LABOR FORCE COMPETITIVENESS IN CROATIA: STATUS AND PROBLEMS

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What is Competitiveness and Why is it Important?

According to the most widely accepted definition, competitiveness is the ability to achieve success on markets, which then leads to a productive economy and improved living standards for the overall population. Acceptance of the concept of competitiveness is key to Croatia’s further development, because numerous studies have shown a strong link between competitiveness indicators and economic growth, and this in turn influences the attraction of foreign investment, alleviation of poverty and inequality, political stability, and so forth. When speaking of a given economy’s competitiveness, the importance of labor force competitiveness is the focus of particular attention. The most important factors in labor force competitiveness are the educational structure, and compatibility of labor supply and demand in the sense of knowledge, expertise, ability and labor costs.

This introductory section shall provide a brief theoretical framework that outlines labor force competitiveness and a presentation of the essential features of the situation in Croatia. Readers shall also be given a view into the most important positions of other authors.

1 Here we refer to the labor force in the broader sense of a human resource, i.e. the employed and unemployed and inactive persons who can potentially be activated and employed.
Theoretical Framework

Economic theory has long emphasized the importance of research and development, employee expertise and knowledge, and social capital, although their respective meanings vary in the world’s developed countries (technology leaders) and less developed countries. A better-educated labor force finds it easier to embrace foreign technology and rapidly develop its own. To be sure, numerous studies have shown that the impact of education and research and development is scant at low developmental levels, and that after a certain level of development is achieved the average number of years of education completed by the employed and the investments in research and development are positively linked to economic development. Simultaneously, it seems that the role of research and development and labor force education could differ in large and small countries. While greater outlays for education and research and development may increase the rate of innovation in larger countries, in small countries such outlays serve to facilitate the transfer of technology from abroad.

Contemporary knowledge clearly indicates that education and research and development are increasingly more important under the current conditions of the global economy and a knowledge-based world. Education, know-how and innovations have been inculcated into all activities, and they are linked to almost all manner of operations and enterprises of all sizes. Educational institutions and the education level of a population not only influence the creation of human capital, but also the invigoration of socially beneficial capital and the minimization of dysfunctional forms of social capital. Education doubtlessly carries ancillary non-market effects (for example, easier access to information, greater care for personal health, more active participation in social life which encourages responsible democratic civic behavior, election of democratic authorities, and actualization of the rule of law).

As a whole, additional research confirms that economic competitiveness and GDP growth are influenced:

• positively by an increase in the share of persons over 25 years of age who have completed secondary, college and higher education;

• negatively by increased public spending: a larger volume non-productive public spending—and the associated higher taxes—means an unfavorable environment for growth;
positively by the index of the *rule of law* (quality of governmental administration, political corruption, probability that the government will not respect contractual agreements, risk of government expropriation and general respect for the rule of law).

The better education of the general populace and the labor force and lower public spending improve a country’s attractiveness to foreign investors, which facilitates the acceptance and development of modern technological and organizational solutions, paves the way for the rule of law and limits the extent of the informal (gray) economy, increases demands for education and in turn spurs the competitiveness of the economy.

At different levels of economic development, the significance of certain levels of education in the creation of competitiveness changes. For developed industrial countries, research has indubitably shown that there is a close positive link between education and economic growth, with higher levels of education having a greater impact on economic growth. The importance of tertiary education is especially great, as it directly influences the productivity and competitiveness of a national economy and the improvement of general living standards.

Education is certainly essential in the creation of the necessary competitiveness of an economy and society as a whole. It helps a country move up “the ladder of development” and prompts its transition from producing simpler products to more complex items. A more educated labor force finds it easier to adopt foreign technology and to more rapidly develop its own. Another vital aspect in all of this is the acceptance of the rule of law.

The value of formal education in and of itself should not be uncritically overestimated. Most researchers agree that human capital is an essential component of competitiveness and economic development (return on investment in education is greater than that of any other investment), but this is not a *guarantee* of development because countries with the finest human capital do not necessarily achieve the best developmental results. Under conditions of rapid technological development and commerce based increasingly more on conceptual rather than on material production, academic diplomas and degrees are no longer a guarantee of economic success to either individuals or society as a whole.

In transition countries it is particularly true that the existing educational level of the employed and the population as a whole is no guarantee of competitive ability and economic growth. The labor force can easily be
insufficiently or inappropriately educated, i.e. the (formally educated) employed do not have the know-how necessary for successful market competition. Furthermore, the existing systems, with regard to educational results, are expensive and ineffective, but there are no simple formulas to improve them. Here expertise is not sufficient: employees today have to be capable of creating, analyzing and transforming information, communicating effectively, and organizing and coordinating business activities. Developed communication skills, computer knowledge, and the ability and willingness to engage in further education and training are all sought-after qualities.

We can estimate with relative certainty that educational programs in the transition countries of Central and Eastern Europe (particularly those based on the Austro-German model) are more oriented toward the rote memorization of course materials than on independent analytical/critical thinking and deduction and the innovative approach, which is certainly a hindering factor in other approaches to education and future work. Today the emphasis is placed on analytical abilities – the possibility of seeking and selecting information, clarifying problems, formulating assumptions, confirming and assessing evidence, and finding solutions.

Even a well and adequately educated labor force can, for a number of reasons, remain unutilized or underutilized, which has a direct impact on economic competitiveness. There are a number of reasons for this, but most often it involves the unsatisfactory level of social capital and the non-existence of public confidence caused by the high costs of transition. Furthermore, even the best educated and professional labor force will not be sufficiently competitive under conditions of unsatisfactory levels of innovativeness and entrepreneurship in society, non-existence of the rule of law, extensive and deeply-rooted corruption and/or an omnipresent informal economy. Additionally, a disproportionately expensive labor force (given overall salaries and contributions) in relation to actual productivity is certainly not competitive.

Finally, the achievement of a competitive economy and economic growth is hindered by a government that is either inefficient or prone to spending, or an unprofessional and unskilled public administration. Thus, the formation and reinforcement of professional institutions of public authority and a non-governmental sector are equally important to the improvement of labor force competitiveness and the creation of economic growth. In overcoming all of the aforementioned obstacles, an important
positive role can be played by pressure from international organizations or external anchors, such as EU requirements based on the acquis communautaire to develop expert and effectual governmental and public institutions.

In short, the educational structure of a population and employees in line with economic needs is an essential component of competitiveness and economic development, but there are also many other factors that can greatly blunt competitiveness, such as insufficient social capital, a social climate not conducive to free enterprise, lawlessness, and an ineffectual government or governing institutions.

Croatia

Over a relatively short period, the labor force structure based on degree of (formally) acquired educational qualifications improved considerably (naturally, the actual quality of individual educational programs and study courses is not being considered here). The share of unqualified employees declined significantly, while the share of qualified employees—especially those with high and very high qualifications—grew.

Despite the aforementioned formally acquired educational qualifications, Croatia still seriously lags behind the EU member states and some of the Central and Eastern European transition countries. The percentage of highly educated persons is still below the European average, and the same can be said of the effectiveness of schooling and university-level study. Adult education, which is practically the most dynamic sector of lifelong learning throughout the world, is the most neglected area of Croatia’s educational system.

The greatest problem of elementary and secondary education is insufficient differentiation. The curricula for higher elementary grades are formed to continue on into secondary school (gymnasium), and not for continuation of schooling in vocational or trade schools (even though only one fourth of all elementary school pupils go on to study in the gymnasiums). A considerable number of youths in Croatia drop out of secondary and higher educational institutions. According to a rough estimate, approximately 1.5% of enrolled students do not complete secondary school (this percentage is considerably lower for the gymnasiums, and palpably higher in three-year trade schools). Systematic work with gift-
ed and talented students is also lacking, even though this could be done without moving such students into separate classes. It will be necessary to conduct systematic evaluations of the educational system’s results and make comparisons between Croatia and other countries in the region and countries about to join the EU, and launch plans for admittance to PISA and IALS programs2.

The average duration of college/university study is very long, and only one in three students complete their studies, while a large number discontinue them. The number of students who go on to earn degrees in relation to the number of students enrolled in the first year (with a 5-year shift) is only 39%, which shows a low success rate for this type of study.

The educational system must therefore be made more flexible, so that it could become a system that would be navigable, thus avoiding “dead-ends” and lower the early drop-out rate, increase the internal differentiation of students, reinforce informal methods of acquiring knowledge and skills, and improve knowledge of foreign languages. The systematic analysis, disencumbrance, and modernization of educational curricula and programs are essential.

The high percentage of highly educated persons is not directly and/or unambiguously linked to competitive performance. Croatia has more highly educated persons among its employed and overall population than Austria and the most successful transition countries. One can say with relative assurance that the highly educated in Croatia have largely completed studies at university departments and academies which are not directly catered to the needs of a modern economy, and they often do not possess the vital and required knowledge and skill-sets for sought-after occupations.

In a word, it is relatively certain that the labor force in Croatia is (probably) not sufficiently qualified or perhaps inappropriately qualified for the needs of a modern market economy. Efforts must be invested in educational and job-training programs, systematic coordination of education, so that it complies with the needs of the market and encouragement of lifelong education. Investment in human capital is certainly desirable, but it probably will not produce results over the short term. Furthermore, attention should be directed to persons 25 years of age and younger.

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2 There are two occasional OECD research studies: PISA (Program for International Student Assessment) and IALS (International Adult Literacy Survey). See: www.pisa.oecd.org.
An educated labor force is not, in and of itself, a sufficient developmental resource if it is not utilized to apply new technologies. In order to achieve this, technical know-how and management skills are needed throughout society. Improving the institutional environment and social capital is equally important. Several research studies have indicated weak institutions and a visibly lower level of social capital in almost all transition countries. The level of trust is also an indicator of institutional development. Croatia has a considerably low level of mutual trust among its overall population. Furthermore, in terms of trust in the country’s political institutions, Croatia stands roughly at the average of countries about to join the EU, but it lies far below the average of member states. An almost crucial issue in behavior and the decision to comply with or violate the law and obligations is the question of justice and validity of social norms, so that confidence in existing norms is an important indicator of social trust. The more individuals personally perceive widespread violation of norms, the less likely such individuals are to have confidence in them. This is why the consistent prevention of illegal behavior and corruption—particularly the limitation of the opportunity and need for its very emergence—is so necessary and important.

The unsatisfactory level of administrative/governance capacity, in the sense of long-term and highly standardized operations at all levels of governance, is often cited as an almost crucial aspect of the overall competitiveness of Croatia’s economy and labor force. The shortage of qualified officials and organizational ability of administrative employees is frequently noted. Public administration has been plagued by negative selection and de-professionalization for many years now (the result of low salaries and inadequate rules of seniority with a view to advancement), which certainly plays a role in the large-scale departure of professionals and qualified employees from governmental/public bodies, as they can find employment outside of this sphere, while those who lack this opportunity remain.

Other essential components of labor force competitiveness are the (non)existence of entrepreneurial ability and an entrepreneurial climate. Croatia lags considerably in this sense, and according to the index of Total Entrepreneurial Activity – TEA, it was ranked 32nd out of 37 countries studied (Singer et al, 2003). Research identified two basic motives for en-

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3 The Church, military, the educational system, the press, trade unions, the police, Parliament, public services, the social security system and the health-care and justice systems.
entrepreneurial activity: knowledge of circumstances which could be commercialized by launching a business, and necessity, i.e. a lack of any other alternative. In terms of education, most entrepreneurial activity is conducted by respondents with secondary school qualifications, followed by those with college or higher educational qualifications, while the least educated account for the smallest share of entrepreneurs. In general, entrepreneurs in Croatia are three times more likely to be men than women, between the ages of 25 and 34, with secondary school qualifications and higher incomes.

An essential (although not exclusive) component of economic and labor force competitiveness on the international market is the total price of labor. A cheap labor force is an important component of investment in Central and East European countries, while Croatian labor is relatively expensive. The total annual costs of labor in Croatia, calculated according to market exchange rates, was US$ 9,500 in 2002. This is twice the amount in Slovakia, while the difference in relation to the Czech Republic, which came closest to Croatia, is approximately 13%. Based on these data, one can conclude that labor in Croatia is more expensive than in other countries that should accede to the EU in the first round of enlargement, with the exception of Slovenia, which was not included in this sampling because the relevant data were not available. In terms of buying power, net salaries in Croatia were 3% less than in the Czech Republic, but it otherwise far surpassed the other countries in the sampling by between 10 and 40 percent.

The situation is particularly troubling if salaries and labor productivity are compared. Rutkowski (2003) states that salaries in Croatia are high in comparison to other (especially transition) countries and do not correspond to the difference in labor productivity. If per capita GDP is used as a crude measure of labor productivity, it follows that the differences in salaries in Croatia and other transition economies are greater than the differences in productivity. For example, salaries in industrial production in Slovenia are approximately 60% higher than in Croatia, while productivity is almost twice as high, which implies that despite higher salaries, the unit cost of labor in Slovenia is lower. By the same token, while productivity in Hungary is at about the same level as in Croatia, Hungarian salaries are one third less on average.

The high share of taxes and contributions in labor costs has an unfavorable impact on the interest of employers in hiring new employees, (prob-
ably) spurs the impulse to lay off redundant workers, encourages em-
ployment in the informal sector of the economy, reduces domestic (pri-
vate) savings and investment, and has unfavorable long-term effects on
economic growth, the creation of new employment, and the acceleration
of competitiveness. A positive development is that contributions have de-
clined over the last several years, even though this has not been accom-
panied by a reduction of public spending, so that the required funds are
compensated from the central budget and they lead to larger fiscal defici-
cits and public debt. Croatia still has a large share of its budget and pub-
lic spending reflected in GDP, which creates a large fiscal burden and cer-
tainly reduces the competitiveness of the labor force.

External pressure can also help economic development and speed up
competitiveness. Here Croatia’s stable and sustainable economic growth
is perhaps the most important factor. Nothing brings a country closer to
the EU than several years of powerful and sustainable economic growth.
The EU is based on interest, and interest in a country grows if it is pro-
gressive and competitive. Based on several indicators, Croatia has sus-
tainable economic growth, and it has relatively favorable perspectives for
long-term economic growth (5%). The inflation rate is low (2-3%), inter-
est rates are coordinated, the currency’s value is stable, a good portion of
the banking system has been stabilized, and despite of all the changes it
still has a sound tax system that generally complies with EU standards.
Unfortunately, in light of EU accession, these positive aspects are out-
weighed by its shortcomings: a low private sector share (60%, compared
to 80% in candidate countries), high budget deficit (7% of GDP in Croatia,
compared to the 3% of GDP stipulated by Maastricht criteria), and a high
public debt (although still lower than the 60% of GDP stipulated by Maas-
tricht criteria). Furthermore, there are obvious shortfalls in certain vital
microeconomic segments, such as the securities market and market com-
petition policy, and a relatively large dependence on State assistance.

So, developing human capital is necessary, but not sufficient to secure la-
bor force competitiveness. Generating economic competitiveness requires
qualified and capable citizens and employees, but this must be accompa-
nied by the appropriate economic policies – primarily the development
of strong and independent institutions, improvement of public adminis-
tration, curtailment of corruption and the informal economy, and im-
provement of the free enterprise environment. This is no simple task that
can be accomplished quickly, but rather a clear developmental guideline
in which citizens will see improvement in these sectors and can, in a relatively short period, produce valuable results.

Securing labor force and economic competitiveness requires rapid and stable growth, maintaining a low inflation rate and external stability, continuing fiscal adaptation, reducing the deficit and debt levels, limiting subsidies, and encouraging domestic savings. It is equally important to undertake public administration reforms, encourage the emergence and development of independent bodies, and strengthen institutions. Approaching and eventually joining the EU will certainly help Croatia raise its competitiveness and create economic and social development, but expectations here are without doubt too high and unrealistic. Only the citizens of Croatia can jointly achieve competitiveness and economic development, establish efficient institutions and create a society which respects both laws and individual rights.

Creating and improving the Croatian labor force’s competitive edge is not a short term activity that can be achieved quickly, and requires more than just the strength and explosiveness of a 100 meter sprint. It is a long-term process—which is more akin to a triathlon—so it requires persistence, decisiveness and diverse knowledge, expertise and skills in society as a whole.

Other Authors and Works in Publication

It is virtually unnecessary to recall the importance of human capital. In this vein, all developed countries have conducted reforms to encourage the development of human capital, primarily through better education and ongoing training. All of these are directed toward the enhancement of flexibility and openness to the future, strengthening the role of knowledge and increasing innovation. In this fashion, human capital is confirmed as the foundation for understanding reality, regulating interpersonal relationships and improving living conditions, health and freedom. Educational system status and reforms, and comparisons between Croatia and other countries, are the subject of works by Joseph Lowther. Lowther stresses the difficulty of making an unequivocal assessment of the Croatian educational system because Croatia has not participated in international assessments of education and literacy. Even so, the considerable problems faced by the educational system can be cited with relative certainty: lack of emphasis on developing analytical and problem-solving abilities, very weak links between education and the professional
world, and the non-development of lifelong learning. Although numerous education strategies have been proposed, they were neither put into operation nor fully implemented, nor were any major reforms implemented at any level. Curricula and course programs at all levels should thus be reformulated to bring them into closer correspondence with economic needs. Furthermore, the number of required courses should be reduced and the number of electives should be increased, while problem-solving abilities should be improved, teamwork should be encouraged, and learning skills should be enhanced.

Vedran Šošić has undertaken a none-too-easy task by deciding to tackle an almost completely neglected topic in Croatia: the return on investment in human capital as a vital component of Croatia’s competitiveness. He has written an exceptionally high-quality and absolutely fascinating study, and Croatian scholarship as a whole—not just economics—would benefit greatly if all research work was approached so seriously, thoroughly, methodically and accurately. Šošić explains the meaning of investment in human capital, among other things as a means to reduce poverty, unemployment and social exclusion. Political control of wage structures has largely been cancelled in transition countries. As a result, the return on education has grown and begun to resemble the structure observed in developed market economies. The central section of his study is dedicated to human capital and the returns from education in Croatia. Šošić warns that real wages in Croatia are highly unstable, indicating their decline at the beginning of the 1990s and intense growth in the middle and second half of the decade. Wage premiums for education were relatively stable in Croatia during the entire transition period, only recording significant growth toward the end of the period. While the rate of return on an additional year of education was approximately 7.6% in 1996, in 2001 it grew to 10.5%. The return on investment in education in Croatia is somewhat higher than the average in EU member states and other Central and Eastern European countries. Šošić concludes his study with some very important observations and recommendations.

Mario Švigir analyzed structural aspects of Croatian labor force cost competitiveness in manufacturing industry. The author explains income trends within seven different sectors during the 5-year period and compares them to productivity trends in order to understand their influence to import-export. During the observed period, Croatian export was experiencing noticeable structural changes which clearly separated win-
ners from losers in each sector. Although incomes increased slowly within the labor-intense sectors, their share in total export decreased. At the same time, sectors with average income growth increased their share in total Croatian export. Švigir’s data clearly demonstrate that the most important indicator of successful export and of market competitiveness lies not in the income level of certain industry sectors but in indicators such as technology investments, high level of design and product quality, new market awareness, understanding consumer needs, and other.

Alka Obadić uses International Labor Organization (ILO) data to compare labor market competitiveness of developed as well as transitional countries. This topic is definitively very important and up to date. The text comprises of a great number of indicators which illustrate the situation in details. It was the author’s wish to determine Croatia’s place in relation to EU members and transitional countries waiting for accession. The author interprets data for total and economically active population, employed and unemployed, precisely defined number of working hours, incomes and employers’ costs. Possible accession to EU and greater economic connections can be an important initiative for Croatia to compare its accomplishments and labor force competitiveness with highly developed EU countries. Efforts to meet EU standards open various possibilities for many companies and individuals but also represent a serious threat to others, and will definitively influence domestic labor market. In further economic development, and prior to the complete accession to EU, employment difficulties will continue because there will not be enough quality educated labor force that speaks foreign languages and possesses adequate computer skills. At the same time, ongoing education of employees, as well as of those still in the process of education, is of crucial impact.

Based on empiric research results, Nina Pološki Vokić and Dubravka Frajlić explored an interesting and important topic – fairly neglected in domestic literature – Croatian labor force competitiveness. The authors investigate different indicators of employees’ human capital: demographics (gender, age, and qualification structure), mobility, compensation, and investment in education. Besides, they analyze managers’ answers regarding their employees’ competitiveness. Top values of each indicator serve as benchmarks, or better said, as a goal to be reached by every Croatian company. Considering that the wanted value level is mostly above the average, realistic value, the authors conclude stating that Croatian employees are not competitive enough. Their research indicates
that the most competitive employees are highly skilled ones whose existing flaws, such as lack of computer skills or foreign language inefficiency, can be remedied by additional investment in their education.

“What exactly determines competitiveness and economic growth?” is a question almost impossible to answer with just one answer. It is very hard to reach adequate competitiveness and growth level, while it is very easy to prevent and slow down its development. Countries with same or similar policies achieved different economic results. Even more, certain countries with almost unchanged policy were taken as a success example during one period and as a failure example in another period. To achieve human competitiveness and economic growth is like putting puzzle pieces together; it takes time and effort to put all the pieces together and then, all of the sudden, an open door current (or a mistake) can ruin it all. Still, it is quite clear that competitiveness and economic growth will not be achievable where there is no technology development, no science improvements, no expertise, not enough skilled population, bad entrepreneurship atmosphere, lack of trust in the society, corruption, insufficient public administration, and too huge and irrational public expenditures.

LITERATURE


