar, Saatli, Zagatala), the survey participants also spanned a broad sector range of the non-oil economy, from agriculture and food processing to wholesale and retail trade and catering, to transportation and IT services, to banking, law and accountancy. In addition, a pilot study survey was conducted with seven business owners in Mingachevir, the results of which are also included into the analysis. In total, 30 respondents participated in focus group surveys of enterprise restructuring, including 15 managers and 15 employees and unemployed. Among the participants were also representatives of the local administration, including the Center for Social Protection, the local employment office, and local mass media. [11]

In Mingachevir, most of the individuals surveyed were at their prime working age of between 41 and 50 years old, with a high formal educational level. Around 49 percent of the workers and 44 percent of the unemployed belonged to this age group. The second largest group was between age 31-40, and 17 percent of workers and 10 percent of the unemployed were at pre-retirement age of 51-61 years. [12] Most surveyed unemployed had secondary general (53 percent) or secondary special education (22 percent), and 10 percent had a higher education. This indicates that many of the professional education establishments produce workers with skills that are not currently in demand in the labor market. Among the workers, these two groups of respondents with secondary general or secondary special education represent, respectively, 28 and 24 percent of the surveyed respondents. The largest group of workers surveyed had obtained a higher education (35 percent). Thus, workers surveyed who were still employed by SOEs attained higher educational levels.

[11] For more details on the sampling frame and complete survey results, see Volume II, Annex II to V.

[12] The official retirement age in Azerbaijan is 57 years for females and 62 years for males.



Source: World Bank/Institute of Labor and Social Protection (2004). Social monitoring of the displaced workers in Mingachevir city.

Most importantly, the employees still hired by SOEs are as a rule the primary and generally only wage earners in the households. In two-thirds of the households, he or she is the only family member who is employed on a permanent basis. For numerous reasons (delays in wage payments; he/she did not work although still on the enterprise roster; on leave, etc.), about 7 percent of workers received no income from salaries or social benefits and payments. And because of their "employment" status, they do not qualify for social assistance benefits. So any change in their employment status will hurt the welfare status of the whole household. Among the unemployed, 78 percent responded that no one in their household was currently employed, and only one member was employed in 20 percent of the households of the unemployed (Figure 2). Households are quite large: 42 percent of the unemployed and 38 percent of the employed lived in households of five and more members.

1.4 The characteristics of the working place before redundancies

In the city of Mingachevir, large enterprises dominate the local economy, which is also reflected in the size of companies. More than 42 percent of the surveyed redundant workers or workers still employed were and still are engaged in companies with 1,000 or more employees.

For many of the employees and unemployed individuals, this is or was their first job, i.e., 47 percent and 58 percent, respectively. Regarding years of work experience before they lost their job, 16 percent worked 25 years or more, and 50 percent between 11 and 25 years. Still-employed workers tend to have longer job tenure: 37 percent have been employed for over 25 years, and another 46 percent between 11 and 25 years. This may indicate that in making decisions about redundancies, workers with longer job tenure and older age may be given preference, or alternatively the workers with shorter job duration may leave first as their chances to find alternative employment might be greater.

Prior to their redundancy, 63 percent of the surveyed respondents worked in the production process or maintained machines, and were predominantly employed by SOEs (93 percent of total). Of about the same share of workers now employed, 62 percent of the total surveyed work in the same type of job.

Some portion of employees can be declared redundant based on their eligibility to retire from active service. Seven percent of respondents stated that they do meet some of the conditions for retirement. Moreover, 17 percent of the surveyed workers were age 51-61, and 3 percent at age 62 and over. So for some segment of employees, the transition from employment into retirement can be mitigated by offering an early retirement scheme for labor market reasons; others already have reached retirement age or fulfill other preconditions for early retirement proposed by existing legislation.

A vast majority of the unemployed have become redundant due to economic reforms, i.e., involuntarily. This is confirmed by the fact that 33 percent of the respondents became unemployed as a result of production stoppage in their firms; 28 percent as a result of a bankruptcy or liquidation; and 30 percent because of enterprise restructuring or privatization. Only 3 percent of the unemployed left their job voluntary. Nationwide, using labor force survey data, of those unemployed, 54.1 percent were dismissed as a part of staff reduction or closing enterprises; 7.4 percent became unemployed because of liquidation of their own business; and 13.8 percent because of completion of temporary, seasonal work, or contracts for a specified amount of work.

This shows that big industrial centers, such as Mingachevir, are much more vulnerable to economic downturns and transitional shocks. Surprisingly, in the last 12 months, 89 percent of the workers responded that the number of employees in their workplace remained the same, and 5 percent reported that the number of workers even increased, despite other survey results indicating still-existing labor hoarding by enterprises.

1.5 Labor market adjustments in SOEs

Wage or price adjustments, and employment or quantity adjustment, are the main forms of labor market adjustment to economic downturns. In addition, at the enterprise level, measures to avoid retrenchments may include:

- work sharing, such as arrangements for more flexible working schedules and more part-time work;
- delaying job cuts or spreading them over time, which would add to the cost of restructuring but save on unemployment benefits; and
- redeployment and retraining, where possible.

Adjustments in working hours are less common over the region, largely explained by the low level of real wages, which means workers cannot “afford” to work part time.

As discussed earlier, during the transition period, total employment did not decline much in Azerbaijan; however, certain sectors, especially in urban areas, have been hit hard. In particular, in the industrial sector, the number of employed dropped from 421,000 in 1990 to 206,000 in 1998; in construction from 223,000 to 63,000, and in transport from 184,000 to 68,000 for the same period (STATCOM of Azerbaijan 2001a).[13] These are the jobs that dominate in urban areas. Mingachevir city was also hit hard.

An alternative method of reducing labor costs of surplus workers is to cut their working time and thus wages earned. This method of "spreading the work" may be preferable to workers, compared to unpaid leave, as it maintains some income in addition to employment status. On the other hand, it indicates the potential for further redundancies in the surveyed companies. In Mingachevir, though a vast majority of surveyed employees (94 percent) work fulltime on a daily basis (8 hours a day), only 74 percent were engaged fulltime per month, while 15 percent were employed 10 to 20 days per months or even less (around 8 percent of workers were on annual or sick leave). The legal framework also accounts for the preference for full-time positions and discourages part time jobs.

Part time work is still not common in Azerbaijan, and is usually involuntary due to labor market reasons. According to the labor force survey, nationwide in 2003, employed males worked at a main workplace an average of 43 hours and females 37.5 hours, including 13.6 percent of males and 14.7 percent of females who worked less than 30 hours per week, and 22.7 percent of males and 17.7 percent of females, respectively who worked 41 hours or more per week.

One form of labor-hoarding is placing workers on unpaid leave. In some cases, workers are expecting the free distribution of privatization vouchers from their enterprises, so they maintain their employment record at the enterprise. In Mingachevir, three percent of the workers responded that they did not work at all, though they still appeared on the enterprise roster as employees. [14]

Labor market adjustments in SOEs mostly take the form of wage adjustments. In Mingachevir, threats for redundancies allow the management to keep wages low; most workers who are still employed have quite low wage levels. While the average wage in Azerbaijan in September 2004, when the survey was conducted, was AZM 473,000, almost 60 percent of surveyed workers in the city had nominal wages below AZM 300,000, and the wage of only 13 percent was over AZM 500,000 manat (or more than US$100). Wages are compressed and so low in almost all jobs that they can be disregarded as an incentive. Workers who were made redundant had much lower salaries before losing their job: almost half had salaries up to AZM 100,000 and another one-third

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[13] Since 1999, by the administrative data, the employment is registered based on the kind of economic activities versus employment by branches prior to that year, and thus the employment data by sectors and activities before and after 1999 are not fully comparable.

[14] The survey may have not captured all the workers on the payroll but not working, e.g., on the administrative leave.

between AZM 100,000 and 200,000. Such low wages partially may be attributable to many workers terminating their contracts many years ago.

Delays in wage payments in SOEs are common. Almost 80 percent of workers reported delays during the last 12 months, albeit most delays are short term, with up to 90 percent up to one month. Non-payment of wages also has caused great hardship on employees. Sometimes this has been caused by government subsidies being cut or simply not paid as failure to restructure became unsustainable. This also indicates that most enterprises surveyed are struggling to survive. In large SOEs, salary payments "in envelope" seem uncommon: nearly all respondents in both surveys (98 and 99 percent, respectively) reported they never received salaries unofficially under-the-table.

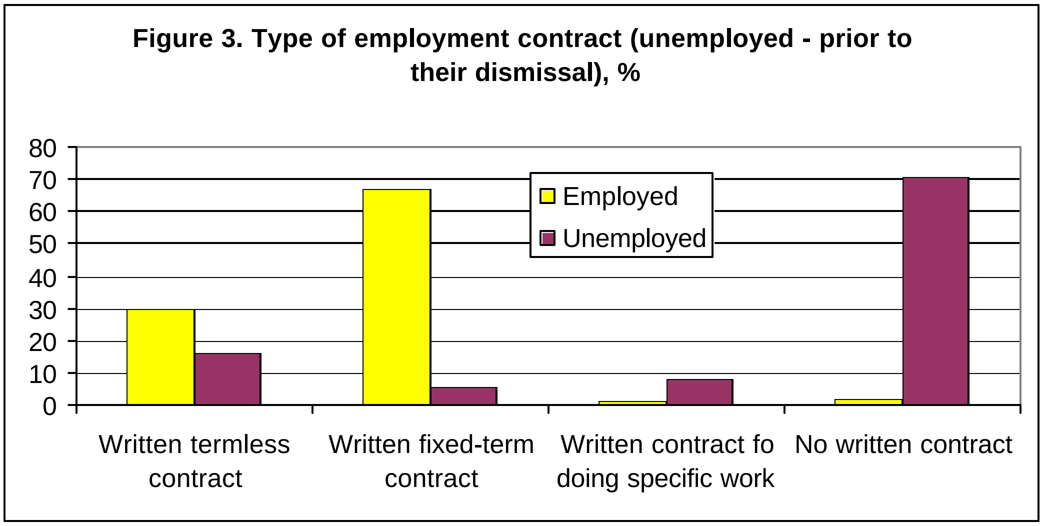
There are other direct and indirect indicators that firms may continue redundancies. In particular, 13 percent of respondents said that in the last 12 months someone they know in their company has been sent on unpaid vacation, and around 6 percent consider it possible that in the next year they will lose their current job. In terms of enterprise product development activities, only about 30 percent of respondents said that some new products, new ways of working or new technical equipment has been utilized or adopted.

In summary, despite the continuing job and wage cuts, many firms in Mingachevir continue to be overstaffed. On the other hand, all managers of SOEs interviewed during the focus group survey emphasized that their factories have enormous potential to hire additional personnel--except that there are no production orders designated for their factories. Previously employment levels were protected by guaranteed state orders and soft budget constraints. Now SOEs are struggling to adjust to market realities.

1.6 Labor contracts and other contractual obligations

Labor contracts are the most important contracts for most individuals. The terms and conditions of employment are stipulated in a contractual relationship between the enterprise and the employees, typically set out in legislation, in collective agreements, or in individual employment contracts. When those contracts are not respected and enforced, this reduces confidence in other labor and non-labor contracts into which the individual might enter. Based on the survey data, as it was typical in the Soviet period, most redundant workers in Mingachevir – 71 percent – had no written labor agreement, e.g., they were hired based on an internal order of the administration, typically for an open ended period of time. This may have had an impact in protecting their legal labor rights in the earlier years of transition, including with respect to back wages or severance payments.

The Law on Individual Labor Contracts, adopted May 1996, prescribes in detail the statutory framework for labor contracts in written form. Since many of the redundant workers were dismissed at an earlier stage, or the written contracts were not concluded with them prior to their dismissal, only 16 percent of redundant workers had written open-ended employment contracts; another 13 percent had written fixed-term contracts or contracts for doing specific work in a specified period of time.



Source: World Bank/Institute of Labor and Social Protection (2004). Social monitoring of the workers in big enterprises in Mingachevir city.

Currently employed workers are better protected. Around 30 percent of the workers have written open-ended employment contracts; however, 68 percent of workers have fixed-term contracts or contracts for doing specific work in a given time, and 2 percent still lack a written labor contract. According to the 2003 labor force survey, 32.3 percent of the employed population was hired by employers on the basis of a written contract for a fixed or specified time. In Mingachevir the share of workers in SOEs on fixed term contracts is significantly higher.

The Law on Individual Labor Contracts permits fixed-term contract for a period of up to 5 years. Although there are no other restrictions, given the unstable situation of SOEs, managers may abuse the fixed-term concept by instituting more flexible employment contracts. On the other hand, making flexible contract forms legal would give more employment options to managers in periods of high uncertainty, and bring more of the workforce into the 'formal' economy. Also, potential investors are not as concerned that they will become locked into indefinite contract obligations with an existing labor force.

Although workers engaged in the production process dominate the surveyed employees, for most employees, salaries are fixed, with little or no monetary or other incentives to work more. Thus the wage system in SOEs is quite rigid. Survey data reveal that 83 percent of workers received a fixed monthly salary; some 5 percent had regular additional payments to their salary; however, earnings of only 11 percent of respondents were linked to the results of their work.

Pension rights and entitlement to other benefits (sick leave; maternity leave, unemployment benefit, etc.) are directly linked to social contributions paid by the

employer. Nearly 75 percent of respondents who are still working reported that their company is paying all required contributions and taxes; 4 percent responded that social contributions and taxes are not being paid, and about 20 percent were not aware of the situation. Among the surveyed unemployed, 85 percent responded that the firm paid all required taxes and contributions in full. Large SOEs are typically more disciplined in paying taxes and are often more scrutinized by tax authorities.

Violation of labor rights is still common. As noted above, a significant share of workers (78 percent) experience delays in wage payments. Although most delays are short--51 percent up to two weeks and in another 37 percent up to one month--9 percent of workers received no wages for the last 2 to 6 months and 3 percent over six months. Redundant workers are in an even more desperate situation, with 27 percent owed wages by their previous employer.

ILO Convention No 95 clearly states that upon the termination of a contract of employment, a final settlement of all wages due shall be effected within a reasonable period of time having regard to the terms of the contract. Also according to this Convention, in the event of the bankruptcy or juridical liquidation of an undertaking, the workers employed therein shall be treated as privileged creditors as regards wages due to them for service rendered during such a period prior to the bankruptcy or liquidation.

Statutory payments, together with contractual benefits, can represent a substantial proportion of the overall payments to workers. Arrears, comprising unpaid salaries and social protection fund contributions, can be substantial if financial difficulties have led enterprises to defer payments for months or even years. In Azerbaijan a significant number of social benefits to working families--lump sum maternity allowance; maternity leave benefit; funeral benefit; several disability benefits, etc.--are paid by enterprises and the costs are deducted from social contributions. Enterprises may have trouble finding funds to cover these social benefits, especially on short notice, or such payments may be canceled altogether.

1.7 Severance payments

Labor relations are regulated by the new Labor Code that entered into effect in 1999. The Labor Code establishes the necessary provisions for a contractual agreement between legal entities and employees. In particular, the Labor Code permits termination for the following reasons, among others: i) the liquidation and reorganization of the enterprise or change in ownership; and ii) the reduction of contract employees or staff numbers.

Workers officially terminated are entitled to a severance payment from their former employers. Severance payment requirements make permanent separations a more costly way of reducing the workforce. According Article 77 of the Labor Code, the employee has the following entitlements when dismissed: (i) two months' notice before dismissal; (ii) during the notification period, the employee is entitled to one day off per week to search for new employment; (iii) on condition of registering as unemployed with the local Employment Center, and receiving an unemployment certificate (official unemployment status) delivered to the enterprise, he or she is entitled to one average monthly salary as dismissal payment, and, in addition, an average salary for up to three months after dismissal, or until a new job has been found. In case of bankruptcy, the owner of the enterprise (Ministry of Economic Development) is obliged to provide the severance payment. There is no special separation package in Azerbaijan for workers declared redundant as a result of mass layoffs, including for early retirement for labor market reasons.

Severance payments and unemployment insurance are typically the primary source of income support during the transition period to alternative employment. According to survey data, the majority of respondents (71 percent) were not informed about the basis for or the amount of severance pay. To the question, “Did you receive the whole amount of the severance pay?” 59 percent said yes, while 41 percent of unemployed workers responded they did not receive the full amount, which is in violation of the Labor Code.

Compensation for job loss is mostly spent on daily needs. About 95 percent of respondents spent their severance pay on living expenses, and only 2 percent tried to start a business of their own. This confirms that severance as seed capital failed to result in an appreciable level of development activity and new businesses were not created--partially because severance allocations are too small. Even if even intention is there, no additional support is provided by any other source of financial assistance, such as providing financial and advisory services for start-up of small businesses, for example, to help underwrite initial operating costs.

This confirms the experience of other transition countries as well, i.e., that the use of severance (or grants in lieu of severance) as seed capital for small businesses is generally not sufficient.. In most cases, there will be incompatibility between the basic attributes of the severance policy and the needs of a successful small business development program, which requires a supporting infrastructure and a filtering process that targets individuals likely to succeed in a small business. (World Bank 2002).

Many governments have resorted to voluntary departure programs by providing severance payments that exceed legally mandated requirements. The main challenge lies in devising severance payments that are attractive, financially affordable, and sustainable. In Mingachevir, as in SOEs in other regions of the country, most enterprises surveyed have major problems in paying even statutory severance payments.

1.8 Stakeholders’ involvement

There are many stakeholders, i.e., groups and institutions that may be affected by or influence the design, implementation, and outcomes of labor restructuring and privatization. Particularly the dialogue with trade unions and other stakeholders should start at the very beginning of the privatization and restructuring processes. ILO

Convention No 158 "Termination of Employment" suggests that in case of terminations of employment for economic, technological, structural or similar reasons, the employer shall (a) provide the workers' representatives in good time with relevant information including the reasons for the terminations contemplated, the number and categories of workers likely to be affected and the period over which the terminations are intended to be carried out; and (b) give the workers' representatives concerned, as early as possible, an opportunity for consultation on measures to be taken to avert or to minimize the terminations and measures to mitigate the adverse effects of any terminations on the workers concerned.

The full involvement of employee representatives in design, planning, implementation, and monitoring is desirable not just on ethical grounds but because it produces useful, tangible results for labor, society, and the enterprises themselves. In particular, trade unions are a source of knowledge and ideas both at the enterprise and macroeconomic levels. For example, they can recommend how to minimize employment and social costs, improve the quality of services, and increase enterprise competitiveness. In the absence of negotiations and even mere consultation, enterprise transformations in the region have met strong opposition.

There are two commonly used measures to assess bargaining possibilities: i) trade union density, i.e., union members as a percentage of the workforce, and ii) collective bargaining coverage, i.e., percentage of workers with wages determined by collective bargaining.

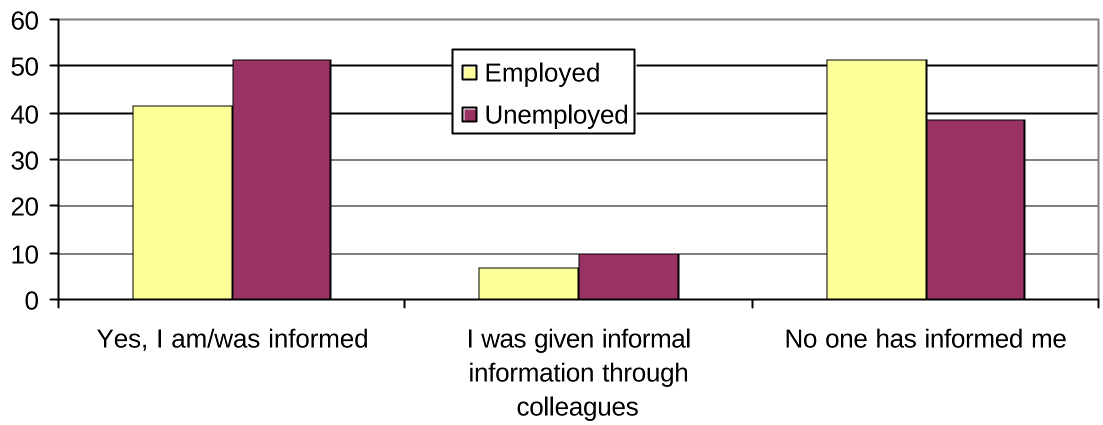
In the Soviet era, virtually all workers belonged to trade unions. However, the function of these unions differed greatly from those in market economies. Their major role was to provide social services, recreation and culture, housing, consumer goods and services in short supply, and sick pay. Collective bargaining over terms of employment, including wages, did not take place.

Currently, enterprises take part in the delivery of at least 11 social assistance benefits to families of workers and employees. The firms also pay pensions to working pensioners. So losing a job also means that some benefits, notably maternity leave payment, is interrupted until a new job is found.

Membership in trade unions is no longer universal. Available data indicate around 70 percent of employees in Azerbaijan belong to trade unions (EBRD 2000). The Labor Flexibility Policy Survey in Industrial Enterprises of Azerbaijan indicated that 68.5 percent of industrial enterprises had functioning trade unions, and 65.3 percent of the total number of employees in these firms paid trade unions dues. (STATCOM of Azerbaijan 2002).

Collective agreements over wages are not so common. According to 2001 data, in Azerbaijan agreements over terms of employment (including wages, premiums, benefits, and work time) were concluded in some form in 72 percent of enterprises, and in 55 percent of enterprises at the firm level and 14 percent at the branch level. However, negotiation over wage conditions rarely takes place, with real wage bargaining quite rare. Only 92 enterprises, out of 396 firms that concluded collective agreements in 2001, were wages part of the agreement. Thus, an important instrument for wage corrections does not function effectively in the country.

Figure 4. Availability of information about enterprise restructuring, %



Source: World Bank/Institute of Labor and Social Protection (2004). Social monitoring of the workers in big enterprises in Mingachevir city.

In the city of Mingachevir, whose SOEs are typical, the union density rate of 93 percent of workers is nevertheless high. The same rate of union membership appeared among redundant workers. As far as collective agreements are concerned, the survey revealed that only 59 percent of workers were informed about the existence of collective bargaining agreements in their firm. Only 10 percent of workers declared redundant knew of any collective agreements at their previous place of work.

Both employees and employers rated unions poorly in terms of their performance in representing the interests of workers during the restructuring process. Participation of social partners usually takes three main forms: i) information; ii) consultation; and iii) negotiation. About 52 percent of surveyed workers responded that no one informed them about the potential for or ongoing transformation in their firms, and another 7 percent received relevant information by word of mouth from other workers. Only about 44 percent of workers were informed about plans for privatization of their firm (if applicable). The unemployed sought information and thus were slightly better informed about the transformation of their enterprises before their dismissal. (Figure 4).

Moreover, trade unions perform very poorly in terms of informing their members about their legal rights, pursuant to the Labor Law, Law on Bankruptcy and the Law on Privatization, if and when they are declared redundant. Only 16 percent of workers were informed about their legal rights by trade unions, and another 26 percent informed themselves about their rights. Most workers were not informed at all about any ongoing transformation and related issues. Among the workers already declared redundant, 51 percent responded that they were officially informed about the transformation of their company, and another 10 percent were given information by colleagues. However, 30 percent of redundant workers were not informed, even about the grounds on which they would receive severance pay. These data indicate workers generally are not provided with information concerning their legal rights if and when declared redundant by either management or their trade unions.

Early communication and consultation with labor is important to ensure fairness and transparency of the process. Such efforts help build trust and support and assure workers that adequate arrangements are being made and measures taken to compensate them for losses and mitigate the social impact of adjustment. The fears and concerns of workers can be significantly reduced when explicit efforts are made to inform them about the objectives, timing, and methods of enterprise restructuring, as well as packages and incentives that will be developed to minimize social impact.

1.9 Training opportunities and provision of other ALMPs

Growth in labor productivity requires a highly qualified workforce. Continuing investment in education will be needed to develop a skilled and well-educated labor force. Typically real wages are higher for more educated workers; and highly educated individuals experience a lower rate and duration of unemployment than less educated workers.

ILO studies suggest that training is the third most important concern of employees after employment and income security, and is closely linked to both of them. The common objectives of training and related types of labor programs are to reduce the duration of unemployment and prevent displaced workers from entering a pool of long-term unemployed. Upgrading the labor force, or vertical mobility, is a precondition for rapid structural and technological change in transition countries to foster competitiveness in the world market and raise the share of high value-added products and services in those markets.

Two major forms of vocational education and training (VET) can be distinguished: entry-level training directed mainly towards training young people for their first job; and adult training. Despite the increased earning potential from education, a rapid decline in the number of graduates from professional schools has become a common phenomenon all over the FSU. To some extent it reflects the mismatch between proposed curricula and labor demand. The vocational education system in Azerbaijan is poorly targeted to skill shortages and is adjusting to market needs very slowly. Students are less inclined to opt for vocational education, which to a large extent suffers from old-fashioned curricula, worn-out equipment, and insecure labor market prospects. The structure of enrollment in VET and the structure of employment in the country are unbalanced. On the other hand, there has been a rapid increase in the number of students of general education establishments. This means that more and more labor market entrants need short-term, on-the-job training immediately after hiring, and their chances to find a job are reduced. (See Kuddo 2002 for details.)

The results of the Labor Flexibility Policy Survey in Industrial Enterprises indicate that between October 2000 and October 2001, 34.9 percent of enterprises had organized professional training for workers. On-the-job training was conducted in 29.3 percent of enterprises; 3.2 percent of employers organized the training classes in enterprises and 2.4 percent of enterprises organized training classes outside the firm (STATCOM of Azerbaijan 2002). However, the outcomes of enterprise training programs were not measured during the survey.

In a rapidly changing market economy, an individual's occupational future is uncertain, and educational institutions have to define occupations that are much broader and would enlarge employment opportunities for graduates. In many cases occupations themselves have become more complex.

Employment cutbacks are creating a strong demand for training for combinations of professions. Therefore, it is advisable to prevent early specialization and narrow-track vocational preparation. Instead, a more broadly-based foundation training for related occupations may be provided with progressive specialization (partly) taking place on the job at a later phase of vocational preparation.

Some of the VET providers have started offering new courses in areas of high skill demand – general occupational office services, administration, trade, commerce and other business services--but with a time lag and with varying quality assurance. Specifically, there is a need for training courses in how to create one's own enterprises in a particular field, or to become self employed or to work in small enterprises, as one of the preconditions for the development of entrepreneurship activities in the country.

Shortage of labor with relevant skills is one of the constraints for hiring new personnel, especially in SME sector (discussed fully in Chapter II). The survey in Mingachevir confirms that a significant portion of workers, one-third of the total, have tried to obtain retraining to enhance skills and qualifications to secure their current jobs or prepare to find jobs elsewhere if required. Most workers who do fail to seek training opportunities cite lack of money as a key constraint. Another 35 percent of respondents believed that even with retraining they would not find a new job.

Redundant workers are much less active in seeking training and retraining opportunities. Approximately 97 percent of unemployed workers responded that they never tried to obtain retraining, citing mostly lack of money. Most unemployed have never been included in any other active labor program. Only 16 percent of them participated in some of the employment programs provided by the employment service—nearly equal participation rates for training or retraining, employment counseling, and public works.

It is common throughout the FSU that only a small percentage of active job seekers ever apply for help at the PES. The 2003 national labor force survey found that only a fraction of the unemployed (4.3 percent of the total) applied to the State Employment Service for work. Of those unemployed, 41.2 percent sought a job with assistance of friends, relatives, and acquaintances; 11.4 percent by advertisement; with 5.6 percent applying directly to an organization or employers.

The minor role of employment services in job-seeking assistance reflects their poor reputation. In most cases, there is a serious mismatch between job offers registered with employment bureaus and job seekers both quantitatively and qualitatively. For this reason, a many job seekers do not restrict their job search to the PES. Employment services are to some extent a last resort when other sources have been exhausted.

Low participation of unemployed in ALMPs is largely because programs are heavily under-funded. Also the net impact of active labor programs on job placements has not been assessed in Azerbaijan. In 2004, the expenditures of the Employment Fund equaled AZM 15.4 billion, or around 0.04 percent of GDP (AZM 20.7 billion in 2001). This is one of the lowest ratios of GDP expenditures for employment programs among FSU states. Most spending is for job creation programs, which generally involve the creation of small agricultural firms under the auspices of local employment offices; however, these programs help only a small number of job-seekers. In Azerbaijan, job and vacancy fairs are also popular. Between April and August 2004, vacancy fairs were conducted in 18 rayons, which resulted in 1,058 people finding jobs. In 2003, the NES also offered training courses to 1,521 unemployed (around 3 percent of total registered unemployed), of which 95 percent participated in professional training courses for the first time.

In September 2004, a vacancy fair was organized in Mingachevir city in which 45 enterprises and organizations offered 627 vacant jobs, including 331 jobs for workers; 139 jobs for employees, and 157 jobs in the service sector; 193 jobs were offered in state enterprises and organizations, and 434 jobs in the private sector. Unfortunately, only 82 individuals were placed in jobs.

Despite a critical situation in the job market, job seekers are not eager to accept any job offers. Job rejections are related to low wages or unfavorable working conditions, or employer qualifications set too high for job seekers to meet. In particular, wage expectations of many of the unemployed (the reservation wage) are quite high. This could be explained by their previous social status and qualifications. The prevalent wage levels offered during the vacancy fair in Mingachevir were around AZM 200-300,000, i.e., wages of most workers currently employed in SOEs, but two to three times the minimum wage in the country; even so, this was insufficient to motivate people to accept a job offer. [15]

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[15] The level of a minimum wage was increased to AZM 100,000 in June 2004, and to AZM 125,000 in December 2004.

There are on average seven registered job seekers for every registered vacancy in the country, but regional differences in unemployment/vacancy ratios are enormous. Unemployment is partially structural: displaced workers lack skills, or their skills are not in demand, and need some re-tolling to compete and re-enter the labor market. There is demand for highly qualified workers, including metal-workers, welders, turners, drivers, carpenters, and construction workers; however, insufficient qualification levels of registered job-seekers in these specialties keep them from being placed in these jobs. In addition, almost half of all registered job seekers are between 18 and 30 years old, and thus frequently either lack sufficient work experience or have no work experience at all.

1.10 Looking for a new job

The longer the privatization of these enterprises is delayed, the more employees of these enterprises will be forced to look for alternative sources of income--which they often find in the informal economy. The lack of alternative jobs for workers adversely affected by enterprise restructuring is a major concern. And labor market rigidities make it harder for workers to move into new jobs as enterprises adjust.

Nearly 40 percent of the currently-employed are already looking for a new job, in most cases for more than 12 months although typically they seek another job in the same firm. This implies dissatisfaction with their current employment status. The biggest obstacle to finding a new job is that workers: cannot move to another town where job opportunities might be better (29 percent of respondents); lack qualifications or education (14 percent); or simply do not have the money for a job search (14 percent).

Most of the unemployed (70 percent) started to look for a new job immediately upon dismissal. The fact that almost all the surveyed unemployed are ready to begin working if an appropriate job becomes available confirms that these are indeed genuinely unemployed, i.e., they are without work, currently available for work, and are seeking work, and have taken specific steps to seek paid employment or self-employment.

Surprisingly most unemployed individuals fail to recognize that the biggest obstacle to finding a job might be lack of qualifications and skills. Only 24 percent of respondents mentioned this as a key obstacle. Also, a significant portion of job seekers believe that even with retraining they still will be unable to find a job. This includes 35 percent of job-seeking employed workers and 14 percent among the unemployed.

Among the unemployed, being out of work for a long period of time makes many willing to accept any job (41 percent); however, another 31 percent of the unemployed would only accept a job similar to the one they had at their previous qualification level. Many people still do not realize that labor market realities may not allow them to find a similar job. With regard to the job in which they expect to be employed, nearly half of the employed respondents (47 percent) look only for a job similar to their former one. The same is true for the unemployed: 49 percent are looking for similar jobs, but only about 14 to 16 percent (among workers and the unemployed) are looking for a job that differs from their former job. Clearly, the labor market situation has changed; nevertheless, this has not affected workers' aspirations to find similar work despite this change.

Workers inform themselves about available jobs and possibilities of new employment using different means. As is typical in other countries, many respondents (40 percent) are looking for vacancies through friends and relatives, and about 20 percent through colleagues in their firm. The Employment Bureau is the source of information only for 15 percent of job-seeking employees and 23 percent of the unemployed. However, chances to find a new job in Mingachevir seem to be slim: more than 90 percent of workers are seeking a new job, and the unemployed do not expect to find a new job or do not know when a job will become available.

Both the workers and the unemployed are attached to their current or last firm. Two thirds of workers and around half of the unemployed expect to find a new job in the same firm or where previously employed. This confirms that employment (inter-firm) mobility, in addition to skill and geographical mobility, is very low.

There is already a large and stagnant pool of long-term unemployed in the city. It is worrisome that about 40 percent of unemployed job-seekers have been looking for work more than two years. According to the 2003 national labor force survey, the average time for job-seeking by the unemployed was 15.6 months, and some 28 percent of the respondents had been unemployed for more than one year. This suggests that the labor market situation in Mingachevir is much worse than elsewhere in the country.

1.11 Creating small businesses

In an environment where obtaining a new job is difficult, starting one's own private business may be one option to overcome this problem.

As is common in other transition countries, relatively few job-seekers try to start private businesses. Only 15 percent of the unemployed and 9 percent of employed workers tried this. The main obstacle to establishing one's own business was lack of money or other means. Obtaining credit from banks is a significant obstacle, particularly for smaller entrepreneurs, who have little collateral to offer that normally would be acceptable to banks. There are additional constraints for the establishment of private small businesses or for becoming self-employed. In particular, among CIS-7 countries, according to the Doing Business 2005 report, in Azerbaijan the duration for business registration is by far the longest, taking on average 123 days, and involves 14 different procedures (See Table 2). (The business environment and private sector job creation are discussed in Chapter II.)

In Azerbaijan, the micro-finance sector is small and has not yet reached the stage of long term sustainability. Nevertheless, it plays an important role in providing access to credit for small and very small businesses, especially in rural areas. According to FSAP, 16 micro-finance institutions (MFI) currently operate in different regions of the country with total assets of AZM 80 billion (as of September 2003) serving about 30,000 clients. However, there is growing evidence that average loan size and interest rate levels are too high (3.5 percent per month), beyond the reach of most SMEs. (See World Bank (2003) for more details.)

In August 2002, a presidential decree[16] established a National Fund for Entrepreneurship Development (US$50 million) under the MED to provide a variety of funding for SMMEs, including micro-finance schemes, assistance to credit unions, and venture capital..

Table 2. Starting-a-Business Indicators – measures to register a business formally in CIS-7 countries and in some other countries

	Number of procedures	Time (days)	Cost (% of income per capita)	Min. capital (% of income per capita)
Armenia	10	25	7.0	4.5
Azerbaijan	14	123	14.7	0.0
Georgia	9	25	13.7	54.5
Kyrgyzstan	8	21	11.6	0.6
Moldova	10	30	18.6	24.6
Tajikistan	…	…	…	…
Uzbekistan	9	35	17.0	21.9
Average for 10 EU Accession Countries*	8	41	11.9	70.4
EU14**	7	31.4	9.4	36

* – Bulgaria, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania, Slovakia, Slovenia.
** - EU15 except Luxembourg.

Source: World Bank (2004).

SMEs account for more than 80 percent of registered enterprises in Azerbaijan. During the last five years, the share of SMEs in GDP grew from under 25 percent to almost 43 percent. However, as in many of the CIS countries, in terms of sales, small enterprises are growing much slower than their larger counterparts in Azerbaijan. Thus, the entire institutional infrastructure for the development of small businesses needs to be enhanced (discussed in detail in Chapter II).

1.12 Living standards of the surveyed unemployed and the employed

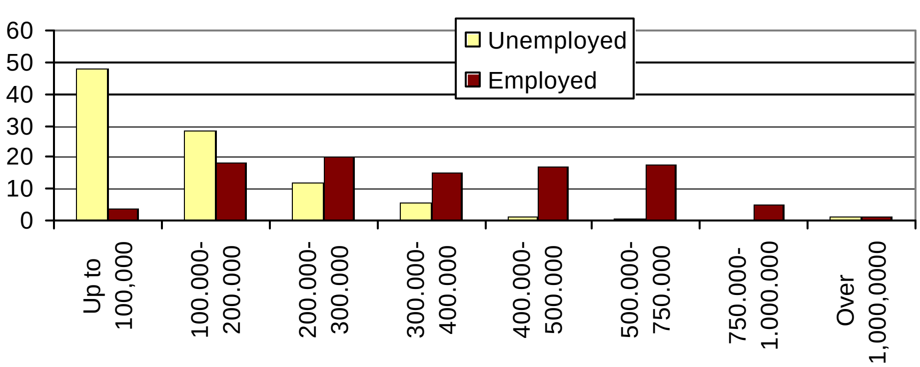
As a result of steady economic growth in Azerbaijan, average monthly wages and population money income is increasing rapidly, and especially the wage increase, which rate outpaces GDP and labor productivity growth. In 2001-2003, average

[16] State Program on Small and Medium Entrepreneurship Development in the Azerbaijan Republic (2002-2005). Approved by Decree No. 753 dated August 17, 2002, of the President of the Azerbaijan Republic.

reported nominal wages increased more than 20 percent annually. Money incomes of the population, by the data of the National Bank of Azerbaijan, in the last three years have increased 10-11 percent annually. (Annex I Table 3). According to preliminary results of the household survey, in 2003, some 15 percent of the population received income of less than AZM 120,000 per month (8 percent by aggregate consumption), or below the official poverty threshold. Approximately 80 percent of the population earned a per capita income between AZM 100,000 and 240,000 (71 percent using consumption data), e.g., most of the population show relatively similar income levels.

Survey data on incomes of families of the unemployed and workers in Mingachevir present a rather grim picture of their welfare status. Around 48 percent of the families of the unemployed had total incomes (salary, pension, social benefits, and income from agriculture) below AZM 100,000, and another 28 percent between AZM 100,000 and 200,000 (See Figure 5). This is largely because in 78 percent of the families of the unemployed no one is employed on a permanent basis; moreover, only one family member is employed in 20 percent of the households of the unemployed. In about 39 percent of the households of the unemployed, one or more household members are engaged on a part-time or temporary basis. As a result, in half the families of the unemployed, no one receives regular income from any source.

Figure 5. Average monthly income of the family in AZM (manat), %



Source: World Bank/Institute of Labor and Social Protection (2004). Social monitoring of the workers in big enterprises in Mingachevir city; World Bank/Institute of Labor and Social Protection (2004). Social monitoring of the displaced workers in Mingachevir city.

The low incomes of non-working families can be attributed to the low level of social benefits. The most important family program is the family benefit for low-income families, which is financed by the state budget. For children under 16 (or 18 if still in school), the monthly benefit per-child is AZM 9,000 (2 percent of the average wage in 2004), if the average per capita household income per month is less than AZM 16,500 (roughly 3.6 percent of the average wage). [17] This benefit has a very modest impact on household welfare status.

Most of the unemployed have exhausted their eligibility for unemployment benefits. According to the new Law on Employment, beginning in 2002, to qualify for the benefit, individuals must have 26 weeks of paid work in the last 12 months. The replacement rate of the benefit equals 70 percent of the amount of the last wage and can be paid for 26 weeks in a 12-month period. In other cases, the minimum benefit is paid at a level determined by local authorities. More than 80 percent of the surveyed unemployed have been out of work for more than 24 months, and another 7 percent between one and two years. So they would no longer qualify for the benefit.

Families of workers in the surveyed enterprises show significantly better welfare status. Still around 4 percent of them have household incomes below AZM 100,000, and 18 percent between AZM 100,000 and 200,000. However, in two-thirds of these households, the worker is the only family member employed on a permanent basis; in 24 percent of the families, one or more family members are employed on a part time or temporary basis. Among the workers' families, 7 percent received no income during the month prior to a survey, mainly because of wage arrears.

Survey results suggest even families of workers currently employed are vulnerable to any further shocks associated with enterprise restructuring and privatization. A vast majority of households of unemployed are living in extreme poverty.

1.13 Coping strategies

Survey results identified several coping strategies for households with both unemployed and still employed members. One traditional way unemployed individuals cope with economic downturns is by drawing down assets and not saving, especially for consumer durables. Two-thirds of unemployed respondent families sold some of their property to make ends meet. Reduced incomes also lead to reduced consumption, especially for expenditures for household durables, healthcare, education, and purchases of clothing, as well consumption of lesser quality food.

Some families may rely on in-kind incomes from subsidiary household plots or farmland. However, relatively few employed people in urban areas own land, farms or orchards (only 14 percent) or have a summer house outside town (6 percent). Among the unemployed respondents, the ratio of landowners or owners of summer houses with subsidiary household plots is more than twice as infrequent, partially because they may have already sold their land holdings.

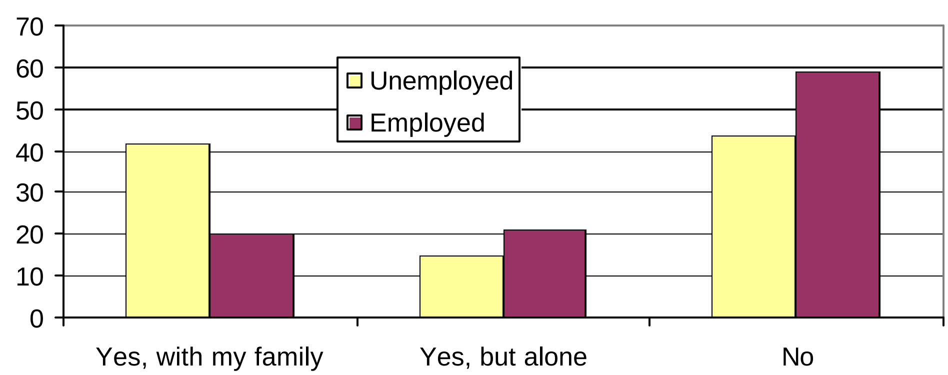
[17] The Household Budget Survey indicates that there are only about five hundred households that have incomes below AZM 50,000 per month in the entire country whilst around 600,000 families currently receive the benefit, i.e., the targeting errors are enormous.

Private transfers help the unemployed and the employed alike. Around 20 percent of both the employed and unemployed reported that other members of their extended family or friends supported them regularly or occasionally, and about 25 percent of the unemployed and 10 percent of employed received humanitarian or social assistance. The weakness of the official safety net is confirmed by the fact that 55 percent of the unemployed surveyed did not know where to apply for social assistance or humanitarian aid.

Better education may be a coping mechanism, especially for young people who cannot find a job, as better-educated persons are less likely to be unemployed. However, as noted above, only 3 percent of the unemployed surveyed have tried to obtain training and retraining.

Internal, and in the 1990s, external labor migration has affected labor supply in the country and in certain regions in two important ways: First, it arises as a response to lack of employment (or employment acceptable to the migrating individual); and second, it relieves the pressure on the local labor market for those who do not migrate, thus helping to achieve equilibrium in the local labor market (although those departing may be more likely to possess marketable skills and be more productive workers). Thus, labor migration to Russia and other countries in search of work, as well as remittances to support families at home, played an important role in mitigating unemployment and providing household income.

Figure 6. The share of employed and unemployed population who are ready to move to another place, %



Source: World Bank/Institute of Labor and Social Protection (2004). Social monitoring of the workers in big enterprises in Mingachevir city; World Bank/Institute of Labor and Social Protection (2004). Social monitoring of the displaced workers in Mingachevir city.

The scope of overall migration and labor migration, in particular, is difficult to estimate. According to official records, Russia alone has received 90,000 legal migrants from Azerbaijan; however, official estimates indicate that there are two million Azeris living illegally in Russia. Many people from rural areas and some towns are also moving to the Baku area—either temporarily (seasonally) or permanently--as employment and especially income opportunities in the capital are much more favorable.

The surveys confirm that a significant share of both the employed and unemployed population is ready to move out of Mingachevir. Around 42 percent of the unemployed and 20 percent of the employed are ready to move out of the city with their entire family (Figure 6. This is further evidence that job prospects in the city are slim. Whether these intentions are ever acted on depends on many factors. Generally, the economic constraints alluded to above prevent people from moving out immediately.

The high cost of moving, particularly given the rigidity of the housing market, has made out-migration for some groups quite difficult. The greatest obstacle to migration is the need for sufficient cash to purchase housing in a new region, as mortgage markets remain undeveloped. One of the major reasons for low territorial mobility of the workforce is the deeply-rooted cultural and socio-psychological customs and traditions and preferred patterns of living. People prefer to stay in regions where they grew up, went to school, and worked. Many households have tangible roots in the community, such as a plot or a summer cottage built during the Soviet period, or a piece of property that owned by their parents. In addition, they place great value on close ties with relatives, friends, and co-workers living in the region. Many people do not consider the lack of local employment opportunities a strong enough incentive to migrate. Such traditions and patterns cannot be ignored in the design of employment, investment, regional, or other policies.

Chapter II. A Glance at Labor Market Demand: Positive Developments and Challenges Ahead

2.1 Employment growth

The purpose of this chapter is to provide basic information as well as insights into the dynamics of labor market demand in Azerbaijan. Both job creation and job destruction are discussed in the context of obstacles to job creation and how to overcome them. Selected aspects of the types of jobs being created are also reviewed. Firms are disaggregated by industrial sector, size, and year of establishment to assess the relationship between job turnover and company characteristics. The general analysis incorporates the results of a survey of 100 firms in non-oil-producing activities in the district of Mingachevir.[18] The business environment in which firms develop their activities is also reviewed. This was accomplished by convening focus groups comprised of business owners in Mingachevir and other medium-size industrial cities in the country.[19]

Periodic monitoring of the dynamics of labor market demand is a prerequisite for improving economic, business, and labor policy. Labor market demand is an important barometer of economic activity in the country. Its evaluation can be crucial for making timely policy changes and adjustments. Trends of the labor market have immediate repercussions on employment forecasting and labor restructuring across industries. They also provide important indications about how to adjust and improve skills in the labor pool through targeted skill-upgrading programs to meet emerging demands. Moreover, gauging demand offers important leads on how to improve the business environment and enhance business growth, which is necessary for job creation. It should be noted that the discussion in this chapter is for illustrative purposes only. As the sample is not scientifically selected--and not representative of Azerbaijan in general--inferences should not be made about the country's overall labor market demand. Thus, the aim is to highlight some of the important aspects of labor market demand that ought to be further researched countrywide and subsequently discussed as a means to guide policy advice.

Survey results show a general positive trend in employment growth. During the past year, around 30 percent of the surveyed firms expanded their level of employment. The job creation rate was close to 14 percent, while the job destruction rate was just above 6 percent. Moreover, firms' expectations for the next six months are optimistic: 36 percent are planning growth in employment and the calculated job creation rate would be above 30 percent, with a negligible job destruction rate (1 percent).

Manufacturing and service industries are the largest contributors to job creation. Manufacturing and services sectors contributed around two-thirds of the total job creation during the year, and are expected to contribute a similar portion during the next semester.

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[18] See Annex 4 for a description of the firms and the sampling methodology.

[19] Investment climate in Azerbaijan, including legal and policy environment, and procedural and administrative barriers to investment are discussed in detail in FIAS 2002.

On the other hand, wholesale and retail trade industries show a larger job destruction rate than job creation for the past year. In fact, the latter industry alone has lost roughly the same portion of jobs as services and manufacturing combined. The expectations for the following months show a similar pattern, with manufacturing as the leading industry in hiring personnel

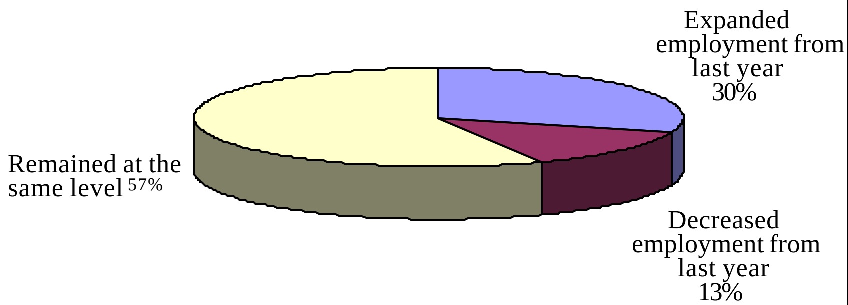
Most hiring takes place in small enterprises and most vacancies are sales and service-related positions. Small and medium-size firms are the most dynamic in the labor market. Overall, 94 percent of the jobs created during the last year were in firms with 30 employees or less. The same contribution is shown for job creation in the next six months. At the same time, most of the demand is for sales positions as well as for service-related personnel. In fact, 83 percent of current vacancies are for employment in these areas, while technical, clerical, and administrative positions are in low demand.

Instability, lack of access to financial resources, and lack of skilled labor rank as the three top constrains for future expansion and hiring of personnel. Despite the overall positive outlook on job creation, there are also some signals of uncertainty and constrains for future employment growth. For example, a large number of firms did not experience any growth in employment in 2004. As a consequence, almost 60 percent of them are either not planning to hire in the near future or simply do not know if they will do so. The main reasons given are (i) a sense of instability in their financial situation and (ii) lack access to loans on attractive terms from the financial sector. In addition, another significant factor preventing expansion and hiring of new personnel is (iii) the lack of skills in the labor market to meet the requirements of the positions available. In fact, the industrial sectors most dynamic for hiring (manufacturing and services) are the very ones encountering the most difficulty in filling their vacancies.

2.2 Labor market demand dynamics

A significant number of firms experienced growth in employment during the past year. As much as 30 percent of the firms reported that they hired new employees during the past year, while 13 percent replied that they decreased the number of employees. However, most firms responded (57 percent) that the level of employment remained unchanged from the previous year.

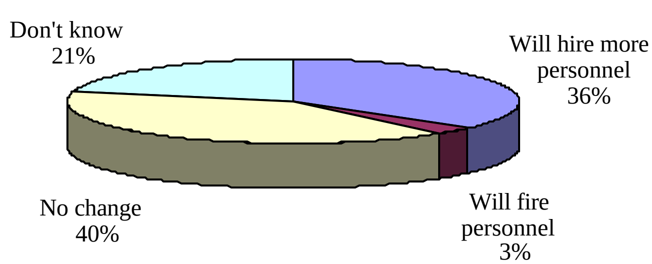
Figure 7: Sampled firms by growth status of employment



Source: World Bank/Caspian Business Consultants (2004). Employment and job vacancy survey in Mingachevir.

The expectations for employment growth mark a positive trend, but there is also some uncertainty. Around 36 percent of the firms expect to increase personnel during the next semester. This percentage is larger than firms which increased their number of employees during the previous year. Only 3 percent of the firms plan to decrease employment during the next semester, which is much less than the 13 percent of firms reporting a decrease in employment last year. However, many companies (40 percent) plan to maintain the same level of current employment the next semester. To this portion will be added the firms that "don't know" if any change in employment will take place in their firms, denoting some uncertainty.

Figure 8: Firms' expectations about hiring during the next 6 months



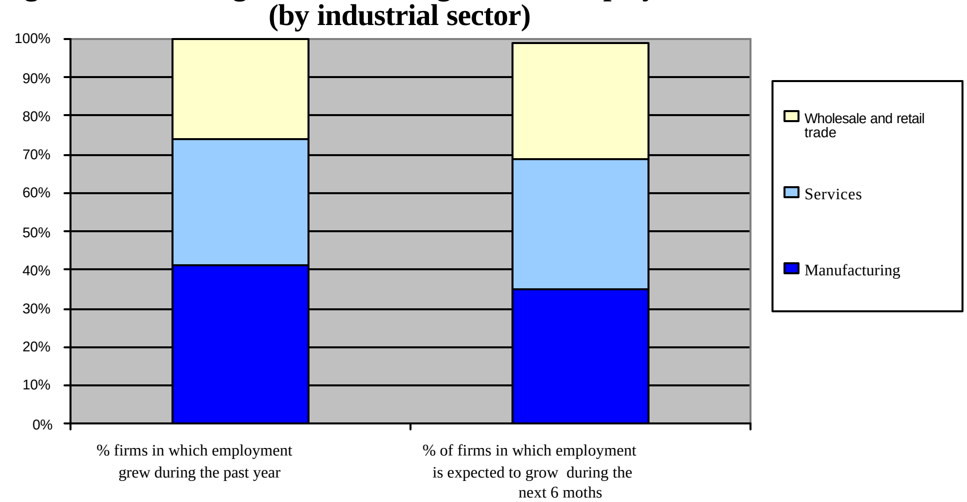
Source: World Bank/Caspian Business Consultants (2004). Employment and job vacancy survey in Mingachevir.

Job creation is more intense in the manufacturing and service industries. The largest percentage of firms that experienced employment growth operates in the manufacturing sector. In all, 41 percent of manufacturing firms responded that the total number of employees increased compared to last year. Firms in the service industry accounted for

33 percent of total firms that experienced employment growth the past year. As for expectations for the next six months, the same trend seems to hold, although the shares of manufacturing and services are similar. Manufacturing firms account for 45 percent of the total firms that expect growth in the number of employees during the next semester, while firms in the service industry account for 44 percent of that total.

Employment expansion was experienced during the last year. The job creation rate in the surveyed firms was in the order of 14 percent while the job loss rate was 6 percent, implying an employment growth rate of 8 percent[20]. The resulting job reallocation rate is 12 percent [21]. These indicators not only mean that more jobs were created than cut during the last year but also are a signal of a relatively dynamic job market in which jobs are shifting rapidly from firms that are reducing to firms that expanding employment. Again, we cannot extrapolate any inferences to Azerbaijan's labor market; however, these numbers show positive signs of enterprise restructuring for the district surveyed. Nevertheless, these numbers say nothing about the productivity, type, or level (i.e., salary) of the jobs created.

Figure 9: Percentage of firms with growth in employment (by industrial sector)



Source: World Bank/Caspian Business Consultants (2004). Employment and job vacancy survey in Mingachevir.

[20] Job creation rate is the sum of employment gains in firms that are expanding employment in a given year, as a portion of total employment at the beginning of the year. Job loss rate is the sum of all employment losses in shrinking firms as a proportion of total employment. Employment growth rate is the difference between the job creation rate and the job loss rate.

[21] Job reallocation is often times used as an indicator of enterprise restructuring. Therefore, the more jobs move from firms reducing to those expanding employment, the more intense the restructuring. The job reallocation rate is the difference between the turnover rate and the employment growth rate (See Rutkowski (2004) for a detailed discussion on these indicators)

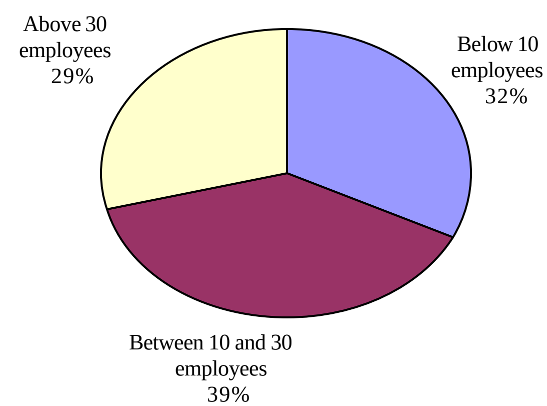
The outlook for job creation in the next six months is very optimistic. The calculated job creation rate is over 30 percent, while the job loss rate is negligible (just 1 percent). These results imply the caveats expressed above about the sample size, sampling methodology, and the locality where the sample was taken. In fact, there are some firms in the survey with exceptionally high expectations regarding hiring new personnel.[22] We also need to consider that most of the firms in the survey had only a few employees, which means that small increases in personnel in absolute numbers may be very high in percentage terms for these firms. Moreover, the number of vacancies currently available, as reported by firms, represents 8 percent of the total current employment, which shows a more conservative estimate of job creation at the moment.

Nevertheless, firms expressed optimism about the near future. These results, together with those obtained for the last twelve months, point to an upward trend in the labor market dynamism.

2.3 Employment growth by firm size

Small and medium enterprises (SMEs) concentrate most of total employment. Small enterprises with 10 employees or less employ 31 percent of the total employment in the sample. Around 41 percent of that total is employed in enterprises with more than 10 employees but less than 30. Thus, almost 75 percent of total employment is represented by firms with less than 30 employees. This condition indicates the relative importance of small and medium enterprises in the labor market of Mingachevir.

Figure 10: Concentration of employment by firms' size (size in terms of number of employees)

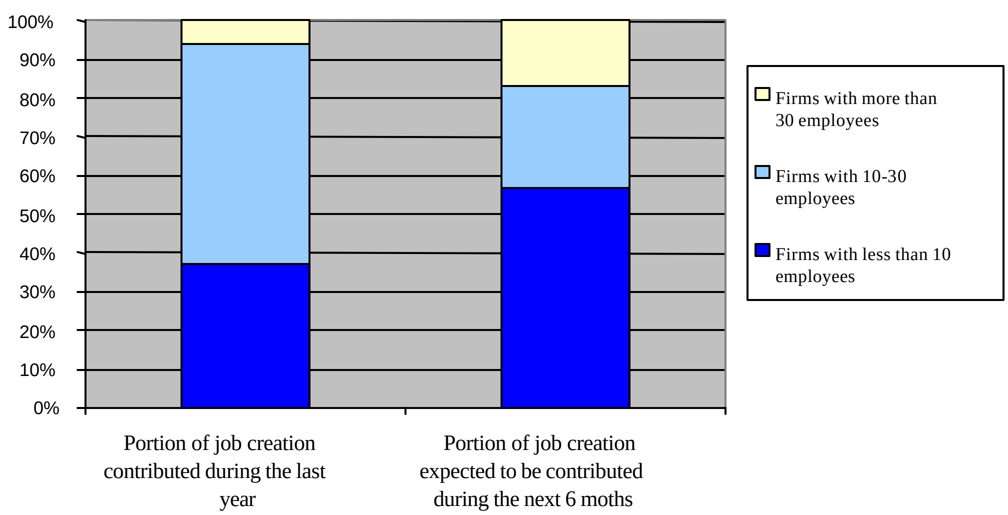


[22] In fact, one observation (one firm) was dropped from the sample as it was distorting the results. This firm expected to grow 300 percent in employment during the next 6 months. In absolute terms, this is an increase of 150 jobs, while the firm currently employs 50 people. Moreover, this firm grew to 50 employees from the 20 it had one year ago.

Source: World Bank/Caspian Business Consultants (2004). Employment and job vacancy survey in Mingachevir.

Small- to Medium-Enterprises are also more dynamic in the labor market. The largest concentration of growth in employment has taken place in the in SMEs. More precisely, 57 percent of the total new jobs have been created by companies with 10 to 30 employees (see Figure 11). Companies with less than 10 employees created 37 percent of the new jobs in past year. Job reduction during the past year followed a similar trend, as companies with 30 employees or less concentrate 87 percent of job destruction. On the other hand, firms with more than 30 employees have a larger role in job reduction than in job creation. The expectations for the next six months show a similar perspective. Overall, these trends show that SMEs contribute significantly to the dynamism observed in the labor market through job creation and job growth rates.

Figure 11: Percentage of contribution to job creation by firm size (firm size in terms of number of employees)



Source: World Bank/Caspian Business Consultants (2004). Employment and job vacancy survey in Mingachevir.

2.4 Employment growth by sectors and occupations

There are differences in labor market dynamism across industrial sectors. The services and manufacturing industries seem to be most dynamic in creating jobs. These industrial sectors accounted for 35 and 30 percent, respectively, of the market job creation during the past year (See Figure 12). The wholesale and retail trade industry has the same portion as the manufacturing industry in terms of job creation, with 40 percent of total job reduction in the labor market during the past year. In fact, this later industry alone has cut roughly the same portion of jobs as services and manufacturing combined. As for expectations over the next 6 months, the manufacturing appears to be the leading industry in hiring personnel (See Figure 13). However, it is closely followed by the wholesale and retail industry as well as the service industries. In terms of job reduction for the next semester, the wholesale and retail trade industry seems likely to follow the same pattern shown during the last year.

Figure 12: Pecentage of Contribution to Job Creation and Job Destruction by Industrial Sector (during the past year)

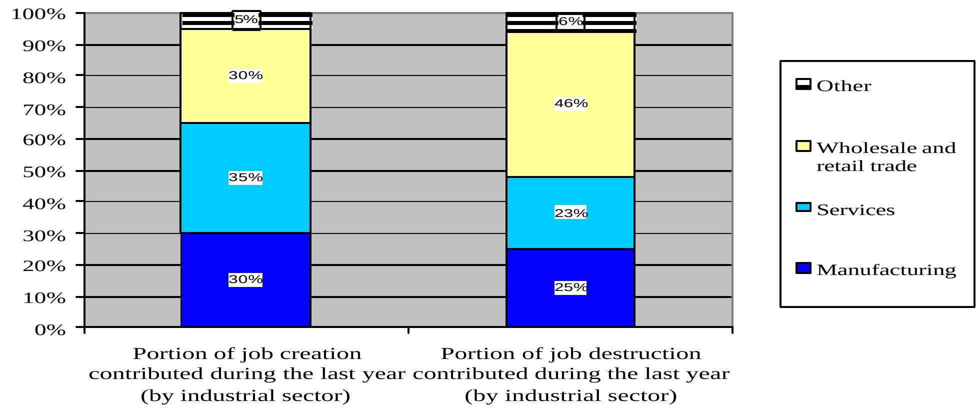
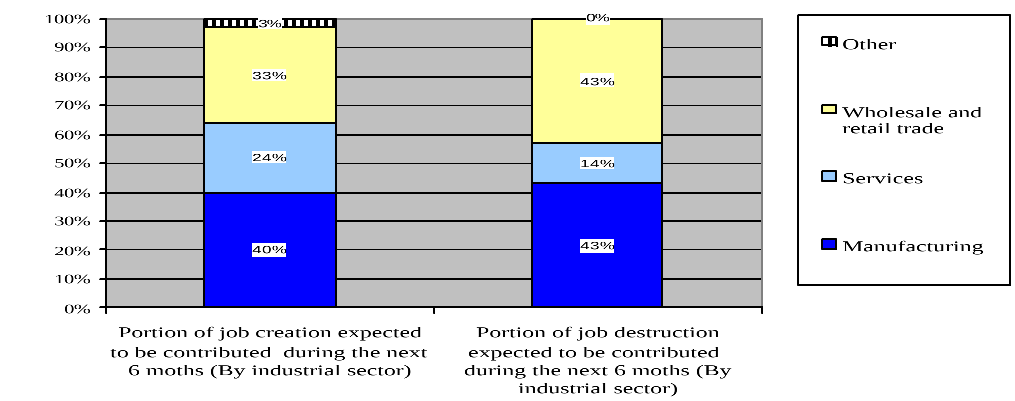


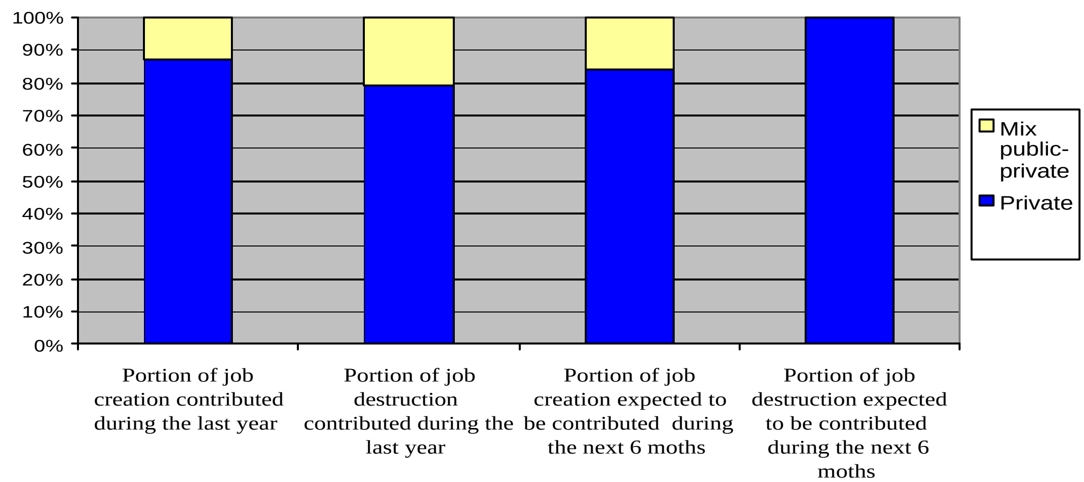
Figure 13: Pecentage of Contribution to Job Creation and Job Destruction by Industrial Sector (Expected next semester)



Source: World Bank/Caspian Business Consultants (2004). Employment and job vacancy survey in Mingachevir.

Purely private firms are more dynamic in the labor market than public-private, mixed ownership firms. In fact, the latter seem to behave more like the public sector. It is not a surprise that companies exclusively owned by private investors are actively generating changes in the labor market. In fact, this is typical in most countries while the opposite is generally true for the public sector, which is known to be passive in both hiring and firing personnel. An interesting feature is the behavior of companies with public and private shareholders. Typically, these partnerships operate in dynamic industries where private capital and know-how are required to improve production and management. Consequently, in most developing countries hiring and firing personnel is done proactively as they expand their operations and/or reduce overhead. The dynamics of such firms as observed in the survey however are similar to other mixed partnerships in CIS countries. The privatization modes carried out in these countries, through voucher and employee/manager buy-outs, combined with different circumstances, did not facilitate the participation of foreign investors, who typically promote innovation and change. In addition, it also seems common in CIS countries for the state to serve as major shareholder, which also constrains the innovative behavior typical of private firms, resulting in a more conservative, risk-averse, public sector approach.

Figure 14: Percentage of Job Creation and Job Destruction contributed By Firm's type of Ownership (past experience and expectation)



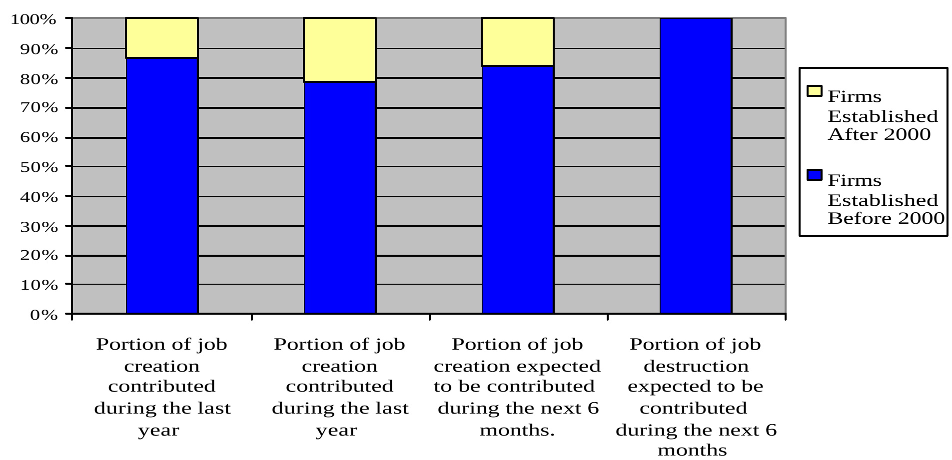
Source: World Bank/Caspian Business Consultants (2004). Employment and job vacancy survey in Mingachevir.

Older firms seem to be more active in hiring and firing compared to more recently established firms. **A**nother interesting feature observed in the sample is that firms established between 1992 and 1999 created 87 percent of the new jobs during the past year (See Figure 15), whereas firms in the survey established before the transition did not create a single job. More surprisingly, firms created since the year 2000 only created 13 percent of the new jobs[23]. Perhaps older, better-known firms have already created credibility in their markets, which accounts for the difference, among other factors; however, it is quite common in developed and developing countries for newer firms to show more rapid growth in employees, at least during the initial years. In that sense, this may be an indication of the need to evaluate more carefully the factors that could cause this result. The same pattern occurs for expected grow, which suggests an issue regarding the growth of newer firms.

[23] The sample is fairly balanced in this regard. As stated in Annex 4, 12 percent of the firms in sample were established before the transition (before 1992); 46 percent between 1992 and1999; and 42 percent since 2002.

Moreover, younger firms are struggling to grow. Findings indicate that the employment growth in firms established after 2000 was negative last year**.** Their job reduction rate was 12 percent while their job creation rate stood at only 10 percent. On the other hand, firms established before year 2000 experienced a growth in employment. The latter group of firms has a job creation rate of 22 percent and a job loss rate of 5 percent. Surprisingly, results show a more dynamic labor market demand in older firms, signaling potential obstacles that newer firms may face in the business environment.

Figure 15: Percentage of Contribution to Job Creation and Job Destruction by Firm's Year of Establishment



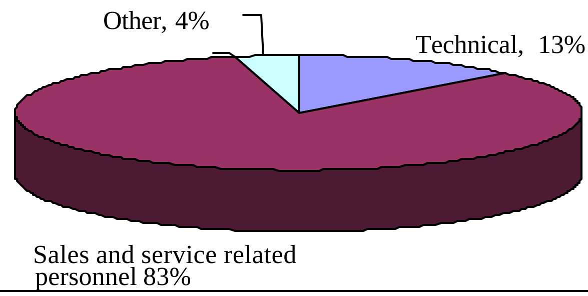
Source: World Bank/Caspian Business Consultants (2004). Employment and job vacancy survey in Mingachevir.

Most of the job creation in the sampled firms is geared toward filling sales and service related positions. Firms reported that most vacancies or job openings are for sales and service related departments[24]. Eighty-seven percent of job openings in the sample were for sales and service while only 13 percent were for technical positions[25]. None of the 100 firms reported vacancies for managerial positions at the professional level or for administrative personal (e.g., clerical). This trend can be observed in different degrees in most CIS countries where sales and service related job opportunities are growing fast.

[24] Here it would also be useful to present an analysis of current vacancies by industrial sector and its relative size compared to the total labor demand; unfortunately the data for this desegregation are not available.

[25] This question in the survey defines technical positions as those that require specialized skills and at least a secondary education.

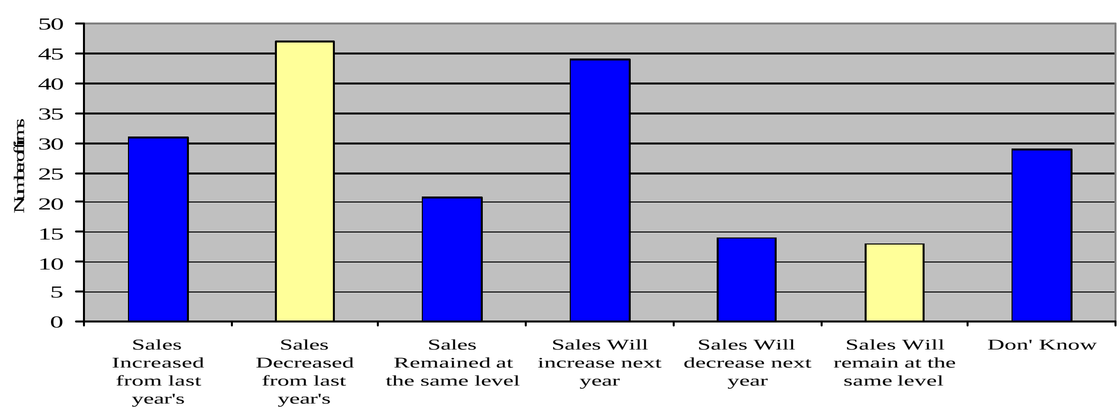
Figure 16: Type of vacancies available



Source: World Bank/Caspian Business Consultants (2004). Employment and job vacancy survey in Mingachevir.

Past experience and expectations about sales growth influence firm hiring plans. Simple correlation analysis shows that growth in sales during the last year was positively correlated with actual growth in employment during the period[26]. In the same way, sales growth expectations are positively correlated with new hiring. A more general trend regarding this relationship can be observed in figures 17 and 18, where firms with growth in sales in the past, and positive expectations about growth sales in the next 6 months, show considerable increase in employment. If these relationships are linked to type of vacancies (see figure 16), by inference companies with positive expectations about sales (44 percent of firms) are preparing themselves for an increased demand for sales personnel, and thus anticipating employment growth in sales positions. Moreover, possibly even those companies that are uncertain about future sales, or have experienced a decline in sales, want to scale back or freeze hiring of clerical and administrative personal; nevertheless, they still want to prepare for improved sales next year by hiring sales personnel.

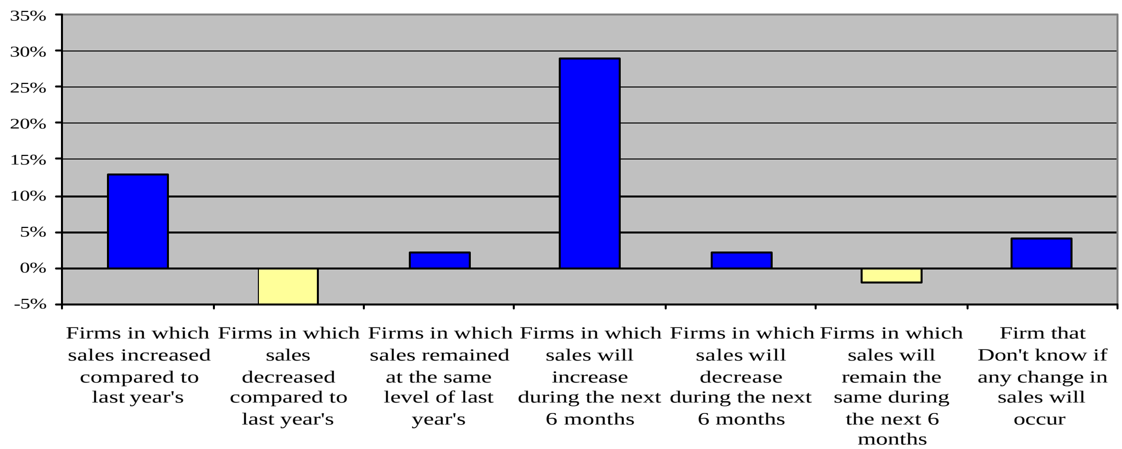
Figure 17: Past experience and expectation for sales



[26] The correlation is not very strong; however, this may be attributed to statistical factors, such as the number of observations. In any case, the trends in employment, type of vacancies, and sales point to the same finding.

Source: World Bank/Caspian Business Consultants (2004). Employment and job vacancy survey in Mingachevir.

Figure 18: Growth in employment by firm's sales growth past experience and expectation.



Source: World Bank/Caspian Business Consultants (2004). Employment and job vacancy survey in Mingachevir.

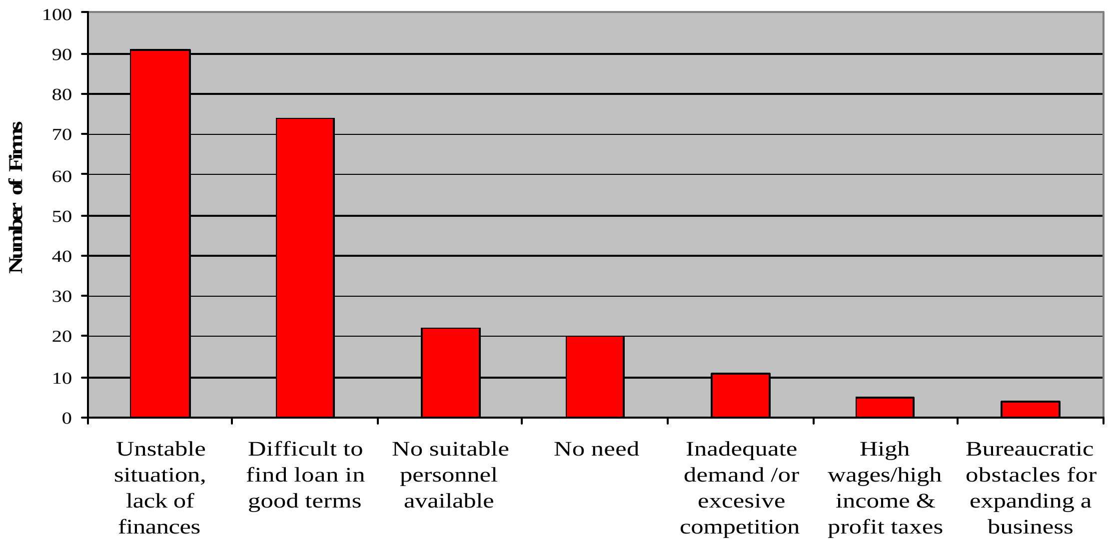
2.5 Uncertainties in employment growth

Despite an overall positive picture of job creation, survey results also found that companies experience uncertainty about growth in personnel. Figure 7 showed that 57 percent of firms did not change the level of employment over the previous year. Figure 8 indicates 61 percent of firms either will not be hiring personnel during the following six months or simply "do not know" if they will do so. These numbers could be taken as a signal of uncertainly about future conditions. Alternatively, they may indicate demand or supply-side constraints that prevent firms from expanding. Consequently, further analysis is required to determine why firms did not hire personnel in the past, and why they would become reluctant to hire more personnel in the near future. At the same time, as a general rule, in all economies the majority of firms do not change current employment levels in the short term.

Lack of financial security and access to new financial resources for expansion are the main reasons for not expanding and hiring new personnel. When companies were asked to provide the three main reasons for not hiring personnel, financial uncertainty and difficulties in accessing banks' loans under reasonable terms ranked at the top. Other, more classical reasons, such as high payroll tax and labor legislation, were not consequential. [27] Thus, the main obstacles to job creation lie beyond the labor market.

[27] In fact, labor legislation was not mentioned at all as a reason for not hiring personnel. Payroll taxes are further discussed in Section 2.6, with the focus-groups results.

Figure 19: Main constrains for not hiring new personnel

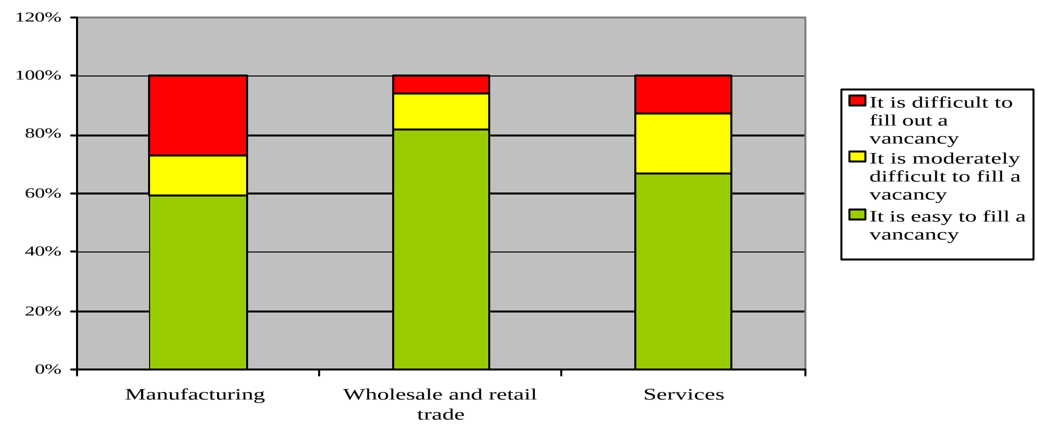


Source: World Bank/Caspian Business Consultants (2004). Employment and job vacancy survey in Mingachevir.

Lack of skilled labor also prevents firms from hiring more actively. Over 20 percent of the firms reported that another important constraint for hiring new personnel is that applicants for job openings simply do not meet the firms' skills requirements. In fact, lack of skilled personnel ranks third among the reasons for not hiring more personnel. Moreover, a question about the degree of difficulty of filling new vacancies revealed that almost 20 percent of the firms believe there is at least some degree of difficulty finding the right people to fill new openings. Specifically, 12 percent responded that it is difficult to fill new job openings, while 14 percent found it moderately difficult. This result suggests a mismatch between the available skill supply and skills in demand in the labor market.

It is relatively more difficult to fill vacancies in the manufacturing sector. Analyzing this issue by industrial sectors may only provide hints about a possible poor fit of skills in the labor market; on the other hand, it can provide an indication about where in the economy the problem is most acute. Disaggregating the data reveals that in relative terms the manufacturing sector suffers more from not finding adequate candidates compared to other sectors (See Figure 20). The sector of wholesale and retail trade seems not to have any problems in this regard. Finally, it is only moderately difficult in the services industry (mainly composed of hotels and restaurants).

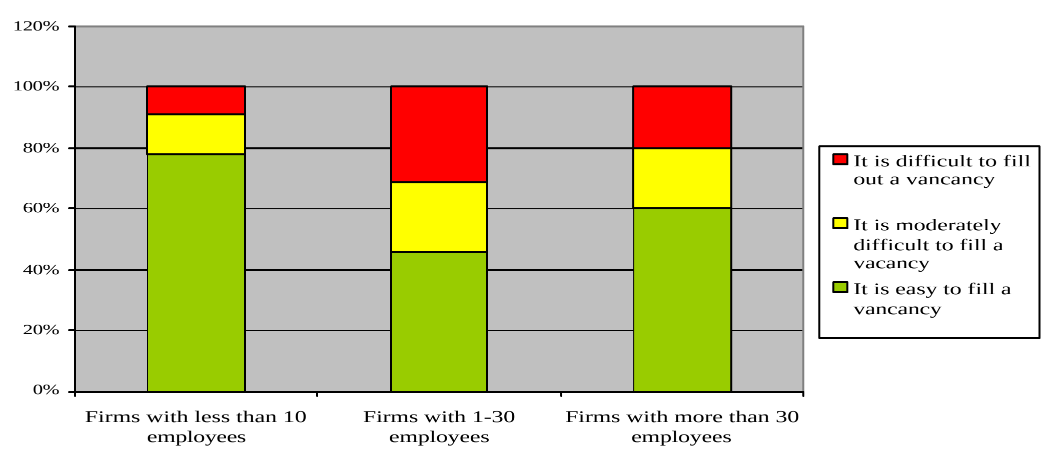
Figure 20: Degree of Difficulty Finding New Personnel to Fill Out Vacancies



Source: World Bank/Caspian Business Consultants (2004). Employment and job vacancy survey in Mingachevir.

Additionally, there is some evidence that larger firms experience more difficulty finding suitable personnel to fill vacancies. The results in the sample clearly show that smaller firms do not have much trouble finding new personnel. In fact, 78 percent of firms with less than 10 employees argued that filling a vacancy is easy; only 9 percent of these firms said that recruiting suitable personnel is difficult. But this result changes for larger firms (see Figure 21). Firms with more than 10 but less than 30 employees apparently face more problems in this regard. In total, 54 percent of these firms argue that filling new openings is either difficult or at least moderately so. The simple correlation analysis also shows a positive correlation between the degree of difficulty of filling new vacancies and firm size (measured by number of employees).

Figure 21: Degree of Difficulty Filling Out Vancancies by Firm Size (firm size in terms of number of employees)



Source: World Bank/Caspian Business Consultants (2004). Employment and job vacancy survey in Mingachevir.

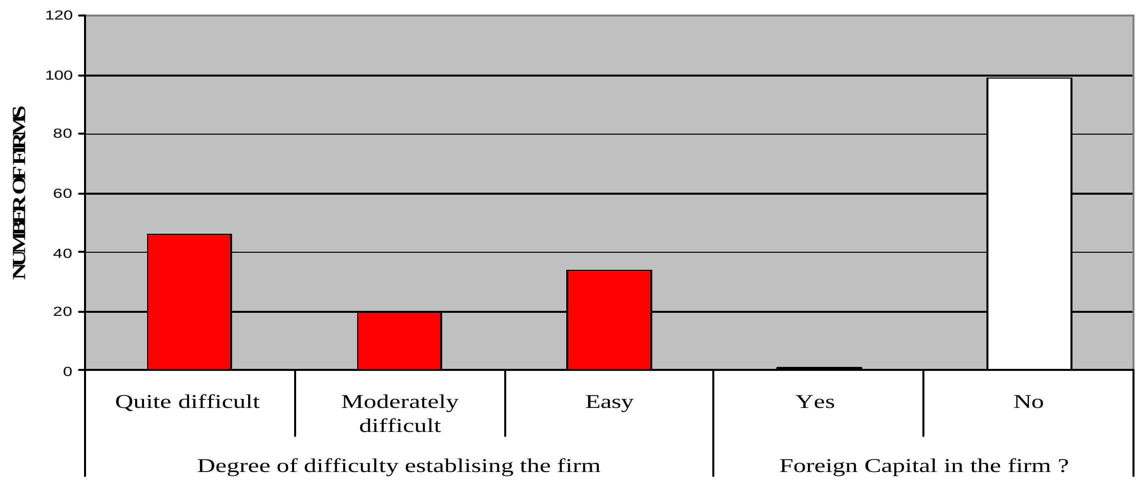
2.6 Business environment and firms' employment expansion

It is difficult to establish a new business in a country that negatively affects the job creation rate. More than 40 percent of the firms sampled agree that it is quite difficult to establish a new business. In total, more than 60 percent agreed that there is at least some degree of difficulty when going through the process of legally starting a new business. Moreover, these results may even underestimate the difficulties of starting a business in the country: as the sample obviously only considers firms currently operating, other entrepreneurs might already have been discouraged at a preliminary stage and never created a business at all. [28] The focus group results confirm the existing difficulties in formally establishing a business. Some of the aspects the business owners claimed as severe deterrents to business creation are burdensome business licensing processes, obtaining land and construction permits, and formalization of real state transactions. However, the participants of the focus groups also agreed that that the licensing issues have at least improved somewhat compared to two years ago. Evidence from other transition economies show that business start-ups account for a large proportion (from 25 to 50 percent) of new job creation. Thus, obstacles to firm entry in Azerbaijan translate into lower job creation and employment growth.

The difficulty of establishing new businesses is reflected in low foreign direct investment. Typically, countries where the business environment is inadequate or enabling for business creation have lower levels of foreign direct investment (FDI). The typical reasons that foreign investors argue for not entering into business in a country are similar to those expressed by local firms in this survey, such as unstable conditions and lack of skilled labor force. Interestingly, this may be the case in Azerbaijan, which exhibits a low level of FDI in the non-oil sectors surveyed. Only one firm out of 100 in the sample had a participating foreign investor.

[28] As in other areas, the sample is biased when analyzing obstacles to establishing new businesses as it only considers operating business and not those that were discouraged from entering the market.

Figure 22: Degree of difficulty of Establishing a Firm & Foreing Direct Investment



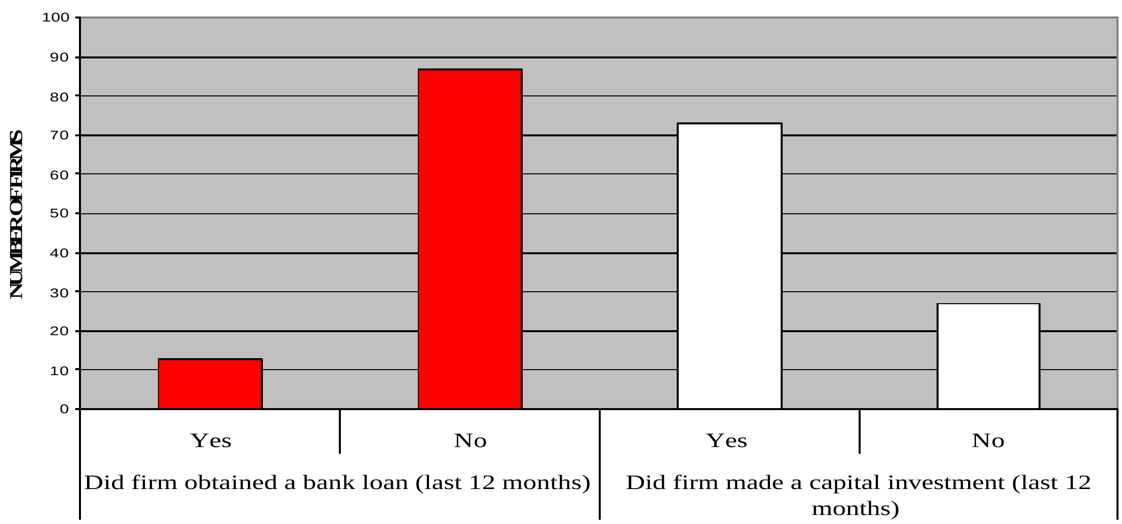
Source: World Bank/Caspian Business Consultants (2004). Employment and job vacancy survey in Mingachevir.

Growth of business in the country is affected by an unreliable rule of law and bureaucratic corruption. When the focus group participants were asked about the constraints for growth in their business relative to the regulatory and governance framework, rule of law and bureaucratic corruption ranked as the most serious problems. Business owners complained that the rules and regulations change continuously, and are complex and contradictory in some cases. Moreover, they said that courts, including the ones responsible for corporate law, are not independent and do not protect firms from the state's perceived unfair practices. They alleged a selective and discretionary enforcement of business regulations on firms that is related to business interests of state officials. A concrete example encompassing these issues occurred in customs. Firm owners noted that customs regulations and enforcement represents a severe problem constraining expansion of business. Enforcement occurs selectively, and custom procedures for export and import have led to arbitrary processing delays.

Access to financial resources, although improving, remains a central constraint for business growth and employment expansion. As shown in Figure 19, access to financial resources under favorable conditions ranks at the top of the reasons why firms allege they are unable to expand employment. The focus group results also spoke to this issue. Participants said that their expansion is severely limited by lack of access to long-term bank loans, high interest rates and no access to alternative financial instruments. Maturity in commercial loans is said to be only short term, averaging between 6 and 12 months. This problem is compounded by rising interest rates and lack of access to instruments such as leasing. Nevertheless, firms also argued that the overall situation in accessing financial markets is showing some improvement compared to two years ago.

Low borrowing from the financial sector seems to affect employment expansion in the firms but does not deter new capital investments. The results of the survey show that companies are not financing their operations and investments through the financial sector. In fact, 87 percent of them have not obtained a bank or other financial institution loan in past year. As noted above, this is an important deterrent to employment expansion. However, this has not deterred firms from making capital investments. In fact, more than 70 percent in the study made some type of capital investment (e.g., in machinery, equipment, or real estate) during the last year. Nevertheless, caution must be exercised about this finding as the investment amount is not known, and could easily be insignificant.

Figure 23: Firms' Borrowing and Capital Investment



Source: World Bank/Caspian Business Consultants (2004). Employment and job vacancy survey in Mingachevir.

Labor regulations represent a problem for employment expansion for firms, but there are mixed opinions about the effect of payroll taxes. Results from the focus groups indicate that firms do not view labor regulations as a constraint on expansion. Hiring, firing, and other rules embedded in these regulations are not considered impediments when companies decide to expand employment. Payroll taxes, on the other hand, seem to be a relatively important issue for some firms. Firms located in districts other than Mingachevir argued that high personal income tax and social contributions discourage formal employment as well as wage increases. They suggest that this places serious constraints on business expansion. While firms operating in Mingachevir identify this as a problem, they downplayed its relative importance.

2.7 Main obstacles for firm growth and job creation

In summary, the main obstacles for firm growth and job creation, as perceived by entrepreneurs, are as follows:

- Difficulty in establishing a new business (burdensome business licensing processes, difficulties in obtaining land and construction permits, and formalization of real estate transactions)
- Lack of access to financial resources on favorable terms (short time to maturity, high interest rates, lack of financial products)
- Lack of skilled personnel (mainly for sales and service-related positions)
- Unreliable rule of law (complexity of rules, contradictory regulations, constant changes)
- Bureaucratic corruption (discretionary enforcement, arbitrary procedures, particularly in Customs)
- High payroll taxes and social contributions

Bureaucratic corruption negatively affects business growth. When the entrepreneurs participating in the focus group were asked about the constraints for growth on their business relative to the regulatory and governance framework, corruption ranked as one of the most severe problems. Business owners alleged selective and discretionary enforcement of regulations affecting firms, often depending on whether or not the firm was willing to pay a bribe. This bureaucratic corruption and arbitrary behavior by public officials occurs in all spheres of the government that have interactions with private firms. The most acute cases, as argued by firms are in the tax and customs administration. For instance, firm owners said that enforcement on custom procedures for exports and imports with arbitrary holdups were very common. Similar situations take place with the tax administration audits on companies. Firms expressed that they would expand business and employment, and even create new firms, if these problems would not be present. Overall, these issues as seen as major constraints on business growth.

The rule of law is unstable and constrains firm expansion. Business owners complained that the rules and regulations governing businesses are complex and change continuously. Moreover, they argued that in many cases rules are difficult to understand, and often are contradictory to other regulations affecting business operations. International experience suggests that regulatory uncertainty and incoherent regulations dramatically affect decision-making by entrepreneurs and their executives with respect to business creation and expansion. In the survey of firms in Mingachevir, it became clear that the unstable legal and institutional environment was a primary reason firms decided not to hiring more personnel. This was also highlighted as an important detriment for business growth by focus groups. Moreover, lack of the rule of law is intrinsically related to the possibility for bureaucratic corruption. As firms argued, courts in the country, including the ones working on corporate law, are not independent and thus do not protect firms from the state's unfair practices.

III Policy Implications

The Government of Azerbaijan has very ambitious and far-reaching plans for social and economic development of the country. In February 2004, the President of the Republic of Azerbaijan, I. Alijev, approved the State Program for Social and Economic Development of Regions and the Republic of Azerbaijan for the period of 2004-2008. According to the Program, by 2008 GDP will increase 2.3-fold and reach AZM 76.3 trillion (per capita GDP projected to reach US$1,578); agricultural production will increase 62.5 percent, or 10-15 percent annually; 600,000 new jobs will be created, and average nominal wages will increase 3.1-fold.

These impressive targets, even if they materialize, may not ease tensions in the labor market. Although GDP is increasing rapidly, this is largely due to productivity improvements in the economy, including due to reallocation of workers into higher value-added jobs. As noted in the report, the population age structure suggests the growth of the able-bodied population may outpace the increase in employment over the period. Moreover, in recent years the number of people fired in the economy is higher than those hired, and the number of employment losses in contracting firms exceeds the number of new jobs in expanding firms. [29] Moreover, the number of workers financing the social programs by their contributions has dropped while the social demands have increased, putting pressure on the tax system. Total employment is showing some improvement largely because of an increase in informal employment, including self-employment.

The general business environment in Azerbaijan needs major improvement. The latest 2005 rankings of the Index of Economic Freedom, prepared by The Heritage Foundation and The Wall Street Journal, placed Azerbaijan 103, together with Chad, and Egypt, among the 155 countries surveyed. With the exception of Bosnia, the country has shown more improvement than any other country between 1996 and 2004; but there is still a long way to go to make the economic environment conducive to job and investment growth. [30] This year the Index indicated that the freest economies show a per capita income of US$29,219, more than twice that of the “mostly free” at US$12,839, and more than four times that of the “mostly unfree.”

The Government has taken measures recently that resulted in a significant reduction of obstacles for private sector development. The licensing regime was reviewed and improved, and the legal basis for a market economy has been introduced based on the new constitution and reforms in the legal system. The introduction of modern criminal, civil, and tax codes lighten the burden and inject objectivity into the tax regime. The

[29] It is reported that during the first year of implementation of the above named State Program, 180,000 new jobs were created, including 90,000 permanent jobs (Izvestija, February 28, 2005). However, due to a high rate of job losses, this has not have a major impact on the employment growth rate.

[30] The Index scores economic freedom in 10 categories, ranging from fiscal burdens and government regulation, property rights, inflation, competitive banking and finance laws to monetary and trade policy. Among the transition countries, Estonia was listed as the fourth freest economy in the world, Lithuania was 23, Latvia 28 and the Czech Republic 33. See The Wall Street Journal, January 4, 2005.

Government has also taken measures to address corporate governance issues, which often greatly impede private investments, and especially foreign direct investment.

EBRD/IBRD's Business Environment and Enterprise Performance Survey (BEEPS), FIAS, and PRS Group's International Country Risk Guide have all reported improvements in Azerbaijan's investment climate, albeit from a low base. On the overall Governance Index, Azerbaijan ranked 11th among the 20 transition countries surveyed (World Bank 2003). The challenge remains to increase the competitiveness of Azerbaijan's non-oil sectors in the marketplace.

Many countries around the world have and are implementing economic restructuring and recovery programs (Fretwell, 1995; Hoeven, 1997; Kikeri, 1998). Some are directly linked with privatization of state-owned enterprises (e.g., transition economies in Eastern Europe and Central Asia) while others (e.g., North America and Western Europe) are part of an ongoing process of economic change and renewal. The design and use of social support programs varies considerably between countries and is greatly influenced by the economic environment, including the level of unemployment, and the type of general social support programs already in place in the country where economic restructuring is occurring.

Mass redundancies can be mitigated, respectively, by developing labor redeployment programs (LRP) and a set of pre-layoff and post-layoff services. Labor redeployment programs, while providing income support to displaced workers, help redundant workers cope with their new status and to reintegrate into the labor market by providing information, counseling, and assisting workers to undertake self-employment, and reduce the short-term negative impact of labor restructuring on affected workers and communities. The detailed list of main labor redeployment interventions and impact evaluations of ALMPS in transition countries is given in Table (i) of the executive Summary.

The general framework for a labor redeployment program in Azerbaijan was developed in 2003 by the German firm ABU Consult. [31] The more detailed and region and enterprise-specific social plans can be developed for each of the large SOEs undergoing restructuring and/or privatization. In particular, "redundant worker action centers" (the term "social adaptation centers" was suggested by ABU Consult) can be established in each large SOE or for the region to assist in the design and delivery of the LRP.

Typically a LRP combines a range of income support programs with a variety of active labor market programs that are already developed and/or made available for individual workers prior to layoff. Most successful programs include direct dialogue between key stakeholders (e.g., the government, enterprise management, workers, and community leaders) both before and during the restructuring program.

[31] The World Bank has developed a Labor Tool Kit "Labor Issues in Infrastructure Reform," which highlights the key components and best international practices on labor redeployment policies. The ILO has also developed a comprehensive Action Program on Privatization, Restructuring and Economic Democracy for use by governments, workers' and employers' organizations and other agencies.

Partnerships are often created where there is a need to respond to problems associated with industrial transformation. Partnerships are primarily based on generating and increasing the stock and flow of social capital. It is well-documented that the "level" of social capital has significant impact on the outcomes policy-makers are concerned with i.e., economic growth, social exclusion, and personal well-being.

At the local level, local partnership groups can be established to facilitate the coordination of stakeholders and oversee implementation of the labor redeployment activities in the cities and rayons. These partnerships may include local stakeholders, such as local administration, labor market bureau, major employers, trade unions, and nongovernmental organizations involved in labor issues.

Their collective involvement may include some of the following activities:

a) identifying surplus enterprise and community assets (premises and equipment);
b) identifying and developing economic development plans and initiatives to absorb redundant workers by expanding the local economic base;
c) reviewing and recommending to authorities specific labor redeployment measures developed as part of enterprise social plans;
d) assisting in identifying local service providers; and
e) assisting in matching redundant workers to potential economic opportunities.

Governments implementing privatization programs often combined severance pay with active labor market programs to help laid-off workers reenter the labor market or become self-employed. Based on international experience, there is a general consensus that even under the best scenarios payoffs to ALMPs are modest, especially if there is a lack of demand for labor. They may work for specific groups in specific circumstances; hence, they need to be carefully targeted. In addition, programs that work for one group in one country may not work for the same group in another country. On the other hand, labor market interventions have great potential to improve labor market performance if they are well designed according to local labor market needs and are targeted to particular groups of job seekers, e.g., employment programs are most cost effective by taking into account workers' employment profiles, including age, education, and skill level (see Betcherman, Olivas and Dar 2004, and Dar and Tzannatos 1999 for overviews of ALMPs worldwide).

In Azerbaijan, public employment services (PES) and other agencies are not equipped to mitigate the impact of group redundancies, in addition to dealing with the unemployed in general. Additionally, PES normally help workers registered as unemployed. International experience suggests that if workers can be assisted while they are still attached to the workplace (during the period of notification), they are less likely to join the ranks of the unemployed; thus, the state can save on severance payments and subsequent social welfare costs.

Employment services fulfill brokerage functions, matching available jobs with job seekers. The aim of the program is to provide a broadly-based all-round job assistance and counseling service to people registered at employment services, with the aim of increasing their chances of finding jobs in the labor market.

Job search assistance and counseling have been found to be the most cost-effective labor market measures for the general population of the unemployed. That is, they achieve similar results as other interventions and at a significantly lower cost. The surveys conducted in Mingachevir clearly indicate that workers often lack information and confidence about how to look for a job. Experience from industrial countries shows that counseling can be crucial in helping individual workers obtain information about education, training, and alternative job opportunities, in making other employment services more demand-oriented, and in better targeting expenditures for other employment services. The job and vacancy survey conducted confirmed that there are vacancies available in the expanding small private firms. Other relatively inexpensive but effective employment services include job clubs, vacancy fairs, and employer contact services.

Any use of more expensive options, such as public works programs and active job creation programs, should be specifically targeted at the economically depressed areas. These programs must be limited and carefully targeted to the vulnerable because of high unit costs and considerable evidence that they have no impact, and often negative impact, on post program employment and wages. Also, small-scale public training programs work best when targeted to the specific needs of job seekers and local employers.

As the experience in Mingachevir indicates, one of the cost-effective ways to collect data on the labor market, in addition to regular data-gathering, is to conduct Employment and Job Vacancy Surveys. Such surveys can (a) improve the informational basis for local economic development, education and employment policies, and (b) prepare short-term labor market projections. The specific goal of the survey is to provide information on (a) local demand for workers, (b) employment dynamics, and (c) constraints to job creation and hiring. Also, such surveys help to identify hidden vacancies and employment movements, as employers usually do not register part or most of their available vacancies at the PES, and the job search is mainly conducted using informal contacts (e.g., relatives, friends, acquaintances, and local newspaper ads).

In fact, the results of this type of evaluation, when applied countrywide, provide an analytical framework that can be used to discuss policy alternatives to enhance labor market dynamism and promote business growth. Although conclusions for the country cannot be drawn because of the limited scope of this survey, and even less so in defining policy, results can be used to suggest policy implications.

Also the policy response to high unemployment that follows industrial restructuring is to foster the diversification of the local economy through creation of jobs outside the impacted sector and to try to improve the match between available jobs and workers' skills. In particular, local economic development planning grants can help communities develop the local economy and generate new employment by identifying and marketing regional resources and opportunities to potential investors. The objective of the Local

Economic Development Planning Studies is to help communities develop the local economy and generate new employment by identifying and marketing regional resources and opportunities to potential investors. The studies revolve around job creation, employment strategies, and targeted long-term unemployed populations to help communities experiencing high unemployment develop a systematic business growth and job creation approach to begin local economic development efforts.

These studies will help strengthen capacities of poor communities and municipalities to find local solutions including sources of funding. Typically communities that have planned their own actions for development are more likely to support those actions, and in the longer term are more likely to experience a sense of responsibility and ownership of the assets created.

A better overall approach is to focus on labor market policies that eliminate obstacles to private job creation. In reviewing international evidence on the impact on employment outcomes of different interventions, including in transition countries, generally a favorable investment climate and economic development are the key stimulants to job creation.

There exists a mismatch between labor market supply and the skill requirements of firms. The analysis revealed that vacancies are mostly in sales and service departments and that firms have difficulty filling these job openings due to lack of relevant skills. More critically, the manufacturing and service industries, which are expanding employment opportunities, are the sectors with more difficulty finding suitably prepared personnel. The difficulties arise from different sources; however, lack of adequate skills in one them: lack of skilled personnel ranks as one of the top of reasons for not hiring new personnel. This visible mismatch between labor supply and labor demand may be an important input for policy makers in shaping active labor market programs. Decisions about adjustments or complete re-tooling of training programs may benefit significantly from results of labor market demand analysis.

The business environment is essential for promoting creation of new businesses, growth of established forms, and job creation. The creation of new firms in different sectors of the economy and established firms' growth are the drivers of growth in labor demand. These developments, however, only take place where the business environment is enabling and facilitates expansion.

While the survey does indicate an increasingly dynamic business environment with more enterprise establishment, job creation and labor mobility, it still has features that aggravate business establishment and growth. These pertain in particular to the regulatory framework, governance, and access to finance:

d. **The legal and regulatory framework makes business establishment difficult**. Over 40 percent of the surveyed firms claim that it is difficult to establish a new business in Azerbaijan and 60 percent claim that it is moderately difficult. This is confirmed by international surveys that indicate that it takes an average of 123 days to register a business in Azerbaijan, compared to an average of 35 days in the EU (including new accession countries).[32] Some of the major features that current business owners indicate as deterrents to business creation are burdensome licensing procedures (although these are improving), obtaining land and construction permits, and formalization of real state transactions. As business start-ups internationally account for a large portion (from 25 to 50 percent) of new job creation, excessive obstacles to entry risk translating into lower employment growth.

e. **Weak governance creates an uncertain environment for business investment and expansion.** Survey participants raised concerns about public governance and regulatory and supervisory practice that have adverse effects on doing business: rules and regulations are unnecessarily complex and sometimes contradictory, and subject to frequent changes; the court system is perceived as being biased in favor of the State; and regulations are selectively and arbitrarily enforced by state officials.

c. Access to external financing on reasonable terms is viewed as the major constraint on business growth and increased employment. While the situation is improving, survey participants still raised stringent conditions on the financial markets as the major constraint to expansion: maturities on commercial loans are short; interest rates are rising; and other financial instruments, i.e. micro-credit and small-business financing institutions, leasing, etc., are not available. As a consequence, some 70 percent of surveyed firms do not finance their operations and investments in the financial markets, but rather from their own resources and through informal networks.

Thus, burdensome processes for establishing new formal businesses and the lack of financial products for established firms are serious obstacles for employment growth. This, together with bureaucratic corruption and unclear laws and regulations, not only discourage local entrepreneurs but also deter foreign investment. Consequently, when policy is discussed concerning how to create more jobs, these issues will need to be carefully evaluated and appropriate actions taken.

[32] Source: World Bank, Doing Business 2005

IV Conclusion

During the transition years in Azerbaijan, the previous universal and mandatory system of job security and employment stability has been replaced by a more liberal institutional framework for hiring and firing, and more flexible labor mobility. Transition reforms have led to rapid structural shifts in the economy in firm ownership, their structure by sector, occupations, or skills in demand; also, by forms of production accompanying adjustment of the economy to market needs, which have led to a strong contraction in aggregate output and structural unemployment, in particular.

In restructuring their economies, countries in transition were unable to avoid a rapid decline in aggregate demand in both government and private consumption and in fixed capital investments. This led to major labor shedding and demand-deficient unemployment.

Large industrial centers, such as Mingachevir city in Azerbaijan, have been hit especially hard by economic reforms and associated enterprise restructuring. The survey of redundant workers obtained new information and identified many issues affecting displaced workers, including how they were coping with their new status, and their efforts to reintegrate into the labor market. Although workers of large SOEs still on the payroll are formally attached to their enterprises, the survey confirmed that many of them are vulnerable to further shocks associated with enterprise downsizing, and in fact quite a significant number are already looking for alternative employment opportunities.

Industrial cities, such as Mingachevir, are much more vulnerable to economic downturns and transitional shocks than other regions. A vast majority of the unemployed in the city have become redundant because of economic reforms, mostly as a result of production stoppage, bankruptcy or liquidation, or enterprise restructuring or privatization. Only 3 percent of the unemployed left their job voluntary. The survey of workers indicates that labor hoarding in SOEs is still significant, and labor retrenchments may continue.

Survey results indicate that to hold onto their jobs, the workers themselves have "agreed' to significant real wage cuts to maintain high employment rates. Wage levels in large SOEs in Mingachevir appear to be much below the average for the country. Wage arrears are common and some groups of workers are not being paid at all. Having no prospect of being better paid in the near future workers finally quit or leave the enterprises--although many still continue working with low remuneration or even without pay.

Surveys also confirmed that violations of workers' rights are common, e.g., delays in wage payments and severance pay. Especially vulnerable are workers declared redundant many years ago and who did not have written labor contracts. They may never recover the wages or severance owed to them by their former employer, i.e., state-owned enterprises which may have no funds or be bankrupt or liquidated. It is critical to ensure that displaced workers get their entitled benefits in a timely manner, that they are not re-hired via a "back door", and that workers who have difficulty in re-entering the labor market are identified early and given targeted assistance to ensure they do not slip into poverty.

A significant portion of the able-bodied population, including some of the workers still on the active list of enterprises, no longer receive any earnings, and thus become much more dependent on social transfers from the state or private transfers from relatives. Simultaneously, as reliance on social transfers from the state grows, dependency ratios worsen. Unfortunately, surveys confirmed that state social assistance is limited, and most unemployed individuals receive no social or humanitarian assistance and do not even know where to apply for it. This signals that state-provided social safety nets are weak. Also the surveys confirm that a significant number of both the employed and unemployed population is ready to move out of town to find job opportunities. Mostly economic constraints prevent them from doing so immediately.

Lack of employment seriously affects all aspects of life in the household of the unemployed as well as in society in general. Unemployment is closely related to poverty and its effects, including deterioration of the health of the unemployed and deviances in social and demographic behavior, among others. The most devastating effects of unemployment are psychological, as social identity and status has always been attached to a person being employed, their occupation and specific job. Surveys confirmed that participation of displaced workers in active labor market programs, as a way to improve their employability, is limited. Very few unemployed have sought training or retraining.

A mix of options can be used to deal with labor restructuring. Redundancy is one but not the only option. Other measures include: voluntary separation and early retirement; freezing recruitment, enforcing retirement rules, removing barriers to employees' departure, and reducing costs of staff substitutes, such as overtime.

Surveys confirmed that a significant part of the employed in SOEs are at retirement or pre-retirement age, or would qualify for an early retirement scheme based on disability or other reasons, mostly on the basis of work conditions. So for some employees the transition from employment to retirement can be mitigated by offering an early retirement scheme for labor market reasons or by virtue of employees already being at retirement age, or meeting other conditions for early retirement proposed by existing legislation.

A higher degree of worker participation in the company can be provided by setting up consultation mechanisms aimed at soliciting the opinion of workers about issues affecting the enterprise. However, both employees and employers rated unions poorly in terms of their performance in representing the interests of workers in the restructuring process. Workers often were not informed about the enterprise restructuring and generally did not participate in the process. Displaced workers were not even informed about the grounds on which they were given severance pay.

The potential exists for enterprise restructuring to be delayed or stalled if key stakeholders are not included in the decision. Social partners appear to need help in defining the role they could play during and after the period of economic reforms. There also appears to be a need to facilitate the interaction of social partnerships at all levels.

An enabling business environment is necessary for enterprise creation and growth, and consequently is essential for successful labor redeployment. The creation of new businesses and firm expansion are the drivers of labor demand growth. Concurrently, labor demand growth is essential for labor redeployment, particularly when enterprise restructuring and privatization take place. However, that expansion only occurs where the business environment supports and otherwise enables business operations. Some of the concerns of the firms in Mingachevir, as well as other industrial cities--including burdensome processes for establishing new formal businesses, an unstable rule of law, and bureaucratic corruption--not only discourage local entrepreneurs but also deter foreign investment. Consequently, discussion of labor redeployment programs also involves analyzing constraints that exist for business creation and growth, and accordingly establish policies oriented to surmount those obstacles.

Training programs need to be tailored to match firms' needs in terms of labor skills. The study finds that vacancies are mostly in sales and services; moreover, firms have difficulty filling out these job openings due to lack of relevant skills. Critically, the manufacturing and service industries, which are expanding sectors in employment, are the very ones with more difficulty finding appropriately trained personnel. The difficulties arise from different circumstances, but in general lack of skilled personnel ranks as one of the major reasons for not hiring new personnel. This visible mismatch between labor supply and demand is an important signal for labor market policy-makers. It is clear that labor redeployment would benefit significantly from a good fit between training programs and labor demand requirements. Thus, adjustments or complete retooling of these programs should be based on constant monitoring of what labor skills firms require.

A policy geared to promote small and medium enterprises is key job for creation. It was found that most of the new jobs were created by small and medium enterprises; in fact, 9 out of 10 jobs were created by firms with less than 30 employees. Additionally, small business creation could be a way out from unemployment for job seekers. Thus, this situation should stimulate a policy discussion about constraints on the business environment and the regulations currently in place for small businesses. Fostering the growth of small business through improvements in business environment and lowering the costs of doing business may prove to be critical for job creation and labor redeployment.

Younger firms are not creating employment, which also points to a constraint in the business environment. The survey revealed that firms established after year 2000 were not contributing to job creation as much as older firms. In fact, employment growth was negative in younger firms last year. This struggle to grow should also send a signal to policy-makers working in the business environment of the country. The constraint cited as the most important for growth was the lack of access to financial resources on favorable terms. This obstacle may be affecting younger firms more severely as they have yet to establish a "name" in the market. Thus, the struggle to grow should also form a part of the policy discussion relative to the country's business environment.

The development of the microfinance sector is fundamental for business creation, firms' growth, and labor redeployment. One of the issues that surfaces strongly in the surveys and focus groups is the lack of access to financial resources that firms confront. This situation seems to be even more acute for newer firms that are struggling to grow, as they cannot acquire resources for expansion because of the terms available in the financial system. This situation also affects the establishment of new small firms and the growth of SMEs in general. The development of the microfinance sector has proven to be strategic for firm expansion and job creation in many developing countries, particularly in Latin America. A policy option for the government would be to provide better support to this sector, which remains underdeveloped in Azerbaijan.

To summarize, findings indicate labor market interventions have great potential to improve labor market performance; however, whether or not this potential is realized depends on a number of factors, and numerous variables can intervene to affect the final outcome of their implementation. These include external factors such as stable macroeconomic conditions, a favorable investment climate with an enabling business environment, and a competitive product market. In addition, there are important internal factors: specifically, policy design and implementation. A significant share of the able-bodied population needs better employment opportunities, and state support is necessary to enhance workers' competitiveness in the labor market and assist job-seekers in their employment search.

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ANNEX I

Table 1. Economically active population of age 15 years old and older, and at able-bodied age (males 15-61, females 15-56) in 2003, %

	Population of age 15 years old and older			Able-bodied age (males 15-61; females 15-56)		
	Economically active	Employment rate	Unemployment rate	Economically active	Employment rate	Unemployment rate
			Urban and rural areas			
Total	62.9	56.2	10.7	71.4	63.6	10.9
Males	75.6	68.4	9.6	83.6	75.4	8.9
Females	51.1	44.9	12.2	59.5	52.1	12.5
			Urban areas			
Total	58.8	50.5	14.0	66.8	57.2	14.3
Males	72.8	64.1	12.0	80.6	70.8	12.2
Females	46.3	38.4	16.9	53.8	44.2	17.3
			Rural areas			
Total	68.2	63.5	7.0	77.5	72.0	7.1
Males	79.2	73.7	7.0	87.4	81.2	7.1
Females	57.6	53.5	7.0	67.4	62.5	7.2

Source: State Statistical Committee of Azerbaijan Republic (2004).

Table 2. Basic social and economic indicators of the labor market in Azerbaijan (1993-2002), 1000'

	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002
Population	7494,8	7596,6	7684,9	7763,0	7838,3	7913,0	7982,8	8048,6	8111,2	8172
Labor resources	4135,3	4161,2	4227,8	4278,6	4336,0	4437,8	4566,7	4685,8	4890,5	4896.2
Employed	3714,6	3631,3	3631,0	3686,7	3694,1	3701,5	3702,8	3704,5	3715,0	3726.5
Of which by forms of ownership:										
State sector	2303,0	2190,5	2027,2	1879,9	1717,7	1710,2	1342,0	1278,2	1240,0	1192,0
Private sector	1411,6	1440,8	1585,8	1806,8	1976,4	1991,3	2360,8	2426,3	2475,0	2534,5
Registered unemployed (individuals)	19474	23592	28314	31935	38306	42329	45211	43739	48446	50963

Source: State Statistical Committee of Azerbaijan Republic – www.azstat.org,

Table 3. Azerbaijan: Macroeconomic Indicators

	2001	2002	2003
GDP, % of increase	9.9	10.2	11.2
Volume of industry production, % of increase	5.1	3.6	6.1

Volume of agriculture production, % of increase	11.1	6.4	5.6
Population money income, % of increase	10.4	11.4	11.4
Nominal average monthly wage (1000' manat)	260	312.9	383.1
Wage increase, compared with the same period of previous year	26.7	21.2	21.4
CPI, %, December to December	101.3	103.3	103.6

Source: National Bank of Azerbaijan (www.nba.az).

Table 4. Hiring and firing indicators in CIS-7 countries and in some other countries*

	Difficulty of hiring index	Difficulty of firing index	Rigidity of employment index	Rigidity of hours index	Firing costs (weeks)
Armenia	17	50	36	40	17
Azerbaijan	33	40	38	40	30****
Georgia	78	40	66	80	133
Kyrgyzstan	33	40	38	40	21
Moldova	33	70	54	60	21
Tajikistan	…	…	…		
Uzbekistan	33	100	58	40	28
Average for 10 EU Accession Countries**	33	52	32	39	38
EU14***	36	63	34	44	50

* - Flexibility-of-Employment indexes varying between 0 and 100, with higher values for more rigid regulation, measure various aspects of labor regulation
** – Bulgaria, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania, Slovakia, Slovenia
*** - EU15 except Luxembourg
**** - Notification period and maximum duration of severance payments

Source: World Bank (2004). Doing Business 2005. Washington, DC.

Table 5: Employment growth by industrial sector

	Manufacturing	Services	Wholesale and retail trade
% firms in which employment grew during the past year	41	33	26

% of firms in which employment is expected to grow during the next 6 moths	35	34	30

Table 6: Employment growth by firm's type of ownership

	Private	Mix public-private
% firms in which employment grew during the past year	31	26
% of firms in which employment is expected to grow during the next 6 moths	38	21

Table 7: Job creation and job destruction occurred in firms by industrial sector

	Manufacturing	Services	Wholesale and retail trade	Other
Portion of job creation contributed during the last year (by industrial sector), %	30	35	30	5
Portion of job destruction contributed during the last year (by industrial sector), %	25	23	46	6
Portion of job creation expected to be contributed during the next 6 moths (by industrial sector), %	40	24	33	3
Portion of job destruction expected to be contributed during the next 6 moths (by industrial sector), %	43	14	43	0

Table 8: Job creation and job destruction occurred in firms by firm's size (size in terms of number of employees)

	Firms with less than 10 employees	Firms with 10-30 employees	Firms with more than 30 employees

Portion of job creation contributed during the last year, %	37	57	6
Portion of job destruction contributed during the last year, %	67	20	13
Portion of job creation expected to be contributed during the next 6 moths, %	57	26	17
Portion of job destruction expected to be contributed during the next 6 moths, %	100	0	0

Table 9: Job creation and job destruction occurred in firms by type of firm's ownership

	Private	Mix public-private
Portion of job creation contributed during the last year	87%	13%
Portion of job destruction contributed during the last year	79%	21%
Portion of job creation expected to be contributed during the next 6 moths	84%	16%
Portion of job destruction expected to be contributed during the next 6 moths	100%	0%

Table 10: Job creation and job destruction occurred in firms by firm's year of establishment

	Firms Established Before 2000	Firms Established After 2000
Portion of job creation contributed during the last year, %	87	13
Portion of job creation contributed during the last year, %	79	21
Portion of job creation expected to be contributed during the next 6 months, %	84	16
Portion of job destruction expected to be contributed during the next 6 months, %	100	0

Table 11: Growth in firms' employment according to their past experience and expectations about sales growth, %

	Firms in which sales increased compared to last year's	Firms in which sales decreased compared to last year's	Firms in which sales remained at the same level of last year's	Firms in which sales will increase during the next 6 months	Firms in which sales will decrease during the next 6 months	Firms in which sales will remain the same during the next 6 months	Firm that Don't know if any change in sales will occur
Growth in firm's employment	13	-5	2	29	2	-2	4

Table 12: Degree of difficulty in filling out vacancies for firms by industrial sector, %

	Manufacturing	**Wholesale and retail trade**	**Services**
It is easy to fill a vacancy	59	82	67
It is moderately difficult to fill a vacancy	14	12	20
It is difficult to fill out a vacancy	27	6	13

Table 13: Degree of difficulty in filling out vacancies for firms by firms' size (size in term of number of employees), %

	Firms with less than 10 employees	**Firms with 1-30 employees**	**Firms with more than 30 employees**
It is easy to fill a vacancy	78	46	60
It is moderately difficult to fill a vacancy	13	23	20
It is difficult to fill out a vacancy	9	31	20
TOTAL	**100**	**100**	**100**

Table 14. Real growth rate of industrial production

Production growth rates	*1997*	*1998*	*1999*	*2000*	*2001*	*2002*
Total industry	**0.5**	**2.2**	**4.2**	**6.9**	**5.1**	**4.4**
Energy	-1.6	7.0	5.3	1.8	3.0	3.6
o/w oil and gas	0.2	7.5	7	5.2	5.9	4.1
Metallurgy	364	-54.6	61.3	150	41.7	51.7
Machine building	0.7	-30.4	-55.7	95.8	5.4	-25.1
Chemical and petro-chemical	-28.2	-11.4	8.9	23.2	-8	-78.6
Construction materials	4.4	-22.2	-21.6	19.7	11.1	205.0
Textiles	-13.8	-44.2	-34.6	22.5	-11.6	16.0
Agroprocessing 1/	6.6	-2.7	3.9	2.2	11.1	6.4
Agriculture	6.1	6.2	7	12.1	11.1	6.4

1/ Available data on Agroprocessing indicate a similarity to Agricultural output growth rate
Although questionable, there is no better alternative estimation of Agroprocessing growth
Source: State Statistics Committee, IMF Staff Estimates; World Bank 2003, Vol. II.