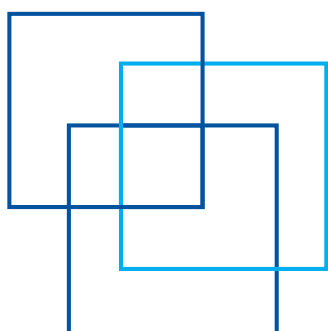




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Youth Labour Markets in Bosnia and Herzegovina

Niall O'Higgins

2009/2

ILO Subregional
Office for Central
and Eastern
Europe

EMPLOYMENT POLICY PAPERS

**Youth Labour Markets in
Bosnia and Herzegovina**

Niall O'Higgins

Employment Programme
Subregional Office for Central and Eastern Europe

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Youth Labour Markets in Bosnia and Herzegovina

Niall O'Higgins

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PREFACE

Across the globe, young women and men are making an important contribution as productive workers, entrepreneurs, consumers, citizens, members of civil society and agents of change. All too often, the full potential of young people is not realized because they have no access to productive and decent jobs. Although they are an asset in every country, many young people face high levels of economic and social uncertainty. A difficult transition into the world of work has long-lasting consequences not only on youth but also on their families and communities.

The International Labour Office (ILO) has long been active in youth employment, through its normative action and technical assistance to member States. One of the means of action of the Youth Employment Programme of the ILO aims to expand the knowledge base on the youth employment challenge across countries and regions.

The working paper *Youth Labour Markets in Bosnia and Herzegovina* was drafted by Mr Niall O'Higgins, Professor of Economics at the University of Salerno (Italy) and former employment specialist of the ILO. It is part of a research programme that is coordinated by Gianni Rosas of the Subregional Office for Central and Eastern Europe of the ILO. This programme seeks to increase knowledge of the quantitative and qualitative aspects that determine the labour market outcomes of young people in South-Eastern Europe with a view to supporting countries devise coherent and coordinated youth employment interventions at national and regional levels.

The empirical research that is presented in this paper was carried out in preparation for the Subregional Tripartite Meeting of Experts on Decent Employment of Young People, jointly organized by the ILO and the Ministry of Labour, Family and Social Affairs of Slovenia (Ljubljana, December 2007).¹ In this meeting, the experts from the Western Balkan countries and Slovenia shared national practice and experience. They also identified priority areas for future regional and national action by governments and employers' and workers' organizations. The last two chapters of the working paper were finalized by the Employment Programme of the ILO for Central and Eastern Europe on the basis of the inputs provided by the tripartite delegations of experts at the above-mentioned meeting and the review of employment policy of Bosnia and Herzegovina that was conducted by the ILO and the Council of Europe between 2007 and 2008.

Mark Levin,

Director,

ILO Subregional Office for Central and Eastern Europe.

¹ The Conclusions of the Tripartite Meeting are available from the following web site:
http://www.ilo.org/public/english/region/eurpro/budapest/download/empl/ljubljana_conclusions.pdf

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I would like to express my gratitude to everyone involved in the finalization of this paper. Thanks go especially to the Directors and the staff of the Statistical Offices of Bosnia and Herzegovina for their availability in sharing statistical data on the labour market.

A special acknowledgment goes to the colleagues who provided comments and feedback on the draft of the paper, Ms Valli Corbanese and Mr Gianni Rosas of the ILO Subregional Office for Central and Eastern Europe and Mr Diego Rei of the Youth Employment Programme at ILO Geneva.

Appreciation is expressed to the members of the tripartite delegation that participated in the Tripartite Meeting on Decent Employment for Young People (Ljubljana, Slovenia, December 2007). They provided invaluable guidance on the finalization of the paper.

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TABLE OF CONTENTS

Preface	iii
Acknowledgments	v
Acronyms	ix
CHAPTER 1. OVERVIEW OF THE ECONOMIC AND SOCIAL CONTEXT	1
1.1 Macroeconomic overview	1
1.2 Poverty and social exclusion	5
1.3 Labour market dynamics	7
CHAPTER 2. ANALYSIS OF THE YOUTH LABOUR MARKET	13
2.1 Socio-demographic characteristics of young people	13
2.1.1 Demographic trends	13
2.1.2 Trends in education	15
2.2 Youth labour force participation	17
2.3 Youth employment	18
2.4 Wages and working conditions of young workers	21
2.5 Youth unemployment and joblessness	23
CHAPTER 3. POLICIES TO PROMOTE YOUTH EMPLOYMENT	31
3.1 Macroeconomic Policy	31
3.2 Education and training	32
3.3 Labour market policies and institutions	36
3.3.1 Employment protection legislation	36
3.3.2 Minimum wages	38
3.3.3 Payroll taxes and contributions	39
3.3.4 Active labour market policies	41
3.3.5 Passive labour market policies	43
CHAPTER 4. KEY ISSUES AND IMPLICATIONS	45
REFERENCES	48

List of figures

- Figure 1.1 Output by economic sector in Bosnia and Herzegovina, 2005
- Figure 1.2 Formal employment by economic sector, 1991 - 2006
- Figure 1.3 Output and employment, 1999-2006
- Figure 1.4 Employment rates by broad economic sector, 2006
- Figure 1.5 Formal and informal employment by economic sector
- Figure 1.6 Nominal net monthly wages in Bosnia and Herzegovina and Entities, 1998-2006
- Figure 2.1 Youth population in Bosnia and Herzegovina and South Eastern Europe, 1980-2020
- Figure 2.2 Dependency ratio in South East Europe, 1989-2006
- Figure 2.3 Ratio of youth to adult unemployment rates in selected transition countries
- Figure 2.4 Youth jobless rates by standardized level of education in South-Eastern Europe
- Figure 2.5 Disaggregation of the jobless by degree of labour market attachment
- Figure 2.6 Principal methods of job search used by the unemployed

List of tables

- Table 1.1 Main economic indicators Bosnia and Herzegovina, 2000-2006
- Table 1.2 Poverty rates in Bosnia and Herzegovina, 2001-2004
- Table 1.3 Labour force participation for Bosnia and Herzegovina and neighbouring countries
- Table 1.4 Employment rates in Bosnia and Herzegovina and neighbouring countries
- Table 1.5 Informal employment as a percentage of all employment
- Table 1.6 Average net wages for SEE countries in euros
- Table 2.1 Educational participation rate Bosnia and Herzegovina 2006
- Table 2.2 Educational attainment, Bosnia and Herzegovina 2006 and comparable countries
- Table 2.3 Labour Force Participation rates in Bosnia and Herzegovina by age, sex and Entity, 2006
- Table 2.4 Employment by age-group, economic sector and form of ownership, 2006
- Table 2.5 Incidence of informal employment by age, sex and industrial sector
- Table 2.6 Incidence of informal employment amongst young people by education level
- Table 2.7 Mobility between labour market statuses, 2001-2004
- Table 2.8 Temporary, part-time work and hours of work
- Table 2.9 Youth and adult wages in Bosnia and Herzegovina (KM per month)
- Table 2.10 Youth and adult wages – formal versus informal employment
- Table 2.11 Youth unemployment and jobless indicators, Bosnia and Herzegovina 2006
- Table 2.12 Incidence of long-term unemployment by age and sex
- Table 2.13 Incidence of long-term unemployment among young people in Bosnia and Herzegovina by education level
- Table 3.1 EPL indices for Bosnia and Herzegovina and neighbouring countries

List of boxes

- Box 1 Bosnia and Herzegovina's education system at a glance, 2004 – 2005

Acronyms

ALMPs	Active Labour Market Policies
BiH	Bosnia and Herzegovina
CEE	Central and Eastern Europe
DB	District of Brčko
EPL	Employment Protection Legislation
EPPU	Economic Policy and Planning Unit of the Council of Ministers of BiH
EC	European Commission
EU	European Union
EU15	Member States of the European Union before May 1 st , 2004
EU25	Member States of the European Union between May 1 st , 2004 and January 1 st , 2007
EU27	Member States of the European Union after January 2007
EU-NMS	New Member States comprising Cyprus, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Slovakia and Slovenia.
FBiH	Federation of Bosnia and Herzegovina
FDI	Foreign Direct Investment
GDP	Gross Domestic Product
KM	Convertible Marks
IDP	Internally Displaced Person
ILO	International Labour Organization
IMF	International Monetary Fund
LFS	Labour Force Survey(s)
LSMS	Living Standards Measurement Survey(s)
OECD	Organisation for Economic Cooperation and Development
PES	Public Employment Service
RS	Republika Srpska
SEE	South-Eastern Europe comprising Albania, Bosnia and Herzegovina, Croatia, the FYR of Macedonia, Montenegro and Serbia
UNDP	United Nations Development Programme
VAT	Value Added Tax

CHAPTER 1.

OVERVIEW OF THE ECONOMIC AND SOCIAL CONTEXT

It is now firmly established that what happens in the youth labour market depends on what occurs in the economy as a whole.² In particular, youth unemployment rates are closely related to aggregate labour demand and it is often argued that labour market regulations such as labour taxes, minimum wages and employment protection legislation are likely to disproportionately affect the labour market prospects of young people. It is therefore essential that any analysis of the youth labour market be prefaced by a discussion of what is happening at the aggregate level, this section of the paper aims to do that by reviewing the general economic and employment situation in Bosnia and Herzegovina.

1.1 Macroeconomic overview

The first and most important aspect that must be mentioned is that the macroeconomic environment of Bosnia and Herzegovina is still adversely affected by the conflict of 1992-95. Although real economic growth beginning in 2000 has remained strong and stable, the level is not comparable to the growth rates experienced in the direct aftermath of the conflict, which were fuelled by the massive arrival of international aid. Gross Domestic Product (GDP) per capita also seems to be on the increase, although comparisons across time are problematic given the lack of reliable data on the total population.³

Inflation has remained low since 2000, with increases in 2005 and a marked surge in 2006 due to the introduction of the value-added tax (VAT). Government expenditure as a percentage of GDP is relatively high compared to other countries in South-Eastern Europe (SEE); however it has fallen significantly beginning in 2000, while from 2003 the government budget has been in surplus. Sustained growth, together with the improvement of public finances, reduced the country's external debt from nearly two-fifths of GDP in 2000 to a little over one fifth in 2006 (Table 1.1).⁴

External imbalances remain the most serious challenge facing the country and the negative balance of payments reported in Table 1.1 is largely the result of a significantly negative trade balance. Trade liberalization (along with an exchange rate pegged to the euro) meant a rapid increase in imports – mainly consumption goods – whilst exports have largely remained in low value-added products (raw materials, ag-

² There are many studies that confirm this. For a recent discussion, see *World Development Report 2006: Development and the next generation* (World Bank, Washington, DC, 2006).

³ There has been no population census since 1991. The war and its aftermath caused fairly massive population movements creating problems for any population-based figures (such as GDP per capita). Various population estimates are in use. The official estimate for 2006 was 3,843,000 persons. The State Statistical Agency used an estimate of 3,372,000 people for the 2006 Labour Force Survey, whilst the US Census Bureau (used for population data in the Transmonee 2007 database) uses the figure of 4,461,000 people. There is also disagreement over whether/when the GDP per capita level overtook its pre-war level. The European Training Foundation (ETF) reports GDP per capita at 1,600 in 2003 or “half the pre-war levels”, European Training Foundation (ETF), *Labour Market Review of Bosnia and Herzegovina* (ETF, Turin, 2006). The BiH State Agency for Employment reports the overtaking of pre-war GDP per capita levels (US\$ 2,000 in 1990) by 2004. In this case the apparent discrepancy is explained largely by the use of base currency. Bosnia and Herzegovina State Agency for Employment, *State Review of Employment Policies in Bosnia and Herzegovina for 2006* (BiH State Agency for Employment, Sarajevo, 2007).

⁴ There are some discrepancies among figures. Table 1.1 reports the Central Bank's figures, whilst the International Monetary Fund (IMF) estimates suggest that the reduction in government expenditure is much more modest. Economic Policy and Planning Unit (EPPU): *Economic Trends, Annual Report 2006* (EPPU, Sarajevo, 2007).

gricultural products and energy). There have been significant improvements recently, with the negative trade balance falling from over 50 per cent of GDP in 2003 to less than 40 per cent in 2006, while in the same year, imports originated mainly from Croatia (16.7 per cent), Germany (12.3 per cent), Serbia and Montenegro (9.7 per cent) and Italy (8.9 per cent). This growth in exports (+29 per cent) combined with productivity gains and increases in export prices, contributed to a real GDP growth of over 6 per cent. In the first four months of 2007, exports continued to increase (+24 per cent) albeit at a slower pace compared to 2006. The end result is that the current account deficit, as a percentage of GDP, was halved between 2005 and 2006 (from 21.3 per cent to 11.4 per cent).⁵

Table 1.1: Main economic indicators for Bosnia and Herzegovina, 2000-2006

	2000	2001	2002	2003	2004	2005	2006 (est.)	2007 (proj.) †
Nominal GDP [Convertible Marks (KM)]	10,713	11,599	12,829	13,443	14,678	15,791	17,750†	19,740
Real GDP growth rate	5.5	4.5	5.5	3.0	6.0	5.5	6.2	6.0
Gross investment (% of GDP)†				20.4	19.4	22.0	16.2	19.8
Industrial production† (% growth rate)				3.0	13.6	11.0	10.4	6.0
Inflation rate	4.8	3.1	0.4	0.6	0.4	3.8	7.4	-
Nominal GDP per capita (KM)	2,833	3,054	3,351	3,508	3,819	4,108	4,671	-
Government surplus/deficit (% GDP)	-6.5	-3.3	-0.1	0.8	1.7	2.6	3.0†	-1.4
External debt (% GDP)	37.9	38.1	33.4	29.9	27.5	27.5	22.6	20.5
Govt expenditure (% GDP)	56.9	50.2	40.1	44.0	41.7	41.5	-	-
Balance of payments (% GDP)	-7.8	-14.1	-19.1	-20.9	-19.2	-21.3	-11.4	-13.4
- trade balance	-54.8	-55.8	-53.7	-53.4	-49.0	-49.6	-37.1	-
FDI (% GDP)			4.3	4.9	7.1	5.2	3.7	11.5

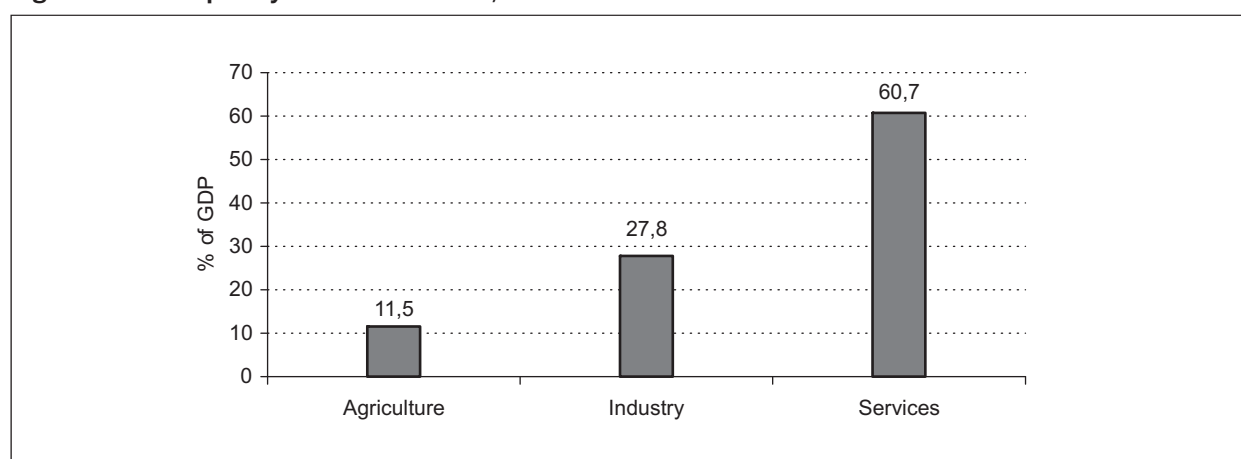
Source: Central Bank of Bosnia and Herzegovina: *Annual Report 2006* (Sarajevo, 2007); where indicated by †, International Monetary Fund (IMF), *Bosnia and Herzegovina: 2007 Article IV Consultation* (Washington, DC, 2007).

⁵ International Monetary Fund (IMF): *Bosnia and Herzegovina: Selected issues*, IMF Country Report No. 07/269 (Washington DC, 2007).

Figure 1.1 shows GDP by broad economic sectors: the service sector now accounts for more than 60 per cent of GDP, while the sub-sectors contributing most to observed economic growth in 2005 and 2006 were wholesale, retail and real estate, while manufacturing, electricity, gas and banking also made significant contributions; all these sub-sectors together accounted for 54 per cent of growth in 2006. Other data sources suggest that the tourism and construction sectors are also growing, however, their contribution to registered economic activity is not significant, as the two sectors are the ones most subject to informality and their contribution is not recorded in official statistics.

Several attempts have been made to estimate the size of the informal economy in Bosnia and Herzegovina, for example, research conducted in 2003 reveals that the overall Non-Observed Economy (NOE) in BiH was as high as 53 per cent of GDP, whilst the informal economy – defined as the share of GDP hidden for economic purposes – comprised 33 per cent of national output.⁶

Figure 1.1.: Output by economic sector, 2005



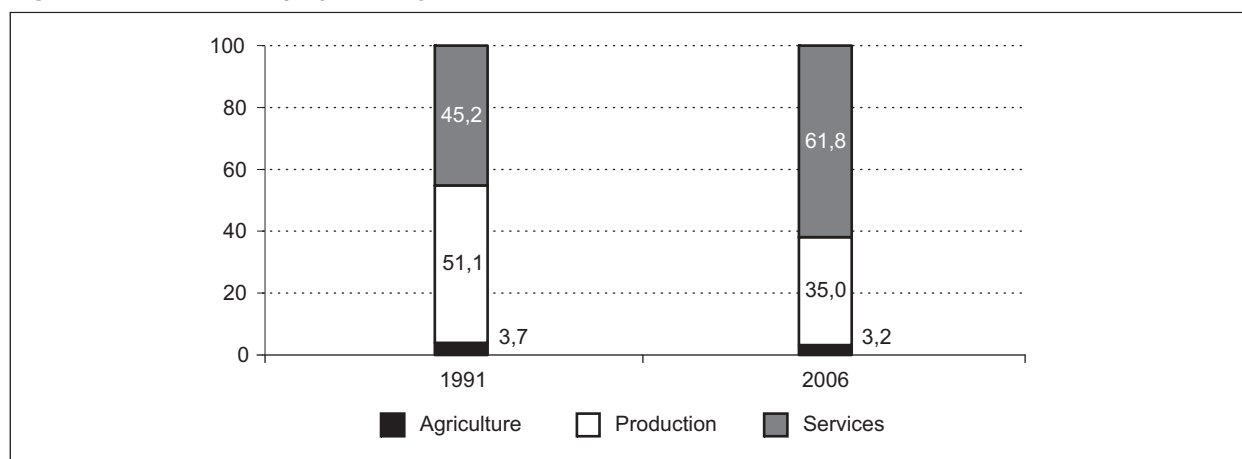
Source: World Bank: *Bosnia and Herzegovina: Addressing Fiscal Challenges and Enhancing Growth Prospects* (Washington, DC, 2006).

The data on registered employment by economic sectors in 1991 and 2006 reflect, *inter alia*, the size of the informal economy (Figure 1.1); for instance, the comparison of Figures 1.1 and 1.2 shows that the low level of registered employment in agriculture is due to the informal employment of workers in this sector: the agricultural sector's contribution to Bosnia's and Herzegovina's GDP is well over 10 per cent, however, employment in agriculture accounts for less than 4 per cent of *registered* employment. As labour productivity in agriculture is generally lower than in industry and services, one would expect that the percentage of workers employed in agriculture be larger than the percentage of GDP produced by the agricultural sector. However, official data shows the exact opposite: employment in agriculture is - in percentage terms- less than half of agriculture's contribution to GDP; the explanation for such inconsistency is to be found in the extent of informal employment in agriculture.

⁶ The Non-Observed Economy includes areas of activity not usually included in the informal economy as conventionally measured – illegal activities as well as activities which are unobserved for statistical - as opposed to - economic reasons. R. Dell'Anno and M. Piirisild: *Estimate of Non-Observed Economy in Bosnia and Herzegovina* (USAID, Sarajevo, 2004).

Figure 1.2 illustrates the substantial shift from employment in industrial production to the service sector, which has been the characteristic of the post-war period: industrial enterprises, previously state-owned, have since been privatized and have re-activated their production, although many remain at very low levels of production or are not functioning at all, while in the service sector the fastest growing areas have been banking and retail and wholesale trade, both supported by Foreign Direct Investment (FDI).

Figure 1.2: Formal employment by economic sector, 1991 and 2006



Source: State Agency for Employment of Bosnia and Herzegovina: *State Review of Employment Policies in Bosnia and Herzegovina for 2006* (Sarajevo, 2007).

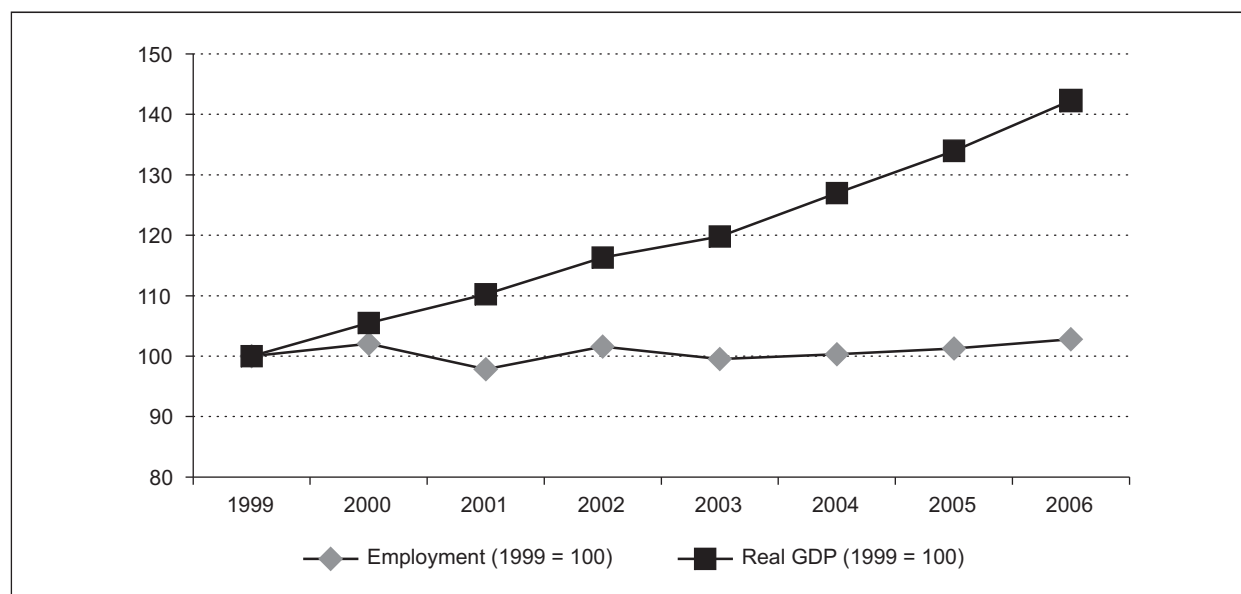
From 1994 to 2006 foreign investments were largely from countries of the European Union (58.1 per cent) and South-Eastern Europe (22.6 per cent), Croatia and Austria being the largest contributors, accounting for 15.9 per cent and 15.4 per cent of FDI respectively.

Persistent and continuing high levels of economic growth have produced improvements in productivity, but have not yet led to employment growth, at least in the formal economy (Figure 1.4); only beginning in 2003 there has been a sustained, albeit modest, growth in formal employment. This modest increase, when compared to the increase in economic growth, is a fairly common feature of the early phases of transition throughout the region.⁷ However – given the delayed introduction of a market economy due to the upheaval of the conflicts – it is not unreasonable to expect that formal employment growth will soon follow, particularly if the current attempts to encourage formalization of economic activities are further expanded.⁸

⁷ Since the employment figures are based on registered employment data, they ignore developments in the informal economy. The Living Standards Measurement Survey (LSMS) data, show a strong employment growth between 2001 and 2004 in the informal economy. However, caution should be exercised in the interpretation of these estimates, World Bank: *Bosnia and Herzegovina Labour Market Update: The Role of Industrial Relations* (Washington, DC, 2005).

⁸ An example is the introduction of a flat VAT rate in 2006. This encourages formalization because it facilitates tax controls and, above all, internalizes enforcement. In order to reduce their own VAT bill, firms and the self-employed require VAT receipts from their suppliers.

Figure 1.3: Output and employment in Bosnia and Herzegovina, 1999-2006 (1999=100)



Source: Author's calculations on the basis of data of the Central Bank of Bosnia and Herzegovina: *Annual Report 2006* (Sarajevo, 2007) and State Agency for Employment: *State Review of Employment Policies in Bosnia and Herzegovina for 2006* (BiH State Agency for Employment, Sarajevo, 2007).

Note: The output index is calculated from real GDP growth rates and the employment index is based on registered employment data.

1.2 Poverty and social exclusion

The most recent estimates of poverty in Bosnia and Herzegovina are based on the Living Standard Measurement Survey (LSMS) and refer to 2004; although the data suffer from sample and representativeness constraints, this survey has the major advantage of having systematically collected data every year from 2001 to 2004.⁹ According to these figures, the poverty rate has fallen from 19.5 per cent in 2001 to 17.8 per cent in 2004 (Table 1.5).¹⁰

Table 1.2: Poverty rates in Bosnia and Herzegovina, 2001-2004

	Poverty rate		% change
	2001	2004	2001-2004
BiH	19.5	17.8	-8.7
- <i>FBiH</i>	16.3	15.4	-5.5
- <i>RS</i>	24.8	20.8	-16.1

Source: Economic Policy and Planning Unit (EPPU): *Medium-Term Development Strategy BiH 2004-2007 (PRSP)*, Revised Document, (Sarajevo, May 2006).

Although poverty has indeed fallen, certain groups are more at risk than others: households with two, three or more children (66 per cent); refugees and displaced persons (37 per cent); the elderly (31 per cent); the unemployed (29 per cent) and people with only primary education or living in a household whose

⁹ The LSMS is a panel study that allows the analysis of individuals' experiences over a four year period. The sample size in 2004 was a little over 6,500 households or in the region of 1.5 per cent to 2 per cent of the population, depending on which of the population estimates was utilised.

¹⁰ There are many ways to measure poverty: Table 1.2 is based on absolute poverty measured by the cost of an essential consumption bundle. For the purpose of international comparisons, indicators either use a fixed poverty line (US\$4.30 and US\$2.15 are the World Bank's definitions of poverty and extreme poverty) or relative poverty indices (UNDP's definition of "at risk" of poverty is 60 per cent of national median incomes).

head has only primary education (24 per cent and 25 per cent respectively).¹¹ The Roma population in Bosnia and Herzegovina is far more likely to be living in poverty than members of the majority, as is the case in other countries of the region. A recent report on internally displaced persons (IDPs) and the Roma population in South-Eastern Europe, found that the unemployment rates of the Roma population were over 70 per cent higher than that of other groups; moreover, Roma individuals were around nine times more likely to be living in poverty than individuals of the majority (i.e. with less than US\$4.30 a day).¹² ¹³ The conclusion is that although the Roma are doing better in BiH than in other countries of the region (Croatia being the only country with a lower poverty rate for Roma), in terms of the relative position of Roma *vis-à-vis* the majority population, BiH is ranked almost last in the region (Bulgaria being the only country with an even larger gap).

For young people, the report found that although Roma as a whole are much more likely to be unemployed than their majority peers, the relative disadvantage of youth *vis-à-vis* adults is somewhat less among the Roma. In other words, although it is true that young Roma are much more likely to be living in poverty than their majority peers, the gap is less than the difference found between adults. This is a reflection of the extremely disadvantaged situation of the Roma population as a whole: the employment and income position of the Roma population is so poor *in general* that it is difficult for the relative situation of Roma *youth* to be worse.

The *Medium Term Development Strategy* was adopted in 2004 and it set a 20 per cent poverty reduction target to be achieved by 2007. Although there is no reliable data yet available, the reduction in the poverty rate achieved from 2001 to 2004 was insufficient for the goal to have been met; in other words, the growth rates sustained were not large enough for the reduction target to have been achieved. This conclusion led the Economic Policy and Planning Unit (EPPU) to suggest that policies need to be drawn up and implemented in order to ensure a greater participation of the poor in the benefits of economic growth.¹⁴

Notwithstanding the fact that the analysis of poverty rates in the region is hampered by a lack of comparable data, the World Bank reports that in 2001 the incidences of poverty – relative poverty indices at 50 per cent and 66 per cent of median incomes – were 6.9 per cent and 16.7 per cent, respectively.¹⁵ The data suggest that poverty in BiH is higher than in Croatia, roughly the same as in Romania and Albania, and lower than in Bulgaria; while another poverty and inequality report puts BiH at the low end of the scale in South-Eastern Europe.¹⁶ On the other hand, the absolute poverty indices show that the incidence of poverty and extreme poverty in BiH are below those found in Albania, Bulgaria, the FYR of Macedonia, Romania as

¹¹ United Nations Development Programme (UNDP): *Social Inclusion in Bosnia and Herzegovina, NHDR 2007* (Sarajevo, 2007).

¹² United Nations Development Programme (UNDP): *At Risk: Roma and the Displaced in Southeast Europe: Dimensions of Vulnerability* (Bratislava, 2007). The UNDP study was based on surveys carried out in seven countries of the region among Roma, IDPs and majority populations living in close proximity – i.e. in the same or nearby communities (including separate studies for Kosovo, Montenegro and Serbia). This was done to facilitate comparisons between the two groups, but it also means that the surveys were not nationally representative and nor were they intended to be.

¹³ Approximately 27 per cent of Roma and 3 per cent of the majority were living in households with adult expenditures of less than US\$4.30 a day (or equivalent in local currency). The corresponding percentages for adult income are 26 per cent and 2 per cent, however, given the unreliability of self-reported income, the expenditure based figures probably provide a more accurate picture. See United Nations Development Programme (UNDP): *At Risk: Roma and the Displaced in Southeast Europe: Dimensions of Vulnerability*, (Bratislava, 2006), op.cit.

¹⁴ Economic Policy and Planning Unit (EPPU): *Medium-Term Development Strategy for BiH 2004-2007 (PRSP)*, (EPPU, Sarajevo, 2006) op.cit.

¹⁵ World Bank: *Bosnia and Herzegovina poverty assessment*, Vol. I (Washington, DC, 2003).

¹⁶ A. Asad et al.: *Growth, Poverty, and Inequality: Eastern Europe and the Former Soviet Union*, (World Bank, Washington, DC, 2005).

well as Serbia and Montenegro. Bosnia and Herzegovina also appears to be doing reasonably well in terms of inequality; the World Bank poverty assessment suggests that, using consumption based estimates, there is less inequality in Bosnia and Herzegovina than in Croatia and the FYR of Macedonia and slightly more than in Bulgaria.¹⁷

1.3 Labour market dynamics

Table 1.3 shows the national labour force participation rates for Bosnia and Herzegovina, the two Entities and the Brčko District; for comparison purposes the Table also includes information on neighbouring and EU countries. Labour force participation rates in BiH are lower than in neighbouring countries with the exception of Montenegro, this is due to the very low participation rates of women in BiH, as the participation rates of men are only marginally below those of Bulgaria, Croatia and Romania - those of women are instead 20 percentage points lower than their Balkan neighbours, a very significant difference.

Table 1.3: Labour force participation for BiH and neighbouring countries

Country	Men	Women	Total
Bosnia and Herzegovina	65.5	37.4	51.3
<i>FBiH</i>	<i>66.0</i>	<i>35.9</i>	<i>50.7</i>
<i>RS</i>	<i>64.7</i>	<i>40.3</i>	<i>52.5</i>
<i>DB</i>	<i>61.2</i>	<i>34.1</i>	<i>47.8</i>
Bulgaria	67.0	57.3	62.1
Croatia	70.0	56.7	63.3
Montenegro	57.4	42.9	49.9
Romania	69.4	55.3	62.3
EU25	77.8	62.5	70.0

Source: Statistical Agency of BiH: *Labour Force Survey 2006*, (Sarajevo, 2007) and own calculations; for other countries, European Commission: *Employment in Europe 2006*, Directorate General for Employment, Social Affairs and Equal Opportunities, (Brussels, 2006).

Note: Data for BiH is for April 2006, while data for other countries is for 2005.

Table 1.4 reports the employment rates for the working age population in Bosnia and Herzegovina and its Entities, as well as for neighbouring countries; it shows how extremely low the employment rates are and how there is a large gap between men's employment and women's employment. To a certain extent, BiH's pattern is similar to that of Montenegro, both in terms of rates as well as in the gap between the sexes.¹⁸

¹⁷ World Bank: *Bosnia and Herzegovina poverty assessment*, Vol. 1, (Washington, DC, 2003) op.cit. Survey-based reporting of income is notoriously unreliable and the World Bank's poverty assessment suggests that this is certainly the case in BiH, furthermore, anecdotal evidence from discussions with statistical agency staff involved in conducting the 2006 and 2007 labour force surveys seems to confirm this even further.

¹⁸ Council of Europe; International Labour Office (ILO), *Country Employment Policy of the Republic of Montenegro* (Council of Europe, Strasbourg, 2007).

Table 1.4: Employment rates in BiH and neighbouring countries

		Men	Women	Total
Employment rate	BiH	46.1	24.0	35.0
	- <i>FBiH</i>	46.4	22.3	34.1
	- <i>RS</i>	46.0	27.6	36.8
	- <i>DB</i>	40.3	18.6	29.6
	Bulgaria	60.0	51.7	55.8
	Croatia	61.7	48.6	55.0
	Montenegro	42.4	27.6	41.0
	Romania	63.7	51.5	57.6
	EU15	72.9	57.4	65.2
	EU25	71.3	56.3	63.8

Source: For Bosnia and Herzegovina, author calculations on the data of the LFS April 2006; for Montenegro, see Council of Europe and International Labour Office (ILO): *Country Employment Policy of the Republic of Montenegro*, (Council of Europe, Strasbourg, 2007); for other countries, see European Commission (EC): *Employment in Europe 2006*, DG Employment, Social Affairs and Equal Opportunities, (Brussels, 2006).

Note: Data for Bosnia and Herzegovina are for April 2006, for other countries data refer to 2005.

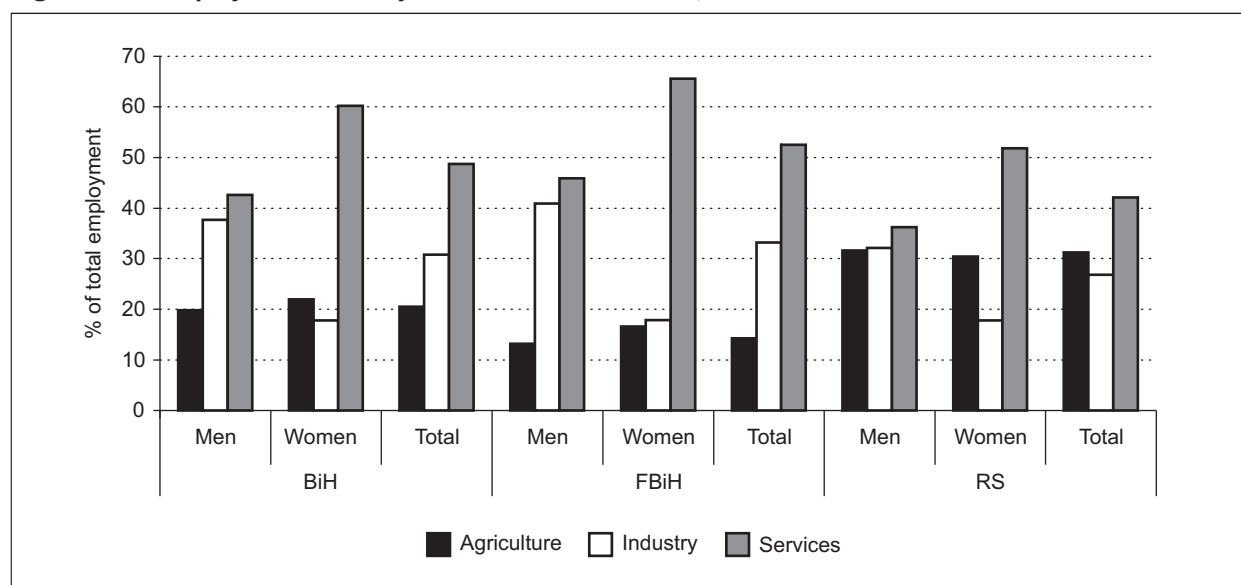
The registered employment data reported in Figure 1.3 suggest modest gains in employment beginning in 2003, while the Living Standards Measurement Survey (LSMS) showed substantial gains in employment in the period from 2001 to 2004, largely attributable to gains in the informal economy.¹⁹ The conclusion that can be drawn from the data is that, although the employment rate continues to be very low, there is at least some evidence that it has increased from the values of 2001.

Figure 1.5 shows employment by broad economic sectors, these data are of particular interest and offer a more accurate picture of sectoral employment in comparison with registered employment for they include informal work arrangements. The data also show employment in agriculture to be 20 per cent of all employment and its concentration in the Republika Srpska (RS), as well as the concentration of women's employment in the service sector for the Federation of Bosnia and Herzegovina (FBiH). The comparison of Figures 1.2 and 1.4 demonstrates how informal employment is the norm in agriculture, as the percentage of employees in registered agricultural employment is only around 3 per cent compared to the 20 per cent reported by the LFS.²⁰

¹⁹ Similar gains are also reported for the employment rate; see H. Poot: *Labour force, employment and unemployment in BiH*, Working paper No. 1 (EPPU, Sarajevo, 2006) and World Bank: *Bosnia and Herzegovina Labour Market Update: The Role of Industrial Relations* (Washington, DC, 2005) op.cit. Indeed, in the Republika Srpska, formal employment fell between 2001 and 2004, whilst the growth in informal employment was barely sufficient to maintain overall employment at the same level.

²⁰ World Bank: *Bosnia and Herzegovina Labour Market Update: The Role of Industrial Relations* (Washington, DC, 2005) op.cit.

Figure 1.4: Employment rates by broad economic sector, 2006



Source: Author's calculations from the *Labour Force Survey, 2006*.

Part-time employment follows the same pattern as in other countries of the region: it is not widespread and accounts for only 11.5 per cent of employment overall. Where part-time employment is more common is in the agricultural sector, with women and in the FBiH; in fact, approximately 56 per cent of women working in agriculture in the FBiH do so on a part-time basis. The general pattern is that part-time employment is found most often in the informal economy.²¹

The data from the LFS suggest that informal employment is around one-third of all employment,²² although when one compares this to the figures derived from the LSMS of 2001-2004 (Table 1.5) one can see that informal employment has fallen slightly in recent years.²³ However, given the different size and sample base across the two surveys, said numbers need to be read with caution.

Table 1.5: Informal employment as a percentage of all employment

	LFS 2006	LSMS 2001	LSMS 2004
BiH	33.6	36.5	41.3
- FBiH	28.3	32.8	36.3
- RS	42.4	40.9	48.8
- DB	33.2	-	-

Source: Author's calculations from *Labour Force Survey, 2006* and World Bank: *Bosnia and Herzegovina Labour Market Update: The Role of Industrial Relations*, (World Bank, Washington, DC, 2005).

Note: The informally employed are defined here as those whose (main) employment does not include either health or pension coverage.

²¹ According to the 2006 LFS, 2 per cent of men and 2.9 per cent of women working in the formal economy have part-time contracts. In the informal economy, part-time employment accounts for 27.9 per cent of men's employment and 33 per cent of women's. In the Federation, 95.6 per cent of women working in agriculture do so in the informal economy and 58.6 per cent of women working in informal agricultural activities do so on a part-time basis, finally, none of the remaining 4.4 per cent of women who work with regular employment contracts in agriculture do so on a part-time basis.

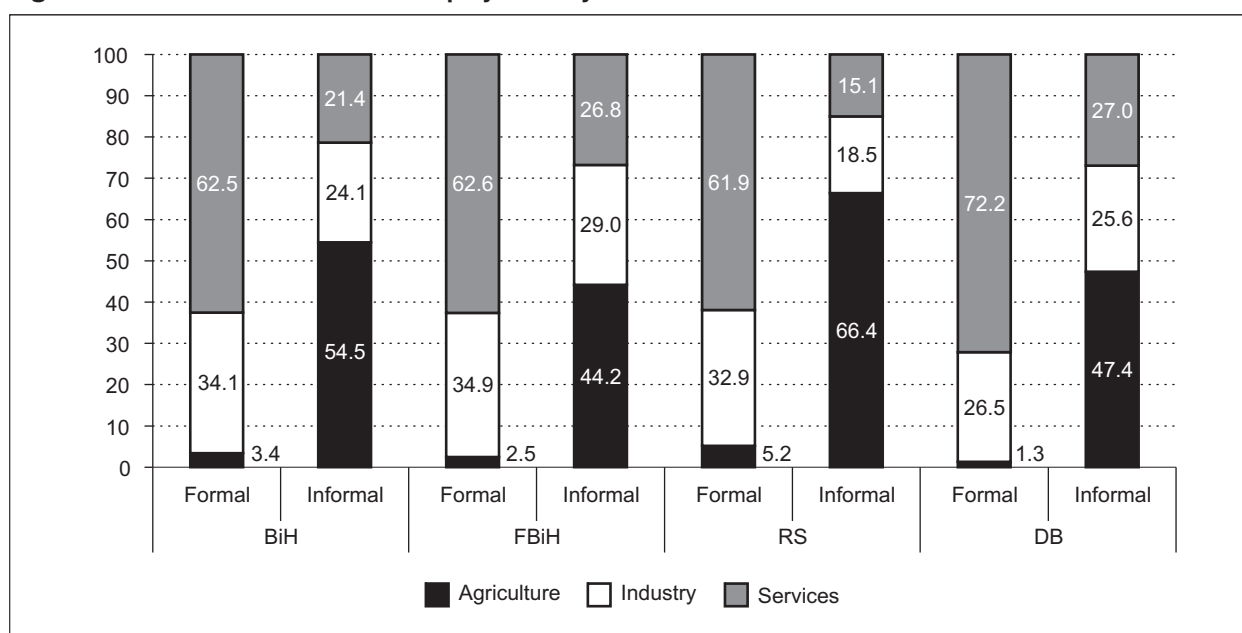
²² As with the previous World Bank estimates, those who work but do not benefit from health and/or pension rights at work are defined as being in informal employment.

²³ These estimates are in line with those found by R. Dell'Anno and M. Piirisild: *Estimate of Non-Observed Economy in Bosnia and Herzegovina* (USAID, Sarajevo, 2004), op.cit. Informal employment –expressed as a percentage of formal employment – would be around 51 per cent; but given that informal employment is generally concentrated in labour intensive activities – in the specific case of BiH this is believed to be in agriculture, construction and tourism – the two estimates are clearly consistent with each other.

Furthermore, Figure 1.5 shows the LFS data on formal and informal employment by economic sector, and highlights the concentration of informal employment in agriculture and its relative concentration in manufacturing as opposed to services.

Interestingly, the incidence of informal employment is lower for women than for men, although this is largely due to the sectoral distribution of informality along male/female employment patterns. Women are more likely than men to work informally in agriculture, but employment in agriculture accounts for around 20 per cent of overall employment, while in industry, which accounts for 31 per cent of all employment, men are much more likely to work informally than women, which results in a slightly higher incidence of informal employment among men overall.²⁴

Figure 1.5: Formal and informal employment by economic sector



Source: Author's calculations from the *Labour Force Survey, 2006*.

Nominal wages in Bosnia and Herzegovina have risen fairly rapidly in recent years and at a faster rate than both inflation and productivity, this is coupled with a convergence among the Entities of average wages paid, which in turn coincides with a convergence of GDP per capita.²⁵ Figure 1.7 shows that, despite rapidly rising prices in RS, the wage convergence is real, albeit much more modest than is depicted in Figure 1.6; real wages rose by around 61 per cent in the Federation and by 85 per cent in the RS between 1998 and 2006.

However, increases in wages in BiH have been fairly modest when compared to the increases in neighbouring countries (Table 1.6). In euro terms, BiH has the second-highest average monthly wage, although that figure is less than half the figure recorded by the region's leader, Croatia. This notwithstanding, in terms of wage growth, BiH ranks only fifth among the seven countries considered, with its wages rising

²⁴ The percentage of men and women working in the informal economy in services is broadly similar.

²⁵ World Bank: *Bosnia and Herzegovina Labour Market Update: The Role of Industrial Relations* (Washington, DC, 2005), op.cit.

by only one and a half times between 2000 and 2006, behind Romania, Montenegro and especially Serbia, where wages (in euros) increased six-fold in the same period.²⁶

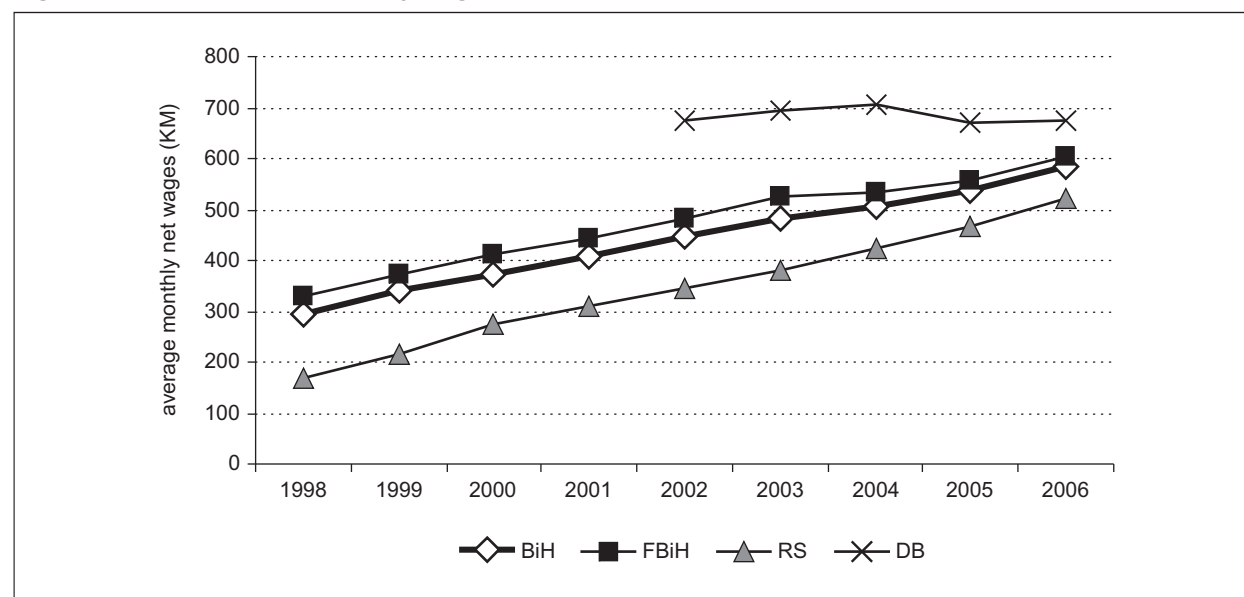
Table 1.6: Average net wages for SEE countries in euros

Country	2006 (€)	Rank	Change 2000-2006	Rank
Bosnia and Herzegovina	300	2	+ 57%	5
Bulgaria	178	7	+ 88%	4
Croatia	625	1	+ 44%	6
Macedonia	219	6	+ 27%	7
Montenegro	246	5	+ 255%	2
Romania	254	4	+ 137%	3
Serbia	275	3	+ 505%	1

Source: Based on data from Economic Policy Research Unit (EPRU): *Economic Trends, Annual Report 2006*, (Council of Ministers, Sarajevo, 2007); for 2006, World Bank: *Bosnia and Herzegovina Labour Market Update: The Role of Industrial Relations*, (Washington DC, 2005); Table 1.8, p. 11, for the 2000 wage data.

The implication of these figures is that much of the economic growth experienced in recent years has fed rising wages rather than encouraged the expansion of employment; furthermore, one might add that rising wages tend to cause production costs to rise as well, which, in turn, are likely to damage the country's export performance while at the same time increase demand for imported (as well as domestically-produced) consumer goods.

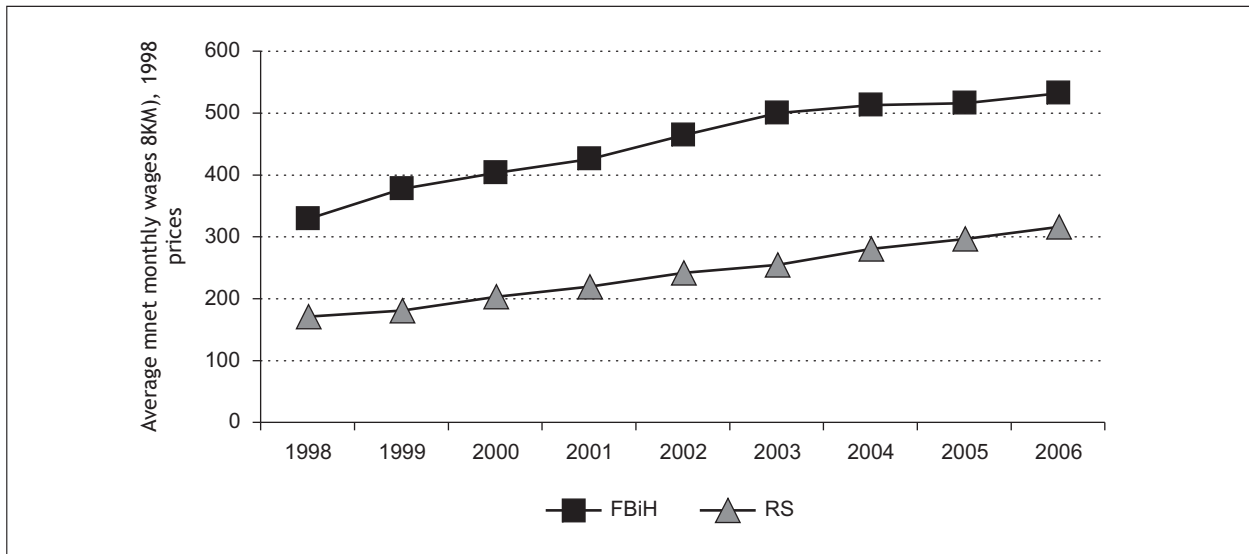
Figure 1.6: Nominal net monthly wages in BiH and its Entities, 1998-2006



Source: State Agency for Employment: *State Review of Employment Policies in Bosnia and Herzegovina for 2006*, (Sarajevo, 2007), op.cit.; Central Bank of BiH: *Annual Report 2006* (Sarajevo, 2007), op.cit.

²⁶ Albania is not included as comparable wage data were not available for 2006. Between 2000 and 2004, Albanian wages rose by around 71 per cent in euro terms so it is reasonable to presume that, if included in the calculations, Bosnia and Herzegovina would rank sixth out of the eight SEE countries in terms of wage growth.

Figure 1.7: Net monthly wages, FBiH and RS, 1998 prices



Source: Author calculations on the basis of data on wages of State Agency for Employment: *State Review of Employment Policies in Bosnia and Herzegovina for 2006* (Sarajevo, 2007), op.cit. On the cost of living see Central Bank of BiH: *Annual Report 2006* (Sarajevo, 2007), op.cit.

CHAPTER 2.

ANALYSIS OF THE YOUTH LABOUR MARKET

In April 2006, the first national labour force survey (LFS) was undertaken in Bosnia and Herzegovina, in 2007 the research was repeated, creating the basis for reliable data with which to study the labour market in the country. Other information available on the labour market in BiH are the records on registered employment and unemployment as well as the data of the LSMS between 2001 and 2004, however, the analysis that follows below is based on the LFS data.²⁷

2.1 Socio-demographic characteristics of young people

2.1.1 Demographic trends

A large youth cohort represents both a potential problem – jobs have to be found for young people, but also a potential asset – as a substantial youth population can make significant contributions to a country's economic and social growth in the long term. The entry in the labour market of large numbers of young people is often associated with a falling dependency ratio, or, in other words, there is the potential for an increase in the per capita labour supply. This is an opportunity for increased growth in the long term, due to the greater (potential) labour supply which increases prospective output per capita, while a rising share of the working-age population implies a higher rate of savings and investment, which in turn leads to increased growth. Yet another factor is the level of human capital, similar to investment in physical capital, investments in the human capital of young people, through education and training, are likely to lead to higher economic growth.

In contrast to these potential benefits it has been argued that in the short term, the larger the youth population, the more difficult it is for labour markets to accommodate the inflows of new entrants; yet there is little evidence to suggest that large youth cohorts cause significant unemployment problems for young people. On the contrary, recent research has provided evidence that in OECD countries there was an elasticity of the youth unemployment rate to the youth-to-adult population ratio of around 0.5.²⁸ An elasticity of a similar scale was found for thirty-two developing and transition countries.²⁹

However, in both studies the extent of the effect of the relative size of the youth cohort is much reduced and/or loses statistical significance when adult employment and unemployment rates are introduced in order to control for aggregate demand factors; while another recent study estimates similar models for a range of developing and transition countries using a variety of specifications.³⁰

The key finding is that there is no evidence that large youth cohorts cause greater unemployment problems for young people, quite the opposite: an analysis of regional labour markets in the USA actually found that the relative size of the youth group leads to a *fall* in unemployment rates. It is perhaps fairest to

²⁷ The reason being that the LFS is more recent and more reliable than registered employment data or the LSMS in providing an accurate picture of labour market developments.

²⁸ D. Neumark and W. Wascher: *Minimum wages and employment*, Discussion Paper No. 2570 (IZA, Bonn, 2007).

²⁹ N. O'Higgins: *Youth Labour Markets in ECA*, (World Bank, Rome, Forthcoming).

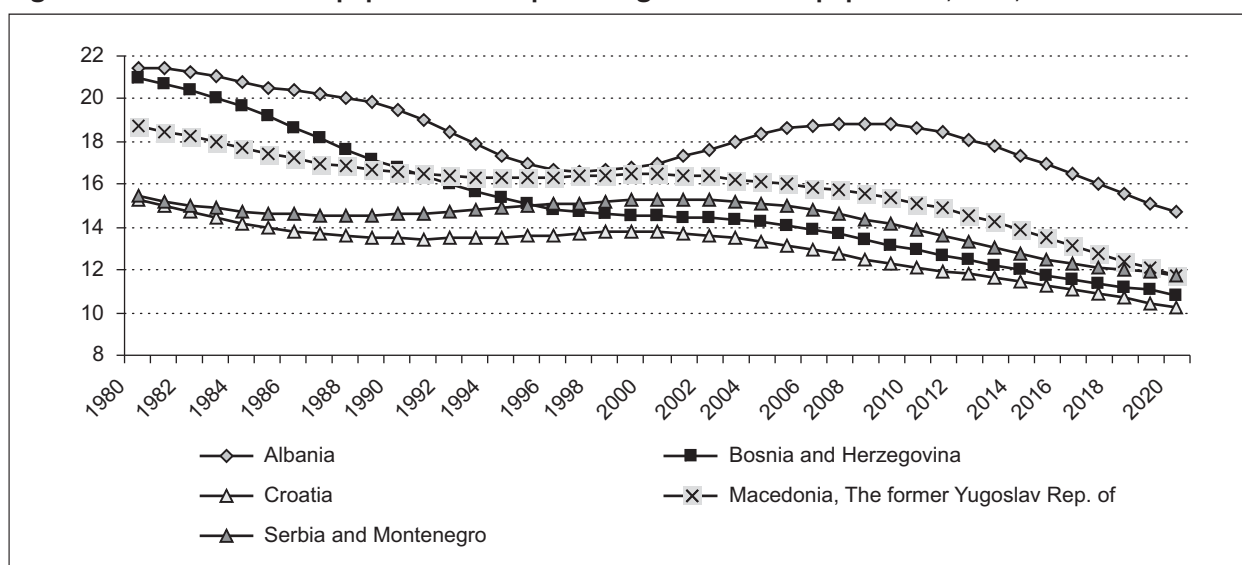
³⁰ J. Fares and E. R. Tiongson: *Youth unemployment, labor market transitions, and scarring: evidence from Bosnia and Herzegovina, 2001-04*, Working Paper Series No. 4183, (World Bank, Washington, DC, 2007).

say that the explanation lies in the variability of the effects of large youth cohorts across countries, as so much depends on how states handle large inflows of new labour market entrants.

Although data on the overall population of Bosnia and Herzegovina is unreliable - the last census dates back to 1991, existing data suggest that the peak in Bosnian youth population (12-24 years) occurred in 1978 and that starting in 2005 it has fallen and will continue to fall at a little under 2 per cent per year, a downward trend that is likely to continue until 2015.³¹

The situation in BiH is similar to that found in other SEE countries, with the exception of the former Republic of Serbia and Montenegro, all countries in the region reached their youth population peak before 1990 and all have experienced a yearly decrease of the youth population (12-24 years) of just under 2 per cent per year (with the exception of Albania which has experienced a slower decrease).

Figure 2.1: Youth (15-24) population as a percentage of the total population, SEE, 1980-2020



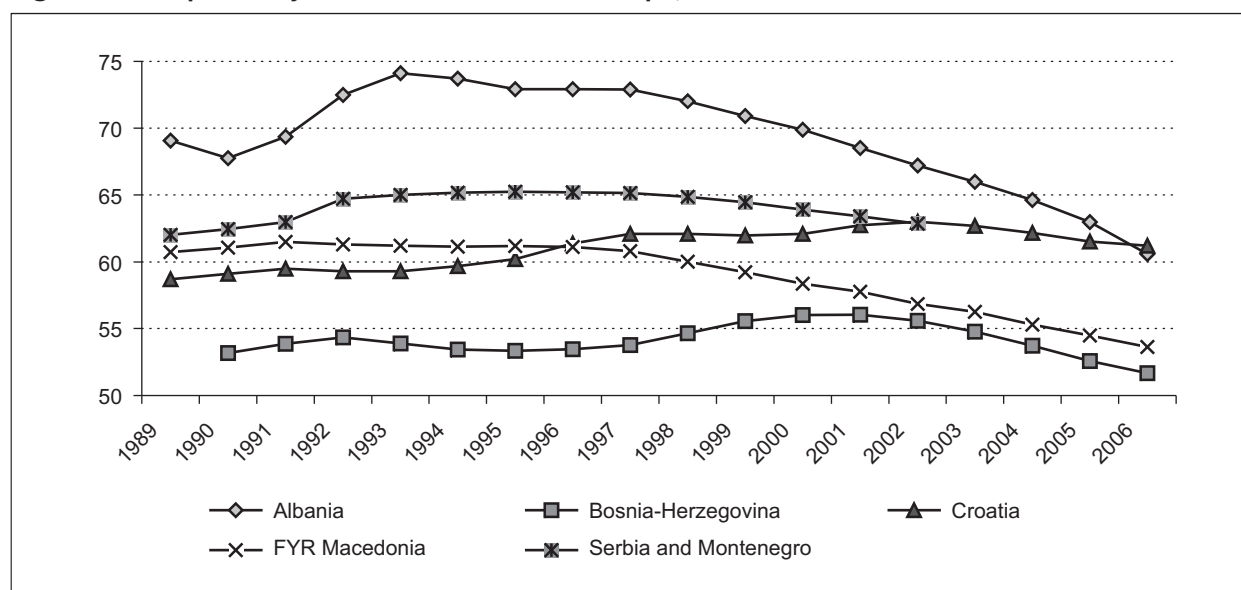
Source: Author's calculations based on ILO: *Economically Active Population, Estimates and Projections 1980-2020*, Vth edition, (Geneva, 2007).

Note: The figures report estimates (1980-2003) and projections (2004-2020) of the youth population as a percentage of the total population in SEE countries.

Figure 2.1 shows the share and future estimates of the youth population (15-24) in South-Eastern Europe over the period 1980-2020; what can be seen is that in most countries, but not in Bosnia and Herzegovina, there was a small increase in youth population during the late 1990s and/or early 2000s. What the 2006 LFS shows is that young people in BiH comprise 14.7 per cent of the total population, which, by international standards, is rather low; while the overall dependency ratio is also falling, similarly to other countries in the region (Figure 2.2).

³¹ D. Lam: *The Demography of Youth in Developing Countries and its Economic Implications*, Policy Research Working Paper No. 4022, (World Bank, Washington, DC, 2006) and N. O'Higgins: *Youth Labour Markets in ECA* (World Bank, Rome, Forthcoming); based on data from Lam's paper, May 2007. The estimated annual rate of decrease in the youth population in Albania over the period 2005-2015 is of around 0.5 per cent.

Figure 2.2: Dependency ratio in South-Eastern Europe, 1989-2006



Source: Based on data from the Transmonee 2007 database, UNICEF IRC, Florence, <http://www.unicef-icdc.org/resources/>

Notes: The dependency ratio is defined here as the percentage of the total population which is aged below 15 or above 59. The use of this age group as opposed to the more usual 15-64 group depends on the data source. The Transmonee database uses the slightly shorter definition of working age population reflecting the tendency, until recently, to set a relatively low pensionable age in Central and Eastern Europe. Data for Bosnia and Herzegovina based on US Census Bureau estimates of 2006.

2.1.2 Trends in education

Table 2.1 reports educational participation rates for teenagers (15-19) and young adults (20-24) in 2006, it shows that the primary reason for non-participation in the labour market is school attendance.

Table 2.1: Educational participation rate in Bosnia and Herzegovina, 2006 (per cent of age-group)

		Men	Women	Total
15-19	BiH	75.0	78.8	76.8
	- <i>FBiH</i>	74.3	79.0	76.6
	- <i>RS</i>	76.5	78.6	77.6
	- <i>DB</i>	74.9	74.9	74.9
20-24	BiH	25.8	32.9	29.2
	- <i>FBiH</i>	28.0	34.1	31.0
	- <i>RS</i>	20.7	30.9	25.6
	- <i>DB</i>	35.0	19.9	72.6

Source: Author's calculations on the basis of the *Labour Force Survey, 2006*.

Note: Based on the response to the question: "Did you attend any School or Training during the last four weeks?"

From the data above it would appear that educational participation is reasonably high in BiH, however, in the context of the Lisbon strategy, it is also important to measure the share of youth who completed secondary education. Table 2.2 shows that BiH is faring reasonably well compared to neighbouring countries, it is close to the Lisbon target of 85 per cent of secondary completion, but fares worse in the less than ten percent "dropout" target. In this area BiH is significantly behind the EU15 and EU27 averages – although well ahead of the FYR of Macedonia and Albania – even more significantly, and in contrast to almost all other European countries, the educational levels of women are lower than those of men.

Table 2.2: Educational attainment, Bosnia and Herzegovina, 2006 and comparable countries (per cent of age-group)

		Men	Women	Total
% of the population aged 20-24 having completed at least upper secondary education	BiH	84.1	83.0	83.6
	- <i>FBiH</i>	84.4	83.5	83.9
	- <i>RS</i>	83.9	82.8	83.4
	- <i>DB</i>	77.9	68.9	73.3
	Bulgaria	80.0	81.1	80.5
	Croatia	92.8	94.9	93.8
	Romania	76.6	77.8	77.2
	EU15	71.5	78.2	74.8
	EU27	74.8	80.7	77.8
% of the population aged 18-24 with at most lower secondary education and no further education or training.	BiH	19.6	26.0	22.4
	- <i>FBiH</i>	19.4	25.7	22.2
	- <i>RS</i>	19.4	25.6	22.1
	- <i>DB</i>	30.5	38.0	34.5
	Albania	-	-	61.9
	Bulgaria	18.2	17.9	18.0
	Croatia	5.3	5.3	5.3
	Macedonia	-	-	36.2
	Romania	19.1	18.9	19.0
	Serbia	-	-	11.4
	EU15	19.4	14.5	17.0
	EU27	17.5	13.2	15.3

Source: BiH - Author calculations on the basis of the *Labour Force Survey, 2006*; Albania and Macedonia – European Training Foundation (ETF): *Key indicators on Vocational Education, Training and Employment in South Eastern Europe* (Turin, 2005); Bulgaria, Romania, EU15 and EU27, Eurostat web site: <http://ec.europa.eu/eurostat>

2.2 Youth labour force participation

The labour force participation rate in Bosnia and Herzegovina (Table 2.3) is very low at 51.3 per cent, a little above the rate of Montenegro, significantly below that found in other SEE countries (around 62-63 per cent) and much lower than the 70 per cent found in the European Union. The disaggregation of labour force participation data by sex, age-group and Entity reveals that these low figures are the result of the low participation rates of younger, older and women workers – particularly in the FBiH.

Table 2.3: Labour Force Participation rates in Bosnia and Herzegovina by age, sex and Entity, 2006

		Men	Women	Total
15-64	BiH	65.5	37.4	51.3
	- <i>FBiH</i>	66.0	35.9	50.7
	- <i>RS</i>	64.7	40.3	52.5
	- <i>DB</i>	61.2	34.1	47.8
	Bulgaria	67.0	57.3	62.1
Croatia	70.0	56.7	63.3	
Montenegro	57.4	42.9	49.9	
Romania	69.4	55.3	62.3	
EU15	78.9	63.2	71.0	
EU25	77.8	62.5	70.0	
By age group				
BiH	15-24	40.1	26.3	33.4
	25-49	81.9	50.0	66.0
	50-64	53.4	22.1	36.6
	65 and over	7.9	3.9	5.6
- <i>FBiH</i>	15-24	39.5	26.6	33.2
	25-49	83.6	47.8	65.6
	50-64	53.6	19.8	35.1
	65 and over	4.4	2.3	3.2
- <i>RS</i>	15-24	41.7	25.4	33.7
	25-49	78.8	54.5	67.0
	50-64	54.0	26.0	39.3
	65 and over	12.5	6.2	9.0
- <i>DB</i>	15-24	38.9	28.0	33.5
	25-49	78.1	46.3	63.4
	50-64	43.4	20.2	30.6
	65 and over	9.5	0.6	4.5

Source: For Bosnia and Herzegovina, author calculations on the data of the LFS April 2006; for Montenegro, see Council of Europe and International Labour Office (ILO): *Country Employment Policy of the Republic of Montenegro* (Council of Europe, Strasbourg, 2007); for other countries, see European Commission (EC): *Employment in Europe 2006*, DG Employment, Social Affairs and Equal Opportunities (Brussels, 2006).

Note: Data for Bosnia and Herzegovina are for April 2006, for other countries data refer to 2005. EU15 and EU25 are the EU members pre- and post- the 2004 accession. EU-NMS comprises the 10 acceding countries at that time (i.e. excluding the most recent entrants Bulgaria and Romania).

2.3 Youth employment

Table 2.4 shows the employment rate, both in the formal and informal economy, recorded by the LFS in 2006 according to age-group, economic sector and form of ownership; what it shows is the very low employment-to-population ratio of teenagers in BiH, which is partly due to educational participation and partly to the high rates of unemployment and joblessness that will be further discussed below.

The employment figures also show that there is a relatively high concentration of young people employed in agriculture, particularly in the FBiH, and among teenagers most of all. The table goes on to show how private sector employment and employment in the informal economy are far more common among young people than adults, and again, this is most marked among teenagers.

Table 2.4: Employment by age-group, economic sector and form of ownership, 2006

	15-19	20-24	25-64	15-64
BIH				
<i>Employment rate</i>	4.2	21.2	41.3	35.0
-Agriculture	39.0	18.4	17.8	18.1
-Industry	28.6	31.2	31.8	31.8
-Services	32.4	50.5	50.4	50.1
- Private	87.1	85.0	55.6	58.0
- Non-private	12.9	15.0	44.4	42.0
- Formal	26.5	54.4	70.1	68.4
- Informal	73.5	45.6	29.9	31.6
FBiH				
<i>Employment rate</i>	3.7	18.9	41.1	34.1
-Agriculture	45.3	17.3	12.4	13.1
-Industry	33.3	31.6	33.9	33.7
-Services	21.3	51.1	53.7	53.1
- Private	85.7	86.8	53.9	56.4
- Non-private	14.3	12.2	46.1	43.6
- Formal	24.6	52.6	74.7	72.7
- Informal	75.4	47.4	25.3	27.3
RS				
<i>Employment rate</i>	5.7	26.5	41.9	36.8
-Agriculture	29.9	20.6	27.5	27.1
-Industry	21.7	30.5	28.4	28.4
-Services	48.5	49.0	44.1	44.5
- Private	89.2	81.9	58.1	60.3
- Non-private	10.8	18.1	41.2	39.7
- Formal	29.7	56.7	61.8	61.0
- Informal	70.3	43.3	38.2	39.0

Source: Author's calculations on the basis of the *Labour Force Survey, 2006*.

The most significant result that can be inferred from the data is that what happens in the youth labour markets in Bosnia and Herzegovina is, to a large extent, determined by what happens in the informal economy, as around three-quarters of employed teenagers (15-19 years), and nearly half of young adults (20-24 years) work in the informal economy; and although there are differences across Entities, these are much less significant than the differences across the various age groups.³² However, teenagers account for a very small portion of the workforce, only around one in twenty teenagers, while one in five young adults are in employment.

Nearly forty percent of employment in RS is in the informal economy, while the figure for the FBiH is slightly below 30 percent; for young people, the situation is reversed: in the FBiH a larger proportion of both teenagers and young adults are informally employed than in the RS.³³ Conversely, in the FBiH the incidence of informal employment is almost twice as high for young people (15-24 years) as it is for prime-age adults (25-49 years), whereas the incidence in the RS is about 1.4.

Table 2.5 depicts the incidence of informal employment by economic sector, sex and by age group, this data show a rather more varied pattern: in the country as a whole teenage girls are more involved in the informal economy than their male peers; young men are more represented in the informal economy than young women, while the highest incidence of informal youth employment is found in agriculture. Finally, the table demonstrates how all teenage girls working in agriculture are employed informally in both Entities, whilst teenage boys in the RS are less likely to be working informally compared to their female peers.

Table 2.5: Incidence of informal employment by age, sex and industrial sector

			<i>FBiH</i>	<i>RS</i>	<i>BiH</i>
Men	All sectors	15-19	68.9	77.0	72.0
		20-24	49.2	46.2	47.7
	Agriculture	15-19	100.0	88.9	95.9
		20-24	86.2	91.7	88.7
	Industry	15-19	47.1	66.9	52.3
		20-24	40.5	40.1	40.0
Services	15-19	54.9	72.7	64.7	
	20-24	41.0	29.4	35.8	
Women	All sectors	15-19	93.4	54.6	77.2
		20-24	44.5	37.6	42.0
	Agriculture	15-19	100.0	100.0	100.0
		20-24	100.0	90.9	96.2
	Industry	15-19	52.7	100.0	76.1
		20-24	16.8	8.4	14.1
Services	15-19	100.0	28.3	51.7	
	20-24	39.2	30.3	36.3	

Source: Author's calculations on the basis of the *Labour Force Survey, 2006*.

Note: Each cell in the table reports the percentage of workers of that type (defined by sex, age and sector) who are employed in the informal sector as previously defined.

³² Given the small sample sizes noted above, attention is limited to the two larger Entities.

³³ For working age adults (15-64). Including individuals aged 65 and over increases the proportion of persons working in the informal economy by a small margin since, although relatively few people work beyond the age of 65, those who do are almost invariably in informal employment.

Given the concentration of informal employment in agriculture and among teenagers, it is likely that informal employment prevails among the poorly educated; Table 2.6 confirms this assumption: similarly to what occurs for youth unemployment, employment in the informal economy is pervasive among those with relatively low levels of education.

Table 2.6: Incidence of informal employment among young people (15-24) by education level

	Primary education or less	Secondary education	Tertiary education	All
BIH	81.8	43.6	33.5	50.4
- FBiH	86.4	45.0	35.5	52.2
- RS	75.7	41.5	33.1	48.2

Source: Author's calculations on the basis of the *Labour Force Survey, 2006*.

Although informal employment may provide young people with a foothold in the labour market from which then to progress onto formal employment, there is actually very little evidence that supports this view; what instead is clear is that employment in the informal economy is characterized by decent work deficits, with no protection and low wages.³⁴

Table 2.7 highlights the low mobility between informal and formal employment: it shows the labour market position of individuals in 2002 and 2004 compared to their employment status in 2001; only around 14 per cent of those in informal employment in 2001 were able to move to formal employment in 2002 and only around 19 per cent managed the transition to formal employment within three years. Conversely, of all those formally employed in 2001, nearly 85 per cent were still formally employed in 2002 and 76 per cent in 2004.

The data does highlight that the main route out of unemployment to employment is through jobs in the informal economy, among individuals who were unemployed in 2001, only one in five managed to move to formal employment three years later. In other words, the predominant pattern is that the unemployed who found work did so in the informal economy and were unlikely to make it to formal employment; on the other hand, formal employment, once obtained, was likely to be held on to long-term.

Finally, the data also indicate that, whilst the majority (62.4 per cent) of the working-age population had a job at some stage over the four years covered by the survey, only 19.3 per cent (or one in five) had a job in the formal economy during the same period.

Table 2.7: Mobility between labour market statuses, 2001-2004

		Activity in 2002				Activity in 2004			
		FE	IE	U	I	FE	IE	U	I
Activity in 2001	Formal employment	84.9	4.7	3.3	7.1	76.0	7.6	6.0	10.3
	Informal employment	13.9	51.6	13.4	21.1	18.7	48.8	12.2	20.3
	Unemployed	12.3	25.3	32.4	29.9	19.9	25.3	24.4	30.4
	Inactive	4.6	10.2	12.9	72.3	8.4	13.2	14.3	64.2

Source: Extracted from European Training Foundation (ETF): *Labour Market Review of Bosnia and Herzegovina* (Turin, 2006), Table 5, p. 21.

Note: The table reports raw percentages.

³⁴ The table is based on data from the LSMS which contains a panel element allowing a glance at movements between labour market statuses over time

2.4 Wages and working conditions of young workers

The LFS data on the type of employment and the hours of work show that young people, particularly teenagers, are much more likely than adults to be on temporary (fixed term) and part-time work, the results are shown in Table 2.8. The balance between these two contractual arrangements is different across the Entities; in the FBiH, young people are less likely to be on temporary contracts, but twice as likely to work part-time, when compared to the RS.

Furthermore, despite the relatively high incidence of part-time employment in both Entities, the reported hours of work remain fairly long, even teenagers work around 36 per week and only in the FBiH are weekly mean and median values below 40 hours.³⁵

Table 2.8: Temporary and part-time work and hours of work

	15-19	20-24	25-64
BiH			
% of employees on temporary contracts	63.1	37.2	13.5
% of employees working part-time	42.2	15.2	9.7
Mean hours of work per week	35.8	43.9	43.6
Median hours of work per week	40	40	40
FBiH			
% of employees on temporary contracts	57.8	39.5	12.4
% of employees working part-time	50.8	18.9	11.0
Mean hours of work per week	31.7	42.0	41.9
Median hours of work per week	30	40	40
RS			
% of employees on temporary contracts	68.0	34.4	16.0
% of employees working part-time	29.7	9.4	7.1
Mean hours of work per week	41.8	46.9	46.3
Median hours of work per week	40	48	40

Source: Author's calculations on the basis of the *Labour Force Survey, 2006*.

Table 2.9 shows the major source of difference between the reported wages for different groups in the LFS, which is participation in the informal economy.³⁶ Overall, youth wages are around 70 per cent of adult wages both for young men and women in both Entities, however, the most striking difference relates to the narrower gap found between youth and adult wages in the informal economy (youth wages are 90 per cent of adult wages), this may be explained by the lower skills level of informal economy workers and which results in a lower youth/adult wage gap.

³⁵ Indeed, in the RS, the median hours of work of young adults (20-24) are 48 hours per week.

³⁶ In order to improve response rates, the LFS asks for interval-based information rather than the actual wage, in order to arrive at mean wages interpolation was required.

Table 2.9: Youth and Adult Wages in BiH (KM per month)

		15-24	25-64	Youth wages as % of adult wages
BiH	All	489	679	72.0
	Formal	528	717	73.6
	Informal	400	442	90.4
	Males	531	805	66.0
	Females	415	630	65.9
	FBiH	555	752	73.8
	RS	383	535	71.6

Source: Author's calculations on the basis of the *Labour Force Survey, 2006*.

The data on formal and informal wages, disaggregated by individual characteristics, show that young workers' wages in the informal economy are closer to adults' wages except in the case of the RS (Table 2.10). In addition, although informal economy wages are lower than formal wages for all groups and in both Entities, reported monthly averages are above the minimum wages established in the FBiH (308 KM) and in the RS (205 KM); these are important findings that will be discussed further in the chapter on minimum wages.

Table 2.10: Youth and adult wages (KM per month) – formal versus informal employment

			15-24	25-64	Youth wages as a % of adult wages
BiH	Formal	All	528	717	73.6
		Agriculture	-	756	-
		Industry	588	657	89.4
		Services	489	747	65.4
		Males	568	748	75.9
		Females	460	661	69.6
		FBiH	617	796	77.5
		RS	408	553	73.8
	Informal	All	400	442	90.4
		Agriculture	-	275	-
		Industry	490	457	107.2
		Services	338	453	74.6
		Males	450	473	95.1
		Females	309	349	88.5
FBiH		436	452	96.5	
RS		310	432	71.8	

Source: Author's calculations on the basis of the *Labour Force Survey, 2006*.

2.5 Youth unemployment and joblessness

The youth unemployment rate, the most commonly used indicator of the disadvantages faced by young people in the labour market, is very high in Bosnia and Herzegovina (Table 2.11); it is roughly three times higher than in Bulgaria and Romania and nearly four times the EU15 average. However, the ratio of youth to adult unemployment rates is not particularly large when compared to neighbouring countries (Figure 2.3) and as youth unemployment is largely determined by insufficient aggregate demand – the general lack of jobs – rather than deficiencies specific to the youth labour market, actions to combat youth unemployment should be part of a more general strategy that promotes employment creation.

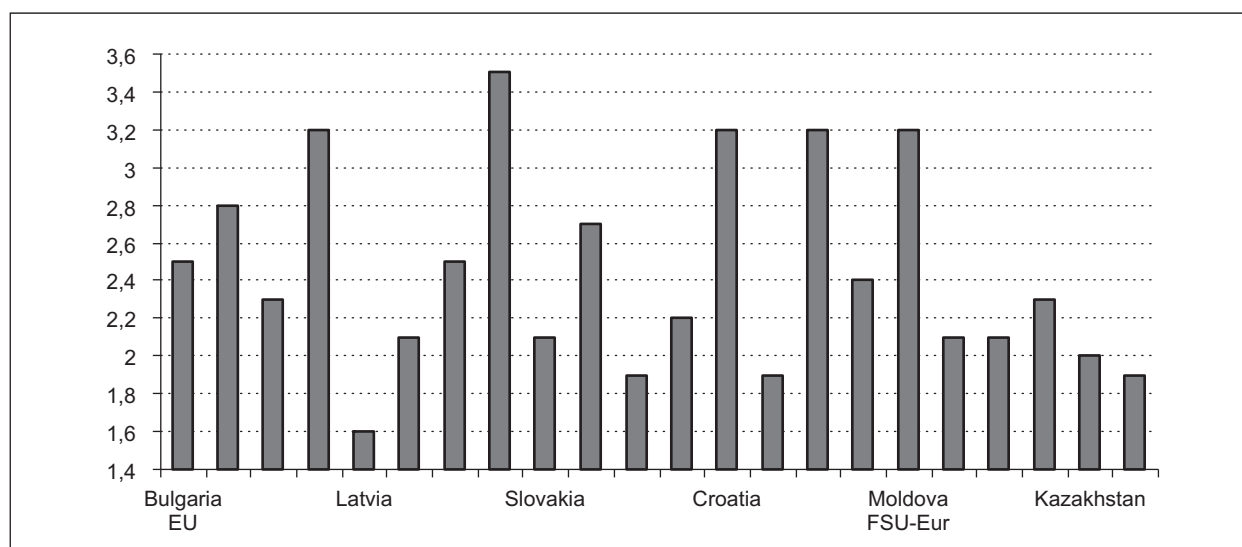
Table 2.11: Youth unemployment and jobless indicators, Bosnia and Herzegovina, 2006

	Men	Women	Total
Youth unemployment rate			
BiH	60.2	65.7	62.3
- FBiH	65.2	68.9	66.7
- RS	48.7	58.4	52.3
- DB	74.6	63.5	70.0
Bulgaria	18.9	20.3	18.9
Romania	22.3	20.2	21.4
EU15	15.7	16.4	16.1
EU27	17.1	17.9	17.4
Ratio of youth to adult (25-54) unemployment rates			
BiH	2.3	2.0	2.2
- FBiH	2.6	2.1	2.4
- RS	1.8	2.0	1.9
- DB	2.5	1.4	2.0
Bulgaria	2.5	2.4	2.4
Romania	3.1	3.7	3.3
EU15	2.6	2.1	2.4
EU27	2.6	2.2	2.4
Youth jobless rate			
BiH	35.0	36.6	35.8
- FBiH	36.4	36.8	36.6
- RS	31.7	35.6	33.6
- DB	37.3	44.9	41.1

Source: For Bosnia and Herzegovina, author's calculations on the basis of the *Labour LFS 2006*; for Albania and FYR of Macedonia, European Training Foundation (ETF) *Key indicators on Vocational Education, Training and Employment in South Eastern Europe* (Turin, 2005); for Bulgaria, Romania, EU15 and EU27, Eurostat web site: <http://ec.europa.eu/eurostat>

Similarly to other countries in the region, the unemployment rate of young women is slightly higher than that of young men, while in terms of differences across Entities, both the youth unemployment rate and the ratio to the adult unemployment rate are lower in the RS than in the FBiH due to the more widespread informal economy in the RS.

The usefulness of the youth unemployment rate as an indicator of youth labour market problems has increasingly been questioned over the last decade; attention has instead shifted towards discouraged

Figure 2.3: The ratio of youth (15-24) to adult (25-54) unemployment rates in selected transition countries


Source: N. O'Higgins: *Youth Labour Markets in ECA* (World Bank, Forthcoming).

young workers – i.e. young people who are neither in education nor employment and who are not actively searching for work – and who are not captured by youth unemployment statistics.³⁷

How discouragement is defined varies – although it can be argued that it should include only those who are not searching for work because they believe that no work is available - in practice it usually includes all those who are not in education or employment.³⁸ In other words, it comprises all young people who are not engaged in a 'useful' or 'productive' activity as well as jobless youth.³⁹ The youth jobless rates are shown in the last section of Table 2.11.

The jobless rate may be larger or smaller than the unemployment rate, according to whether the proportion of the inactive population not participating in education is larger (or smaller) than the proportion

³⁷ See, for example, J.Fares and E. R. Tiongson: *Youth unemployment, labor market transitions, and scarring: evidence from Bosnia and Herzegovina, 2001-04*, Working Paper Series No. 4183 (World Bank, Washington, DC, 2007); A. Kolev and C. Saget: *Towards a Better Understanding of the Nature, Causes and Consequences of Youth Labor Market Disadvantage: Evidence for South-East Europe*, Social Protection Discussion Paper No. 0502, 2005 (World Bank, Washington, DC, 2005); N. O'Higgins: *Youth Unemployment and Employment Policy: A Global Perspective* (ILO, Geneva, 2001); P. Ryan: "The School-to-Work Transition: A Cross-National Perspective" in *Journal of Economic Literature*, Vol. 39, No. 1, 2001 and World Bank: *World Development Report 2006: Development and the next generation* (Washington, DC, 2006).

³⁸ In their exhaustive paper on youth labour market disadvantage in South East Europe, Kolev and Saget report, in addition to the more standard indicators, both the broad ILO unemployment rate and the youth joblessness rate. A. Kolev and C. Saget: *Towards a Better Understanding of the Nature, Causes and Consequences of Youth Labor Market Disadvantage: Evidence for South-East Europe*, Social Protection Discussion Paper No. 0502 (World Bank, Washington, DC, 2005), op.cit.

³⁹ For the purposes of this paper, the issue of whether teenage "home-making" and parenthood is a 'useful' activity is side-stepped by noting that throughout the region, the age of both marriage and first pregnancy is on the increase. The formulas for the youth unemployment and jobless rates are:

$$\text{Youth Unemployment Rate} \equiv \frac{\text{no. of young people who are unemployed}}{\text{no. of young people in the labor market}}$$

$$\text{Youth Job less Rate} \equiv \frac{\text{no. of young people who not employed or in education}}{\text{no. of young people}}$$

the difference in the indicators lies in the differences in both numerator and denominator. Specifically, the numerator and denominator are both larger in the case of the jobless rate; all those who are unemployed are by definition not in education or employment, but the latter also includes those not seeking work. Similarly, not all young people participate in the labour market either because they participate in education or for some other reason they do not actively search for work.

of the active population who is unemployed.⁴⁰ Other things being equal, the higher the educational participation rate, the lower the jobless rate *vis-à-vis* the unemployment rate.

Although it is less common than the youth unemployment rate, this indicator has some useful characteristics that justify its use in conjunction with the youth unemployment rate, for this combination helps to pinpoint youth labour market problems.⁴¹ Its use has three main advantages: first, it includes all those young people who are not actively seeking work, but would work if conditions in the labour market allowed it. Secondly, it provides an indication of the size of youth labour market problems in relation to the youth population as a whole, for it is possible for youth unemployment rates to be very high but, if labour force participation itself is very low, this affects only a very small proportion of the youth population as the youth jobless rate is an indicator of the incidence of youth labour market problems among young people as a whole.⁴² Finally, the comparison of youth jobless with youth unemployment rates can better explain the significance of the youth unemployment rates themselves, it then becomes possible to argue that discouraged young workers are the group most in need of policy intervention in order to prevent their permanent detachment from the labour market.

The rates of youth joblessness in BiH are much lower than the youth unemployment rates, this means that youth joblessness is largely the result of unemployment; in other words, due to the extensive informal economy, the proportion of young discouraged workers is, relative to the unemployed, rather small, as the majority of young people not actively searching for work are either employed or in education. Specifically, among jobless youth, 58.2 per cent are unemployed; a stark contrast to adults, where only 26.4 per cent of jobless adults (25-64) are unemployed.

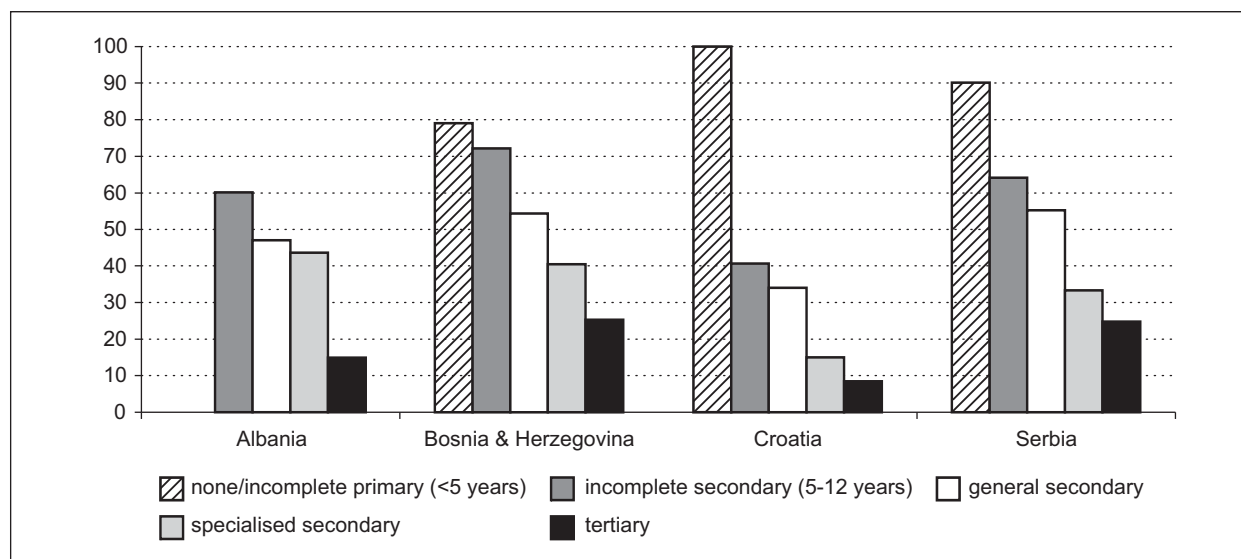
The jobless rate indicates that there is less difference in youth employment problems between Entities, for although the unemployment rates of young women are higher than their male peers in all Entities, the difference between the jobless rates of young men and young women is smaller.⁴³ This implies that differences in youth unemployment are due to factors of labour supply rather than labour demand.

⁴⁰ It is a matter of elementary algebra that, $\frac{a+b}{c+d} > \frac{a}{c} \Leftrightarrow \frac{b}{d} > \frac{a}{b}$. If *a* stands for the unemployed, *b* represents the number of those who are neither employed, unemployed or in education, *c* the size of the labour force, and *d* is the population not in the labour force, then we have the condition stated in the text.

⁴¹ World Bank: *World Development Report 2006: Development and the next generation* (Washington, DC, 2006), op.cit.

⁴² For example, if almost all young people continue education until they are 24 years of age, although the youth unemployment rate is very high, the youth jobless rate will be low. Some argue that this is not – strictly speaking – an indicator of ‘labour market’ problems among young people. Others argue that it is, at least, a useful additional indicator of school-to-work transition problems. This reasoning led the European Commission to include the youth unemployment ratio (i.e. youth unemployment narrowly defined as a percentage of the youth population) in addition to the youth unemployment rate among the standard indicators reported in its *Employment in Europe* annual reports.

⁴³ In general, the information on the Brčko District should be treated with caution. Given the small size of the population, samples sizes are so small they may cause standard errors in the estimates produced – particularly those based on sub-samples of the population.

Figure 2.4: Youth jobless rates by standardized level of education in SEE


Source: Bosnia and Herzegovina – author’s calculations on 2006 LFS; other countries - N. O’Higgins: *Youth Labour Markets in ECA* (World Bank, Forthcoming).

Figure 2.4 looks at the relation between youth joblessness and education level, it reports data for people aged 25 to 34 years of age, as using the traditional youth age-group will inevitably produce a distorted picture.⁴⁴ What is shown is a clear inverse relation between education level and jobless rate in Bosnia and Herzegovina comparable to that found elsewhere in South-Eastern Europe.⁴⁵

However, the relation is somewhat less marked in Bosnia and Herzegovina than in other countries, especially when compared to Croatia. This is likely due to the relatively low level of average educational attainment in BiH, compared to Croatia, and to the relatively large size of the informal economy, as the human capital requirements of the informal economy tend to be lower than those of the formal one.⁴⁶

As mentioned above, one purpose of the jobless rate is to broaden the focus in order to include discouraged workers; Figure 2.5 does this more explicitly by disaggregating the jobless into unemployed discouraged workers and inactive youth - those who are neither searching for, nor wish to work. As mentioned above, most jobless youth are unemployed, while among jobless youth not seeking work, discouraged workers are the majority, with the exception of teenage women.

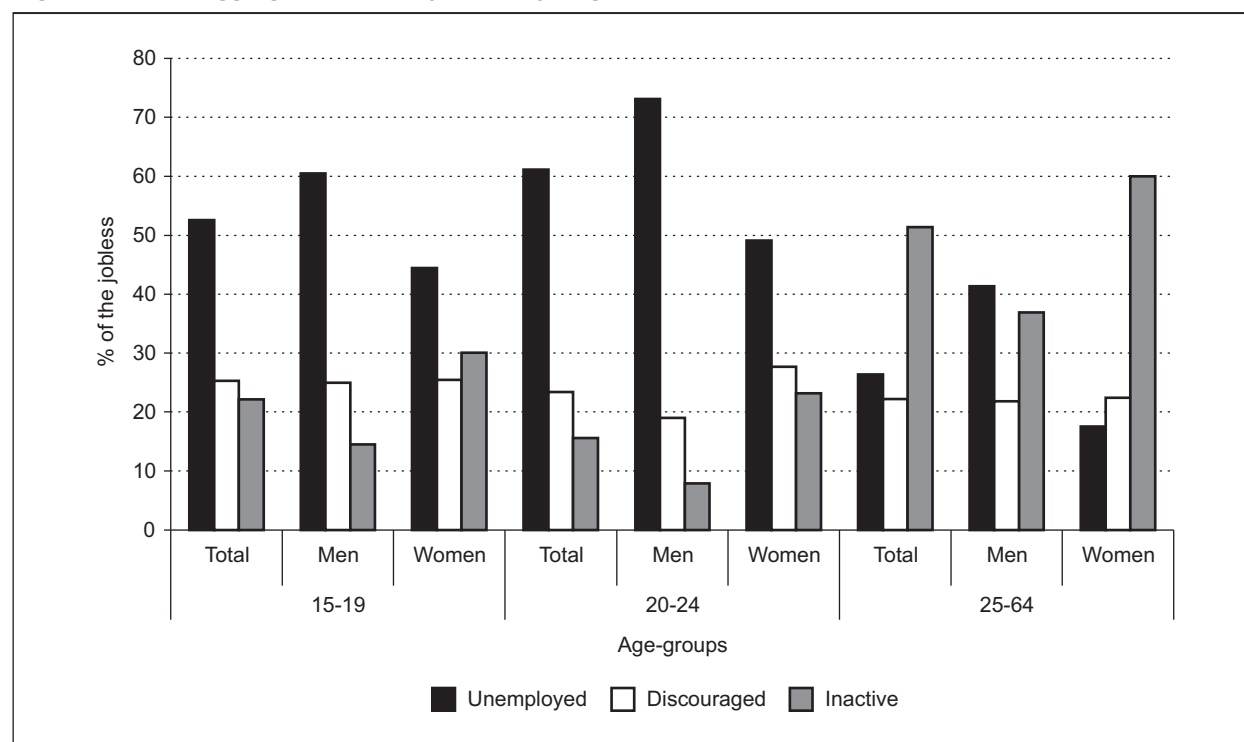
In the inactive group, nearly one in four young men gave as reasons for not seeking work either illness or disability, whereas for young women, the main reason for inactivity (just over one-third) was child

⁴⁴ This issue is discussed further in N. O’Higgins: *Youth Unemployment and Employment Policy: A Global Perspective* (ILO, Geneva, 2001). The problem is one of comparison groups. Implicit in any such comparison is the fact that the principal difference between the groups lies in the variable of interest, that is, in this example, the level of education. However, 15-24 year olds with different levels of education will be different in several ways, not just in their level of education, which will also affect the outcome variable – in this case the jobless rate. Specifically, to take the extreme cases, 15-24 year olds who have completed tertiary education (and no longer study) will be concentrated among the older members of the group, they will also have completed their education more recently than those who have completed only primary and/or secondary education, and they will, in many countries, be only a small subset of those who will, in the end, complete tertiary education. All these factors will affect the probability of joblessness and will contaminate any comparison made on this basis.

⁴⁵ Indeed, this is the case in all transition countries in Europe and Central Asia. See N. O’Higgins: *Youth Labour Markets in ECA* (World Bank, Rome, Forthcoming), op.cit.

⁴⁶ The situation is a little more complicated than what stated here; much depends on where people are employed informally, however, the characteristics of informal employment for young people in BiH suggest that it is concentrated in low wage, low skill jobs.

Figure 2.5: Disaggregation of the jobless by degree of labour market attachment



Source: Author's calculations on the basis of the *Labour Force Survey, 2006*.

care (or care of other non-independent persons). It has been argued that youth unemployment is a less serious problem than it first appears from an examination of youth unemployment (or jobless) rates alone; this is because, although youth unemployment rates are higher than adult ones almost everywhere, what really counts is the duration of unemployment itself, which tends to be far shorter for young people. It is also argued that short unemployment spells are not really detrimental to young people's long-term employment prospects and a higher unemployment rate is a natural consequence of the process of labour market entry where young people 'shop around' for an appropriate job. However, the extent to which young people are subject to significantly shorter spells of unemployment than adults has been questioned by many researchers.⁴⁷

Table 2.12: Incidence of long-term unemployment by age and sex

	15-24	25-49	50-64	All age groups
BIH	78.0	88.8	89.9	85.9
- Men	78.3	88.3	87.5	85.4
- Women	77.5	89.3	95.6	86.5
FBIH	79.0	89.2	90.3	86.1
- Men	78.3	88.7	86.4	85.2
- Women	79.9	89.8	98.1	87.3
RS	75.5	87.9	89.6	85.4
- Men	78.4	87.5	89.0	85.7
- Women	71.4	88.4	91.5	84.9

Source: Author's calculations on the basis of the *Labour Force Survey, 2006*.

Note: The table reports for each sex, age and geographically- defined group the percentage of the unemployed who have been out of work for at least 12 months.

⁴⁷ See, in particular, N. O'Higgins: *Youth Unemployment and Employment Policy: A Global Perspective* (ILO, Geneva, 2001) and P. Ryan: "The School-to-Work Transition: A Cross-National Perspective" in *Journal of Economic Literature*, Vol. 39, No. 1, 2001.

In Bosnia and Herzegovina, the extremely high youth unemployment rates suggest that it is unlikely that the bulk of youth unemployment can be accounted for by this type of frictional unemployment; indeed, the data on the incidence of long-term unemployment (Table 2.12) show that whilst the duration of unemployment does increase slightly with age, it is extremely high for all age groups. In 2005 the incidence of long-term unemployment for adults was 45 per cent in the EU25 and 42 per cent in the EU15; while among Bosnian youth, nearly four out of five of the unemployed had been seeking employment for over a year.⁴⁸

For young people, initial spells of unemployment have lasting negative consequences: being jobless raises the probability of experiencing a subsequent spell of being out of work by up to 30 per cent even two years later, as well as reducing subsequent wages of those who do find work by around 10 per cent, the same comparable effects for other age-groups.⁴⁹

Finally, the duration of unemployment falls with increasing educational levels (Table 2.13).⁵⁰ This evidences that higher levels of education provide a partial way out of the difficult labour market situation faced by young people; the incidence of unemployment and joblessness is lower and its duration shorter for youth with college or university degrees.⁵¹

Table 2.13: Incidence of long-term unemployment among young people in BiH by education level

	Primary education or less	Secondary education	Tertiary education	All
Total	81.6	77.8	56.3	78.0
- Men	83.5	77.5	69.9	78.3
- Women	78.3	78.3	45.7	77.5

Source: Author's calculations on the basis of the *Labour Force Survey, 2006*.

Note: See note for Table 10.

⁴⁸ European Commission (EC): *Employment in Europe 2006*, DG Employment, Social Affairs and Equal Opportunities, (Brussels, 2006).

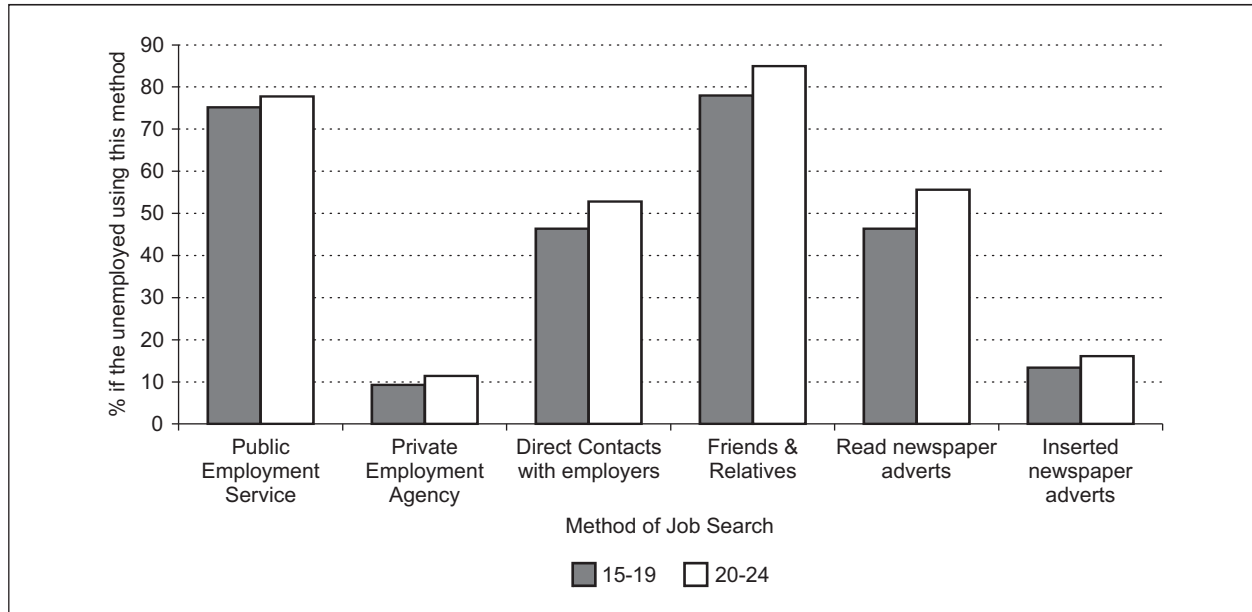
⁴⁹ J. Fares and E. R. Tiongson: *Youth unemployment, labor market transitions, and scarring: evidence from Bosnia and Herzegovina, 2001-04*, Working Paper Series No. 4183 (World Bank, Washington, DC, 2007), op.cit.

⁵⁰ A similar picture is also observable for the working age population as a whole; for details see Council of Europe and International Labour Office (ILO): *Employment Policy Review: Bosnia and Herzegovina* (Council of Europe, Strasbourg, 2008).

⁵¹ Even for young people with tertiary level qualifications, the incidence of long-term unemployment is still higher in BiH than for workers of all ages in the EU25 countries.

Figure 2.6 looks at the job search methods used by the young unemployed; most youth seek employment either through the public employment service (PES) or through informal networks (friends and relatives), while relatively few of them make use of private employment agencies and newspaper advertisements.

Figure 2.6: Principal methods of job search used by the unemployed



Source: Author's calculations on the basis of the *Labour Force Survey, 2006*.

CHAPTER 3. POLICIES TO PROMOTE YOUTH EMPLOYMENT⁵²

3.1 Macroeconomic policy

It is clear from the previous analysis that the difficulties faced by young people in gaining a foothold in the labour market are closely related to the macroeconomic environment. Furthermore, the transition to a market economy in the countries of South-Eastern Europe has brought into question the positive link between employment and growth due to the futile attempt to mitigate the impact of massive industrial restructuring by maintaining unproductive employment.⁵³ In the case of Bosnia and Herzegovina this was further exacerbated by armed conflict, a serious combination of factors which delayed change and – to a certain extent – hampered the creation of new productive employment.

The medium-term macroeconomic outlook in Bosnia and Herzegovina is reasonably positive; although there was a significant drop in investment in 2006, due to a smaller participation of foreign firms in the privatization process and a failure to attract greenfield investments, but this is expected to positively recover in 2007 and gross capital formation is expected to return to its prior level of 20 per cent of GDP, in line with the EU average.⁵⁴

Concern has been expressed in some quarters at the low level of investment due to the expansion of credit to households rather than to enterprises; however, both the pace of financial deepening and the initial concentration on lending to households is in line with that of other CEE and SEE countries, while the privatization of the telecommunications sector and substantial investment in hydro-electric power plants and roads are also expected to make significant contributions to growth in the coming years.^{55 56 57}

The most effective way of promoting employment is to ensure an economic policy environment that stimulates growth with high job creation; this requires a high rate of economic growth coupled with incentives and institutions that make said growth employment-intensive, as well as labour market policies that improve employability, ease transitions in the labour market and match labour demand with labour supply in order to help reintegrate vulnerable groups.

The central goal of the Medium Term Development Strategy (MTDS/PRSP) is the reduction of poverty; this Strategy clearly recognizes the connection between poverty reduction and employment growth and assigns priority, for the 2004 to 2007 period, to labour market reform, achievable through changes in institutions, labour laws and regulations, as well as through the implementation of a series of labour market

⁵² This chapter is based on the paper *Employment Policy Review: Bosnia and Herzegovina*, authored by G. Rosas, V. Corbanese and N. O'Higgins and published by the Council of Europe, Strasbourg, 2009.

⁵³ J. S. Rutkowski et al.: *Enhancing Job Opportunities: Eastern Europe and the Former Soviet Union* (World Bank, Washington, DC, 2005) op.cit.

⁵⁴ Economic Policy Research Unit (EPPU): *Economic Trends, Annual Report 2006* (Sarajevo, 2007), op.cit. This percentage is well below some other SEE countries. Croatia, for example, has an investment rate of close to 30 per cent of GDP.

⁵⁵ See United Nations Development Programme (UNDP): *Jobs and...More Jobs*, (Sarajevo, 2006), op.cit.

⁵⁶ International Monetary Fund (IMF): *Bosnia & Herzegovina: Selected issues*, Country Report No. 07/26, (Washington, DC, 2007):

⁵⁷ Economic Policy Research Unit (EPPU) *Economic Trends, Annual Report 2006*, (Sarajevo, 2007), op.cit.

measures.⁵⁸ Overall, the implementation of several of the 11 policy changes and 12 labour market measures has not been completed or has not yet started; however, the Unit for Economic Policy Planning (EPPU) of the Council of Ministers of BiH is currently working on a new development strategy for the period 2008-2013 which will combine priorities for poverty reduction with those required by preparation for accession to the European Union.⁵⁹

Making employment central to economic and social policies can do much to foster employment-rich economic growth and, as such, employment must become a central element of the new development strategy of BiH, as this would ensure that macroeconomic and sectoral strategies be a central part of economic development and job creation. An active policy on employment can also promote an efficient and equitable functioning of the labour market, it is therefore important that the mid-term development strategy identify policy priorities which foster employment and devise policy objectives and targets that are related to other economic and social policies.

3.2 Education and training

Education and training plays a central role in determining youth labour market outcomes; higher education levels improve individuals' job and wage prospects in the short term and – through their impact on growth prospects in the longer term – promote the general outlook of the economy and therefore youth (and adult) employment growth.⁶⁰

The institutional set-up governing the education system in BiH is complex: there are fourteen Ministers responsible for education; one at State level (Ministry of Civil Affairs), one in each Entity, one for the Brčko District and one for each of the ten Cantons of the FBiH. Beginning in 1996, a number of reforms of the education system were undertaken in order to remedy its complexity, inefficiency and in order to overcome administrative fragmentation. In 2002 the ministries of education of the two larger Entities adopted the *Education Reform Document* aimed at achieving universal primary education by 2010, the elimination of all forms of discrimination, increasing modernization and improving the quality of education at all levels, as well as adopting a comprehensive legal framework and financing system.

Although it has been in preparation for years, little progress has been made in adopting education legislation: the only comprehensive framework adopted relates to primary and secondary education and it was enacted in 2003; this framework envisages the introduction of nine years of basic education and the es-

⁵⁸ The labour market measures provided for by the MDTS/PRSP will be discussed in the sections on labour market policies of this Review.

⁵⁹ Bosnia and Herzegovina signed the Stabilisation and Association Agreement with the European Commission on 16 June 2008.

⁶⁰ The classic example of a system which, through its education and training system, effectively promotes youth employment is provided by Germany, where the ratio of youth to adult unemployment rates is of the order of one-to-one, in contrast to most other countries in the EU15 and ECA region where the youth unemployment rate stands at between two and three times the adult rate. However, in recent years problems have begun to emerge, particularly as regards the fate of young people once they leave the dual system and the system's adaptability in times of rapidly changing occupational and industrial structures. This approach is also costly. Moreover, there are many questions as to the transferability of the German type system to other countries with different institutional settings. For example, the German system rests *inter alia* on the existence of a substantial number of large firms. In post-socialist ECA, companies tend to be small. Notwithstanding this, the German system illustrates the importance of specific design features which could be exported. Perhaps the most important amongst these is the strong involvement of employers in the provision of training which ensures the labour market relevance of training. It provides equitable access to places, and its high (and recognized) quality means that participation does not carry the negative stigma associated with vocational education in many countries. See World Bank: *World Development Report 2007: development and the next generation*, (Washington, DC, 2006), op.cit.

tablishment of a common core curriculum, and has already been introduced in all of the country with the exception of two Cantons.⁶¹

Notwithstanding the provisions of the Framework Law on common core curriculum and the rights of teachers and students to use their own mother tongue, the practice of “*two schools under one roof*” remains widespread; indeed, the bill on Higher Education has been passed by only one of the two Houses of Parliament, while the bills on the Education Agency, the Framework Law on Vocational Education and Training and the Framework Law on Pre-school Education are still pending in both Houses of Parliament.^{62 63}

The box below provides an overview of the current education system, however, the national classification of education does not follow the International Standard Classification of Education (ISCED), although in order to facilitate international comparison, the education structure of BiH has been matched with the main ISCED levels.

Box 1: Bosnia and Herzegovina’s education system at a glance, 2004 – 2005

ISCED	National classifications
0	Pre-primary education starts at the age of 3. In 2004, approximately 13,100 children (around 8 per cent of the age cohort) were enrolled in pre-primary education provided by 200 pre-school institutions (123 in FBiH and 80 in the RS).
1 and 2	Basic compulsory education , extending over 9 years since the reform enacted by the Framework Law on Primary and Secondary Education, comprises 5 years of primary education (ISCED 1) , starting at the age of 6 (level I to V), and 4 years (level VI to IX) of lower secondary education (ISCED 2) . In the school year 2005-2006, there were 1,830 schools with 375,690 students (51.4 per cent boys and 48.6 per cent girls).
3	Upper secondary education starts at the age of 15. It consists of three streams: general secondary education (4 years) providing access to university, four-year technical education and three-year vocational training. The majority of students enrolling in upper secondary education take the vocational training and occupational streams. A total of 165,192 students were enrolled in the existing 304 secondary education institutions in the school year 2005-2006 (49.7 per cent girls and 50.3 per cent boys)
5 and 6	Higher education (according to the Law on Higher Education already approved by one of the two Houses of Parliament), is organised into three cycles. Colleges can grant Bachelor degrees, while only Universities can offer all three cycles. The first cycle of higher education (ISCED 5) lasts 3 to 4 years and leads to a Bachelor degree. The second cycle envisages postgraduate specialisation (1-2 years) and leads to a Master of Arts or Science, while the third cycle (ISCED 6) awards a doctoral academic degree or equivalent and lasts three years. In the school year 2005-2006 there were 105 higher education institutions in BiH of which 8 were universities (6 in FBiH and 2 in RS) with 93,686 students enrolled (55.8 per cent women and 44.2 per cent men). At present, less than 25 per cent of youth is involved in higher education, with an average graduation time of 5 to 7 years.

Source: Statistical Agency of BiH: *Gender 2007*, op. cit.; UNDP: *National Human Development Report 2007*, op. cit.; Framework Law on Primary and Secondary Education (OG RS, No. 38/04), Draft Law on Higher Education and information provided by the State Ministry of Civil Affairs.

The vocational education and training (VET) system is still undergoing reform, many schools have been rebuilt and provided with new equipment, while some piloted new approaches and curricula. Until 2000 there were almost 130 different curricula and qualifications offered in BiH, more than double the av-

⁶¹ The nine years cycle has not been introduced in West Herzegovina Canton, Central Bosnia Canton and has only been partially introduced in the Herzegovina-Neretva Canton.
⁶² School facilities are used by teachers and students of two different ethnic groups with separate administration services and different curricula; in such schools students learn in ethnic isolation.
⁶³ The adoption of the Higher Education Law and Law on Education Agency is considered of particular importance for Bosnia and Herzegovina to meet the requirements of the Bologna Process and the Lisbon Convention.

erage of EU member States and mostly preparing students for jobs that no longer existed. The work undertaken by the EU-PHARE Programme beginning in 2001 produced a new classification of occupations, composed of 13 major occupational areas with a total of 100 occupations, which are now part of the draft Framework Law on Vocational Education and Training.

The VET reform has been slow: the planned large-scale modernization of education and training has not yet materialized, most of the equipment available in VET schools is outdated, the number of teachers trained in new teaching methodologies is still limited and opportunities for work experience in an enterprise are minimal, as the largest efforts have been concentrated on developing mutual understanding and consensus between the many educational stakeholders at Cantonal, Entity and State level.

The VET system currently attracts as many as 60 per cent of secondary education students (slightly more than 60 per cent of them are boys and less than 40 per cent girls) who take vocational education for a period of three years (vocational education) or four years (technical education). These three-year VET programmes normally lead to employment, but have a further option to proceed to the next educational level by taking additional exams; technical education programmes instead lead to employment or to enrolment in post-secondary vocational training or in higher education.

The relevance of VET outcomes to labour market requirements is rather mixed; while the international trend: “*the lower the education and training, the higher the unemployment*” appears to find confirmation in BiH, a number of considerations are needed to better understand VET performance in the country. The finding that the number of unemployed with secondary education attainment is higher than that of the unemployed with primary education should be read with caution, in order to avoid the misconception that education and training have little impact on Bosnia’s and Herzegovina’s labour market.

The fact that the employment rates of workers with secondary and higher education are almost three times those of workers with primary or lower education (74 per cent versus 25 per cent) provides a strong argument to policy-makers for investing in education and training. Similarly, inactivity affects 66 per cent of those with primary or lower education, compared to only 33 per cent of those with secondary and higher education.

As is the case in most countries, in BiH education remains a good investment for the individual; completion rates average about 8 per cent, with higher rates for the sciences and humanities and lower rates for agricultural sciences and other technical subjects.⁶⁴ University graduates are also less likely than those with lower levels of education to be unemployed and much more likely to be employed in the formal economy. Interestingly, people with university degrees are also more likely to be discouraged workers, i.e. without work but not actively searching for employment; in this respect, the tertiary education system seems to be failing to provide graduates with the appropriate skills that respond to the needs of a dynamic labour market.⁶⁵

⁶⁴ Statistical Agency of BiH: *Gender 2007*, Thematic Bulletin, 3 (Sarajevo, 2007), pp. 32 seq.

⁶⁵ World Bank: *Bosnia and Herzegovina Country Economic Memorandum* (Washington, DC, 2005).

Although the evidence is more anecdotal than in the case of secondary education, students, professors and other stakeholders report that tertiary programmes suffer from outdated teaching methodology, curricula and textbooks, as well as suffering from mono-disciplinary programmes which are highly theoretical and unrelated to labour-market realities. The reason for the disconnect between the demand for, and the supply of, university courses, partly lies in the fragmented nature of the tertiary education system and its ineffective management and lack of accountability. The deficiency in inter-faculty cooperation leads to costly duplications in teaching, each faculty organising its own courses without communicating with other faculties and universities. It is also quite possible that the inadequate organization of the university system may be a reason for the low graduation rates.

The weaknesses of BiH's formal education system are compounded by those pertaining to the supply of quality adult training opportunities, as a result, those exiting the formal system with skills that are ill-suited to the labour market have great difficulty surmounting these shortcomings due to the lack of (re)-training and work experience opportunities. Only a small proportion of the working age population (3.3 per cent of youth and 1.9 per cent of adults) currently have the opportunity to upgrade or change their skills, although adult training is offered by a variety of providers, including schools offering second-chance programmes for adults, universities providing courses on managerial skills or for enterprise development as well as a few adult training centres and a number of non-governmental providers offering courses in entrepreneurial skills, information and communication technology, foreign languages and work-related training for disadvantaged groups.⁶⁶

Although training by enterprises was the principal source of adult training in the former Yugoslavia, very little job training by enterprises takes place in BiH today.⁶⁷ For the limited amount of enterprise-based training that does take place, there is no adequate institutional structure for recognising certificates and diplomas and when training is regulated, this is done merely for standards (input) rather than for assessing trainees' competencies (output).⁶⁸ Adult training methodologies and approaches that are self-paced and learner-centred, that build on prior experience and allow flexible entrances and exits at various times in working life, are scarcely found in BiH.

The education sector is funded by the budgets of 13 administrative units: the State, the Entities (the Cantons in the FBiH), the Brčko District and the municipalities; the RS allocates approximately 4 per cent of GDP to education, the FBiH approximately 6 per cent and the Brčko District 3.5 per cent. Total public education expenditure has been growing steadily in the last three years, however, while the overall percentage of GDP spent on education is higher than the regional average and than average spending in OECD countries, in nominal terms the amount spent is around US\$ 535 million per year, given the very low GDP of BiH.

Moreover, the education system is extremely expensive because of its fragmentation: nearly 55 per cent of overall public expenditure is allocated to primary education, with secondary education being allocated 28 per cent and higher education only 17 per cent of the total; furthermore, salaries account for the largest part of budget expenditure by far (88 per cent of total expenditure on education).⁶⁹

⁶⁶ UNDP: *National Human Development Report*, 2007, op. cit.

⁶⁷ This is despite the legal provision that obliges enterprises with more than 50 employees to provide training for workers with work experience over 6-12 months, World Bank, *Bosnia and Herzegovina Economic Memorandum*, 2005, op. cit, pp. 123.

⁶⁸ World Bank: *Bosnia and Herzegovina Economic Memorandum*, 2005, op. cit.

⁶⁹ EU CARDS Programme: *Functional Review of the Education Sector in Bosnia and Herzegovina*, March 2005.

Thus far relatively little is known about the impact of education on the employment experiences of young people in Bosnia and Herzegovina, due the paucity of information available.⁷⁰ The returns on education estimated on the basis of the LSMS data are positive at all levels, although there is a substantial difference between the benefits of secondary and tertiary education.⁷¹ Vocational training has little impact on earnings, except for the youngest of workers, for whom participation in vocational training seems to bring substantial earnings gains.⁷²

The data on educational attainment presented in the previous chapters and the link found between education levels on the one hand, and unemployment and employment in the informal economy on the other, suggest that the country needs to improve the performance of the education system at all levels.

3.3 Labour market policies and institutions

3.3.1 *Employment protection legislation*

Employment protection legislation (EPL) is said to have a variety of possible effects on employment and productivity, some favourable, others unfavourable.⁷³ The main objective of EPL is to provide employment and income security to workers, particularly when they are at high risk of redundancy; in the countries of Central and Eastern Europe a fairly stringent protection was introduced following the collapse of socialism, to mitigate the consequences of the severe recessions which affected most economies during their transition to a market system. Under pressure from the Bretton Woods institutions, and more recently from the EU, South-Eastern European countries began the process of reviewing their EPL, while Western Balkan countries, given the late start of the transition due to armed conflicts, have been slower to remove protections for workers.

The argument often heard is that EPL increases the costs of firing workers, which in turn reduces both hiring and firing, thereby lowering labour turnover as a whole. Whilst labour turnover may facilitate industrial restructuring and improve productivity through better job-matching, the lower job security that accompanies it often impedes in-firm training and, in general, the accumulation of firm-specific human capital. Firms and individuals are less willing to invest in human capital development when the returns on such investment have a shorter or less certain duration, as occurs with the reduction of expected tenure that accompanies a more liberal EPL.

The main negative consequences of a strict EPL are most likely to be felt by those at the margins of the labour market, and in particular by new entrants. A strict EPL may contribute to the creation of a significant pool of long-term unemployed who, as the duration of unemployment increases, find it more and more difficult to re-enter the labour market; it may also contribute, along with taxation and more restrictive busi-

⁷⁰ United Nations Development Programme (UNDP): *Youth in Bosnia and Herzegovina* (Sarajevo, 2003).

⁷¹ J. Fares and E. R. Tiongson: *Youth unemployment, labor market transitions, and scarring: evidence from Bosnia and Herzegovina, 2001-04* (World Bank, Washington, DC, 2007), op.cit.

⁷² The returns on vocational education for young workers (around 21 per cent) are roughly double that of the returns on VET estimated for all workers (around 12 per cent). For estimations on all workers, the returns on vocational education disappear altogether when industry and/or sector are controlled for in the regression.

⁷³ EPL refers to the regulatory provisions affecting "hiring and firing", particularly those governing unfair dismissals, termination of employment for economic reasons, severance payments, minimum notice periods, administrative authorization for dismissals, and prior consultations with trade unions and/or labour administrative representatives.

ness regulations, to the growth of the informal economy, as firms seek to avoid the application of norms and regulations. The most recent research carried out in OECD countries indicates that EPL tends to have a stronger impact on the distribution of unemployment rather than on its level *per se*; in particular, it makes it harder for new entrants and re-entrants to (re-)gain a foothold in the labour market.⁷⁴

In Bosnia and Herzegovina, the analysis of the impact of Employment Protection Legislation is complicated by the lack of a State-level framework, as the EPL is decided at the Entity level (in FBiH at the Cantonal). In practice however, regulations governing the hiring and firing of workers are very similar, albeit not identical, in the three Entities.

Table 3.1 below summarizes the EPL index calculated on the basis of the OECD methodology and compares BiH to neighbouring countries. In common with other Western Balkan countries, the index in BiH is a little higher than the EU and the OECD average index; this is particularly true for the RS, while both the FBiH and the District of Brčko (DB) have indices comparable to those of the EU (in the late 1990s).

Table 3.1: EPL indices for Bosnia and Herzegovina and neighbouring countries

	Year	Regular contracts	Component Indices Temporary contracts	Collective dismissals	EPL summary index
BiH					
- FBiH	2007	1.9	2.6	3.3	2.4
- RS	2007	2.1	3.6	3.3	2.9
- DB	2007	1.9	2.6	3.3	2.4
Albania	1995	2.1	3.0	2.8	2.6
Bulgaria	2003	2.1	0.9	4.1	2.0
Croatia	2003	2.7	2.8	2.5	2.7
Romania	2003	1.7	3.0	4.8	2.8
Serbia and Montenegro	2001	2.2	3.1	3.8	2.9
EU15	Late 1990s	2.4	2.0	3.4	2.4
OECD	Late 1990s	2.0	1.8	2.5	2.0

Source: For Bosnia and Herzegovina, author's calculations on the basis of Entity labour legislation; for all other countries, S. Cazes: *Combining flexibility and security for employment in the Western Balkans* (ILO, Geneva, 2006).

The major difference in the EPL index across Entities arises from the different regulation of temporary and fixed term contracts. In this sense, the relatively high index of the RS is consistent with the finding of a much larger informal economy mentioned in prior chapters.⁷⁵ However, a more rigid EPL is not accompanied by relative higher unemployment rates for young people: the ratio of youth and adult unemployment rates is rather low in BiH compared to other countries in the region; in addition, the RS, which has the strictest EPL, also has the lowest ratio of youth to adult unemployment rates. The implication is that – on the basis of these purely descriptive statistics – the EPL contributes to the distribution of employment be-

⁷⁴ Organisation for Economic Cooperation and Development (OECD): *Employment Outlook*, (Paris, 2006) and A. Bassanini and R. Duval: *Employment Patterns in OECD Countries: Reassessing the Role of Policies and Institutions*, Social, Employment and Migration Working Papers No. 35 (Paris, 2006).

⁷⁵ Indeed, calculations from the *Labour Force Survey 2006* data show that the incidence of both part-time employment and involuntary time-related underemployment are much higher in the informal than in the formal economy. The incidence of part-time employment is 29.6 per cent in the informal and 2.3 per cent in the formal economy. The relative proportions of time-related underemployment are 24.6 and 10 per cent, respectively.

tween the formal and informal economy, as opposed to overall employment or the distribution among age groups. However, a proper investigation of this would require a more sophisticated analysis than the one presented here.

3.3.2 *Minimum wages*

It is often argued that minimum wages may, like a strict EPL, hamper youth employment, the evidence, however, is somewhat mixed; the most recent review finds estimates of teenage employment elasticity with respect to minimum wage ranging from below -1 to above 0.⁷⁶ The authors conclude that the existing evidence points to a negative employment effect of the minimum wage on young people. Of the over one hundred studies considered, nearly two-thirds found negative – albeit often not statistically significant – employment effects, whilst only eight found convincing positive effects. However, the emphasis on demonstrating that the effect is generally negative, misses a key point: the effect of minimum wage in the vast majority of cases is small; in this sense, such results are in line with other reviews that found little or none (i.e. not statistically significant) employment effect of minimum wages for young people.⁷⁷ The effects of minimum wages vary considerably (from negative to positive) according to the presence of other labour market institutions (employment protection legislation, active labour market policies and so on) and the negative effects are most pronounced in unregulated labour markets.

Minimum wage setting is an area where the two larger Entities differ markedly – at least in terms of regulations; in the FBiH, the minimum wage, established in August 2005, stands at 1.75 KM per hour, which corresponds to a net monthly wage of 308 KM.⁷⁸ In the RS, the minimum wage, following its most recent revision in March 2006, stands at 205 KM and, in contrast to the FBiH, allows a sub-minimum wage to be paid to young people. The absence of an hourly minimum wage in the RS is certainly a contributory factor to the very low level of part-time employment in the Entity (8.7 per cent of the employed compared to 15 per cent in the FBiH). In addition to the divergence in average wages between the two Entities, there is also a substantial difference between the Entities in terms of the minimum wage expressed as a percentage of the average wage; in the FBiH, the minimum wage is approximately 53 per cent of the average, whereas in the RS it stands at just under 40 per cent.⁷⁹

The minimum wage might be expected to have a greater impact on wage compression (and therefore a greater detrimental employment impact) in the FBiH than in the RS, however, the analysis of the World Bank suggests that the wage distribution (around the mean) in the FBiH appears to be almost identical to that found in RS;⁸⁰ this implies that the informal economy in the FBiH allows employers to pay lower

⁷⁶ D. Neumark and W. Wascher: *Minimum wages and employment*, Discussion Paper No. 2570 (IZA, Bonn, 2007).

⁷⁷ N. O'Higgins: *Youth Unemployment and Employment Policy: A Global Perspective* (ILO, Geneva, 2001), op.cit. Similar findings are reported also by A. Kolev and C. Saget: *Towards a Better Understanding of the Nature, Causes and Consequences of Youth Labor Market Disadvantage: Evidence for South-East Europe* (World Bank, Washington, DC, 2005), op.cit.

⁷⁸ This is on the basis of a collective agreements rather than a legal minimum wage, due to failure to arrive at an agreed sub-minimum wage for young people. The agreements also provide for differing minimum wages by economic sector.

⁷⁹ This is a rather smaller difference than that reported by the World Bank in *Bosnia and Herzegovina Labour Market Update: The Role of Industrial Relations*, (Washington, DC, 2005), op.cit. Approximately 55 per cent in the FBiH and 20 per cent in the RS. This is because the minimum wage has remained constant since 2005 in the FBiH, but has more than doubled (from 82 KM per month) in the RS in the latest revision in 2006.

⁸⁰ World Bank: *Bosnia and Herzegovina Labour Market Update: The Role of Industrial Relations* (Washington, DC, 2005), op.cit. However, although the study found significant differences between formal and informal economy pay in 2001 and 2002 in the FBiH (with no such corresponding differential in the RS) this difference had practically disappeared by 2003.

wages as well as avoid EPL and tax and social insurance contributions, whilst in the RS informal economy wages are more in line with those of formal economy workers.⁸¹

At first glance, the greater concentration of young people in the informal economy in the FBiH might be assumed to reflect the higher minimum wage in that Entity. As noted above, the incidence of informal employment is roughly twice as high for youth as it is for adults in the FBiH, whereas the incidence in the RS is of the order of 1.4.⁸² One might think that this could be due to a greater propensity of employers to avoid paying the higher minimum wage to young people in the FBiH, however, closer inspection of the available data suggests that this is not the case.

Firstly, the overall incidence of informal employment is much higher in the RS than in the FBiH, if minimum wages were playing such an important role, one would expect the reverse. Secondly, the analysis of reported wages shows that – according to the LFS 2006 data – mean youth wages (in the informal and formal sector) are just over 70 per cent of adult wages in both the FBiH and the RS; in the formal economy, youth wages as a percentage of adult wages are similar in the two Entities, while in the informal economy youth wages are much closer to adult wages in the FBiH than they are either in the formal economy in the FBiH or the informal economy in the RS. If the avoidance of the minimum wage was playing a role, one would expect the opposite.⁸³ Finally, average wages in the informal economy are well above the minimum wage level in both Entities; the minimum wage does not seem to be an important contributing factor to the lack of employment growth in the country, although – like EPL – it may have some impact on the distribution of employment.

3.3.3 Payroll taxes and social security contributions

Between 1999 and 2005 tax revenue as a percentage of GDP fell slightly (from 42.5 per cent to 41.7 per cent).⁸⁴ Such a figure is comparable to the level of tax revenues in the EU15 (40.6 per cent of GDP in 2005) and puts Bosnia and Herzegovina in the higher range among countries of Central and Eastern Europe. Tax revenues are evenly divided between deductions on income and taxes on goods and services – the lion's share being taken by social security contributions, which amount to 15.8 per cent of GDP (or 38 per cent of tax revenues), while indirect (sales) taxes account for 17.1 per cent of GDP (or 41 per cent of tax revenues). By comparison, income taxes (personal and corporate) are low, contributing to only 3.9 per cent of GDP (or 9.4 per cent of tax revenues).

The introduction in 2006 of a flat VAT rate at 17 per cent is likely to increase the proportion of tax revenues on goods and services and preliminary results suggest that indirect taxes accounted for over 50 per cent of tax revenues in the first ten months of 2006; while the introduction of a single rate VAT also marks a

⁸¹ This is supported by the author's calculations on the 2006 LFS. The average informal economy monthly wage in the FBiH was around 57 per cent of the formal economy wage, whereas in the RS, the proportion was 78 per cent.

⁸² Also the slightly higher relative unemployment rates of young people (compared to adults 25-49) in the FBiH compared to the RS tends to point in the same direction.

⁸³ The reported percentages are based on the author's calculations on data of the LFS 2006. There are a number of problems with income data. Incomes are notoriously underreported. However, if at least the *relative* distortion arising from underreporting is roughly the same across Entities, then the argument would still stand.

⁸⁴ World Bank: *Bosnia and Herzegovina: Addressing Fiscal Challenges and Enhancing Growth Prospect* (World Bank, Washington, DC, 2006), op.cit.

significant move towards the harmonization of tax levels across Entities.^{85 86} However, a flat rate tax without exemptions is likely to increase the pressures on the poorest groups of the population and this is exacerbated by the reliance on indirect as opposed to direct (and progressive) forms of taxation. Furthermore, research conducted in OECD countries in 2006 found a robust negative impact of payroll taxes on youth employment, it is then reasonable to argue that such taxes – and above all, social security contributions – are far more significant than the minimum wage in determining outcomes in the BiH labour market.⁸⁷

There are significant differences in tax policy between the two larger Entities, taxes and social contributions are levied at different rates and on different measures of income; in the FBiH, personal taxes and contributions are levied on gross wages, which include the base wage in addition to the employers' share of social security contributions, but exclude allowances (for transport costs and meals). In the RS, taxes and contributions (paid entirely by employers) are levied on the basis of the net wage, including allowances.

These differences are – to a certain extent – more apparent than real, both in terms of their impact on overall labour costs and on the “tax wedge”: the percentage of total labour costs accounted through tax and social security contributions. The World Bank calculates that in 2004 the tax wedge at the average wage was 34 per cent in both the FBiH and the RS.⁸⁸ This is lower than any other SEE countries except Albania, where the wedge is a couple of percentage points lower.⁸⁹ Given the relatively high rates of pay in the country compared to its neighbours, the existing tax wedge is likely to be a significant factor in pushing firms towards the informal economy – far more than the minimum wage.

This is also in line with recent findings in both the OECD and countries of Europe and Central Asia region, which suggest that high payroll taxes – and, in CEE, the “business climate” in general – are more significant factors in determining employment levels than either the strictness of EPL or minimum wages.⁹⁰

In addition, whereas in the FBiH the tax wedge is progressive, i.e. as wages increase so does the tax wedge, in the RS the wedge is purely proportional.⁹¹ A more recent analysis notes that until 2006 the tax wedge in the RS was essentially regressive, by 2007 it had become roughly proportional or very slightly progressive, while in the same year, the FBiH tax wedge was significantly progressive, although not at lower incomes.⁹² Given the lower wages paid in the informal economy, this represents a much stronger candidate for explaining the pattern of informal employment found in the country.

⁸⁵ Author's calculations on the basis of Economic Policy and Planning Unit (EPPU), *Economic Trends, Annual Report 2006* (Sarajevo, 2007), op.cit (Table 6A, p. 74). However, this does not take into account income tax returns.

⁸⁶ The process has not been entirely smooth. The collection of VAT was interrupted several times during 2006 due to disputes at the Entity level over division of the revenues.

⁸⁷ A. Bassanini and R. Duval: *Employment Patterns in OECD Countries: Reassessing the Role of Policies and Institutions*, Social, Employment and Migration Working Papers No. 35, (OECD, Paris, 2006), op.cit.

⁸⁸ As conventionally measured, i.e. as a percentage of total labour costs.

⁸⁹ World Bank: *Bosnia and Herzegovina Labour Market Update: The Role of Industrial Relations* (World Bank, Washington, DC, 2005) op.cit. The choice of wage is important since in the FBiH, non-wage benefits and allowances are not subject to taxes or contributions and, since the value is fixed and independent from income, as income rises so too does the tax wedge expressed as a proportion of labour costs (including allowances).

⁹⁰ Organisation for Economic Cooperation and Development (OECD); *Employment Outlook* (Paris, 2006), op.cit; J. S. Rutkowski et al.: *Enhancing Job Opportunities: Eastern Europe and the Former Soviet Union* (World Bank, Washington, DC, 2005), op.cit.

⁹¹ Despite the fact that contributions are notionally proportional in the FBiH too. Progressivity occurs because allowances are not taxed and, since they are largely fixed sums, the percentage of effective income that is exempt from taxation falls as income rises.

⁹² M. Arandarenko and V. Vukojevic: *Labor Costs and Labor Taxes in the Western Balkans* (World Bank, Washington, DC, 2008).

Currently, both Entities are reforming their taxation system with a view to move towards greater rate harmonization as well as improving tax administration. At the end of 2006, corporate tax was 30 per cent in the FBiH – with a complex system of exemptions and allowances– and 10 per cent in RS. Beginning in January 2007, a new corporate tax rate of 15 per cent was introduced in RS and it is expected that an analogous measure will be introduced in the FBiH in the course of 2007 to reduce the tax rate from 30 to 15 per cent. Similarly, progressivity in personal income tax started in the RS in 2007; the flat income tax rate of 10 per cent was replaced by progressive rates ranging from 0 to 15 per cent, the lower rate applied to earners of the minimum wage in order to encourage their move to the formal economy.

In the FBiH the situation is further complicated by the fact that income tax is also determined at the Cantonal level, although the system does have a degree of progressivity with a base rate of 5 per cent of gross wages and a higher rate applied to incomes above a certain level (varying by Canton). In addition, the personal income tax system is being reviewed and it is expected that new legislation will be introduced in the FBiH in the year 2007.

3.3.4 *Active labour market policies*

The administration of labour market policies involves a State Employment Agency, with representation and coordination functions, Entity-level employment services, and, in the FBiH, Cantonal employment services. In the RS, the Employment Agency is responsible for performing all the employment service functions, while in the FBiH, this responsibility is devolved to the Cantons. Financing also differs across Entities, for although in both cases the bulk of financing accrues from payroll contributions, contributory rates differ considerably across Entities, while the two larger Entities also differ in the composition of expenditures.⁹³

In the FBiH, administrative costs account for 21 per cent of expenditure, passive measures for 33.7 per cent and active labour market policies (ALMPs) for 45.3 per cent. In the RS, administration accounts for 34.3 per cent of expenditure, passive measures total 50.4 per cent and only 15.2 per cent of total expenditures are allocated to ALMPs. Although the number of registered unemployed in the FBiH is 2.3 times higher than in RS, the total expenditure in the FBiH is nearly seven times higher than in the RS.

Access to employment services in BiH is universal, i.e. all job-seekers can use the employment service provided that they register and this registration gives access to health insurance. In fact, the employment service estimates that between 30 and 40 per cent of the unemployed register in order to access health insurance and that as many as 50 per cent of registered unemployed are in reality not actively seeking work.

The high number of registered unemployed results in poor service delivery, inadequate assessment of multiple layers of disadvantage and a lack of focus on the groups most at risk of labour market exclusion. Indeed, it appears that at the moment, the primary function of the employment service in BiH is registering the unemployed, checking their eligibility for unemployment and health insurance benefits while providing basic information on job openings. On the other hand, a number of important functions such as job

⁹³ Council of Europe and International Labour Office (ILO): *Employment Policy Review: Bosnia and Herzegovina* (Council of Europe, Strasbourg, 2008).

brokering, personalized counselling and guidance, screening of the unemployed for participation in active labour market policies (ALMPs) and systematic collection, analysis and dissemination of labour market information are functions not fully performed by the employment services for a number of reasons.

Firstly, the employment services operate under laws and structures that are not conducive to efficiency and effectiveness, for although the employment service is the main institution for implementing labour market policy, when this policy is not coherently expressed, it is difficult for the service to be an effective mediator between labour supply and demand. Secondly, unemployment registers that are inflated by individuals not actually seeking work and the predominance of back-office staff, make it difficult to manage day-to-day work as well as to track the employment status of the registered unemployed.⁹⁴

Slimming down the unemployment register, shifting the balance between back and front staff, better monitoring of the job-search activities of unemployed and the availability of a self-service information system, as well as a more proactive approach in canvassing employers, would certainly improve the effectiveness of the service across Entities. Finally, a revenue system which is based on unpredictable variables such as trends in net/gross wages and the number of reported employees in a highly fragmented and dualistic labour market makes a coherent delivery of the services even more problematic.

Active labour market policies aimed at reducing imperfections in the labour market are justified when they are geared towards alleviating inequalities and social exclusion through better integration of job-seekers and workers through fairer income distribution. International experience indicates that the impact of such active labour market measures is higher if they are effectively targeted, responsive to labour market requirements, linked with work experience and part of a comprehensive package of services.

Throughout Central and Eastern Europe, ALMPs have played a key role in bridging the gaps due to the initial failure of the education and training systems to adapt to the market transition and are likely to continue doing so for some years to come. Recent evidence suggests that ALMPs targeting young people have been more successful in Central and Eastern Europe countries compared to their effectiveness in the United States and the EU15. Moreover, there is international evidence suggesting that the most successful programmes are those targeting specific groups of disadvantaged youth.⁹⁵

The current portfolio of ALMPs across Entities is rather limited, with an emphasis on wage subsidies to employers (for the creation of new jobs, but also to maintain existing ones) and self-employment, while simpler and more cost-effective programmes (job-search, counselling and other basic job-brokerage functions) remain largely underdeveloped. In many countries the labour market information available to young people does not allow them to make realistic choices about the options available to them; indeed the design of ALMPs has increasingly included orientation and guidance through which young people are made aware of available career and job alternatives. This has proven to be a relatively cost-effective form of inter-

⁹⁴ The RS employment service already keeps two types of record, one for those actively seeking work and another for those who register for other reasons (i.e. health insurance, childcare allowances).

⁹⁵ G. Betcherman et al.: *Global inventory of interventions to support young workers: synthesis report*, (World Bank, Washington, DC, 2007).

vention which often obviates the need for more expensive programmes, such as employment subsidies and labour market training.⁹⁶

The main programme targeting young people is the programme for college and university graduates administered in both the FBiH and, beginning in 2006, the RS. This programme provides subsidies for the employment of highly educated young people and although the results of monitoring suggest that the programme is popular with potential participants, no evaluation has been carried out so far.⁹⁷ An impact evaluation will be undertaken to measure the net impact of the programme; however, irrespective of the success of the programme among participants, it does not target the groups of young people who have the greatest difficulty in obtaining employment – those with lower levels of education and/or school dropouts.

The current design and targeting of ALMPs does not cater to the needs of the most vulnerable categories among the unemployed, i.e. those who face multiple disadvantages in accessing the labour market, such as individuals with a low level of education, displaced persons, refugees and members of the Roma population. Overall, both targeting and performance monitoring of ALMPs are weak, and rigorous impact evaluation analyses are not conducted.

The importance of measuring the absolute and relative impact on men and women of the measures implemented by the employment services cannot be overestimated; as it is also important for assessing the cost-effectiveness, relevance and impact of the interventions, as well as for drawing lessons for future programmes. In this respect, the availability of labour market information is essential for the design and monitoring of initiatives.

3.3.5 *Passive labour market policy*

The social protection system in Bosnia and Herzegovina comprises social insurance schemes funded from payroll contributions and programmes funded from general revenues. For both Entities, the social insurance system provides pensions (old-age, disability and survivor), unemployment benefits and health insurance; in the RS, the system also provides child allowances and maternity benefits. Benefits under passive programmes include unemployment benefits for registered unemployed with paid contributions, health insurance coverage for all persons registered as unemployed, and in the RS, pension insurance coverage for recipients of unemployment benefits; it is this free health insurance coverage that is the major incentive to register with the employment services.⁹⁸

⁹⁶ G. Betcherman et al.: *Impacts of Active Labor Market programs: New Evidence from Evaluations with Particular Attention to Developing and Transition Countries* (World Bank, Washington, DC, 2004) and Organisation for Economic Cooperation and Development (OECD), *Employment Outlook* (Paris, 2006); R.G. Fay: *Enhancing the effectiveness of Active Labour Market Policies: evidence from programme evaluations in OECD countries* (OECD, Paris, 1996), op.cit. and more recently G. Betcherman et al.: *Global inventory of interventions to support young workers: synthesis report* (World Bank, Washington, DC, 2007).

⁹⁷ Bosnia and Herzegovina State Agency for Employment: *State review of employment policies in Bosnia and Herzegovina for 2006* (BiH State Agency for Employment, Sarajevo, 2007), op.cit.

⁹⁸ In both Entities, legislation requires the employment services to use available funds to finance unemployment benefit first, and active labour market programmes if, and when, there are residual resources. The free health insurance coverage was quoted by 80 per cent of unemployed beneficiaries as the primary reason for maintaining their unemployed status. World Bank: *Bosnia and Herzegovina: Addressing Fiscal challenges and enhancing growth prospects* (World Bank, Washington, DC, 2006), op. cit.; UNDP: *Jobs and more jobs*, (Sarajevo, 2006).

It is often argued that high unemployment benefits represent an obstacle to the employment of jobseekers of all age groups, however, the extent to which this is relevant in the SEE region has been questioned. The unemployment benefit coverage in BiH is lower than in neighbouring countries; in 2004, less than 1.9 per cent of the registered unemployed received benefits (2.2 per cent in the RS and 1.5 per cent in the FBiH), compared with 12 per cent on average among the SEE countries.⁹⁹ The coverage is even less for young workers: the LFS 2006 reports that only a little over 1 per cent of young people registered at employment offices received unemployment benefits.

More significant are health insurance benefits, as around 80 per cent of young people registered with the employment services receive health benefits. However, this does not seem to be strictly related to employment or unemployment *per se*, as around 30 per cent of young people registered at the employment offices are actually employed.¹⁰⁰ Entitlement to free health insurance for the duration of unemployment registration seems to provide an incentive to stay in the informal economy and avoid paying social insurance contributions.

⁹⁹ World Bank: *Bosnia and Herzegovina: Addressing Fiscal challenges and enhancing growth prospects. A public expenditure and institutional review* (Washington, DC, 2006), op.cit.

¹⁰⁰ Based on data of the *Labour Force Survey 2006*.

CHAPTER 4.

KEY ISSUES AND IMPLICATIONS

Macroeconomic developments have been mostly positive in Bosnia and Herzegovina, the medium term outlook is promising and it appears likely that the country will continue to maintain its sustained level of economic growth for the foreseeable future. However, the positive economic performance of the last period has not been accompanied by employment growth: the economy has entered into a jobless growth path, at least with regard to jobs in the formal economy. The most significant single factor affecting the labour market experiences of young people is the extensive informal economy in the country: more than half of the young people who manage to find jobs do so in the informal economy and for teenagers the proportion is close to three-quarters. These are jobs with poor quality employment conditions and lack of access to social security and pension benefits; in the short term, informal employment also appears to impede the longer term integration of young people into formal employment, in other words, rather than being a stepping stone to the formal labour market, it appears to be more like a gangplank to poverty.

In order to counter some of the labour market problems, the main employment policy priorities for Bosnia and Herzegovina should revolve around the development of the following objectives and policy areas: i) development of an active policy on employment; ii) enforcement of employment protection legislation to cover unprotected workers in the informal economy; iii) education and training; and, iv) employment services and active labour market policies.

Active policy on employment

Although employment promotion is identified as a priority in the national policy agenda, there are no stated employment policy objectives that go in tandem with other economic and social development objectives, nor are there quantitative targets for employment growth. The governments of Bosnia and Herzegovina should consider establishing inter-institutional mechanisms which include representatives of various line ministries and the social partners, all of them tasked with identifying the mix of economic and social policies considered most effective in promoting not only more, but also better employment.

To make sure that employment is considered in its own right and is anchored to economic and social development objectives, it is essential that these representatives take part in shaping the country's development frameworks; employment objectives should be made operational by developing and implementing gender-sensitive employment strategies and related periodical action-plans that address both efficiency and equity targets.

To ensure that the employment policy actually achieves its targets, tight monitoring and evaluation should underpin the overall implementation process. The latter would require strengthening the labour administration system in order to make it more efficient as well as clarifying tasks that are mandated to institutions at different levels; the existence of an adequate system of labour market information is a key pre-requisite for the development of specific interventions, for it can help, *inter alia*, to identify priority areas for action and the specific groups that are to be targeted by interventions.

Here it is important to emphasize the difference between the monitoring of outcomes – for instance the post-programme employment rates of participants of a labour market programme – and the evaluation of impact that involves assessing the change in outcome(s) induced by the programme itself. Currently, in Bosnia and Herzegovina, much work remains to be done to improve the quality of monitoring and to introduce mechanisms for the evaluation of impact. Policy monitoring at present is only understood to mean monitoring that the funds allocated for specific policies are spent, adequate monitoring instead requires the establishment of articulated (and relevant) targets.

The end goal should be the introduction of evaluation mechanisms to measure the extent to which policy interventions helped in achieving specific policy targets – for instance the reduction of informal employment or of long-term unemployment – which can then be used to revise policy in order to improve it.

Employment protection legislation

The analysis found that there appears to be little or no basis to argue in favour of a relaxation of employment protection legislation or a reduction of minimum wages – or indeed the introduction of a special lower rate of minimum wages – to promote youth employment. Two areas where policy action is instead needed are: i) the structure of social security contributions, for it is often regressive and should be made more progressive by the introduction of income thresholds below which contributions are not required; and, ii) the relaxation of the regulation of temporary and part-time employment. Both of these measures would remove disincentives from participation in the formal economy.

Improving education and training outcomes

The need to reform the education and training system is widely acknowledged, policy action should therefore emphasize the improvement of general and job-specific skills for those at the lower end of the spectrum, as the country experiences significant early school-leaving and the analysis in this paper clearly demonstrates that youth unemployment and employment in the informal economy are concentrated among those who have not completed secondary education.

The vocational education and training system is currently undergoing reform. The main features of the reform revolve around the establishment of a common core curriculum based on broader occupational content, the adoption of a modular approach to competency-based VET, the requirement for VET schools to have an advisory council comprising the social partners, and the possibility for VET schools to canvass additional sources of funding through the establishment of public-private partnerships. To make VET more relevant to labour market requirements, it is of the utmost importance to speed up these reforms, since similar actions undertaken by neighbouring countries in recent years have yielded positive results which have redressed the skills mismatch and reduced unemployment among young people.

Progress on the reform of adult training and lifelong learning has been less than satisfactory; current adult training and lifelong learning opportunities only extend to a very small share of the working age population. This is in clear contrast with the profound changes experienced by the Bosnian economy over the past few years and put many workers at risk of losing their jobs because their skills risk become obsolete.

Policy-makers should promote learning and training for adults, especially low-skilled workers and the long-term unemployed; skills training is also important to foster enterprise competitiveness and enhance worker productivity, in order to improve the quality of employment among those young workers who cannot find jobs other than in the informal economy. Adult training and lifelong learning reforms are urgently needed to introduce employment-oriented approaches that allow flexible entrances/exits at various times in working life while recognising prior learning acquired through work experience.

Targeting active labour market policies towards disadvantaged groups

The current portfolio of ALMPs in BiH is rather limited and centred on encouraging employers towards creating more jobs and recruit unemployed people through loans, grants and subsidies. More should instead be done to integrate active measures with other aspects of employment service work (i.e. counselling and job-search assistance) and to sequence them, in order to match them with the disadvantages faced by the job-seeker. An adequate mix of preventive policies could address joblessness and low educational attainment through cost-effective investments in education, as well as with targeted employment programmes that have clear equity objectives. Sequenced counselling, guidance and labour market training – designed to respond to labour market requirements and targeting the unemployed with low educational attainment – could effectively decrease the risk of long-term unemployment.

Active labour market policies addressing young people in BiH are currently mis-targeted; the only labour market programme explicitly aimed at youth is directed towards those with relatively high levels of education. Despite the significant waste of resources – in terms of unused investment in human capital – entailed by the high unemployment rates of highly educated youth, the findings of the analysis indicate that young people with lower levels of education are the ones most in need of assistance to complete the transition to decent work.

Youth employment policy should shift its focus towards young people who are disadvantaged in the labour market, especially those with lower levels of education and early school leavers; indeed, a better design of ALMPs would go a long way towards remedying educational failures and may also be used as a means to coax firms away from the informal economy. Job search assistance and employment counselling to navigate the labour market has been found to be a very cost effective means of facilitating the entry of young people in the labour market; it would therefore be useful for this function of the public employment services to be expanded and strengthened. This combination coupled with more intensive types of assistance – labour market training and employment subsidies – can also improve the overall labour market impact of programmes on final beneficiaries.

There is currently no knowledge of either the efficiency or the effectiveness of the ALMPs implemented so far in Bosnia and Herzegovina; impact evaluation of ALMPs should be carried out to determine whether these programmes are adequately designed, targeted, sequenced and administered and the establishment of a system of both quantitative and qualitative indicators could help assess the programmes' performance.

More specifically, this monitoring and evaluation system would serve to measure the impact on individuals in terms of employment and income, would help identify distortions often produced by these programmes, compare the outcomes of different programmes and identify what does work and for whom. These evaluation results would in turn help improve both the quality and the targeting of programmes as well as inform policy-makers and decision-takers on future financial allocations for programmes that have proved successful.

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