

## **THE IMPACT OF GROWTH ON POVERTY. EVIDENCE FROM THE “JOBLESS GROWTH” IN ALBANIA**

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### **- Abstract -**

Development and growth are supposed to have a positive impact in the labor markets but “jobless growth” seems to be a major obstacle for the poor to benefit from the positive growth performance experienced by this country, as by many other countries around the world. There is a wide disparity in the extent of poverty reduction that a growth process can achieve. Therefore, the impact of growth on poverty is seen as depending on the extent to which growth generates employment and good earning opportunities. If employment growth is achieved at the expense of wage reductions, it may have an inadequate impact on poverty. Moreover, since in many low income countries the poor cannot afford to be unemployed, policies should be more concerned with raising the income of the working poor.

In this paper we analyze the evidence from Albania with the purpose to expand the understanding of these issues, providing empirical effort into the debate that why growth is jobless in this country, by studying the cumulative and sectorized employment and productivity profile of growth and its correlation with observed poverty changes.

The main findings are related to the labor market policies that can improve the working conditions and the sectorized growth which achieves a greater poverty reduction. Interesting implications are explored for policy makers in order to apply successful strategies that enhance the positive impact of growth on poverty.

**Key Words:** *growth, employment, poverty*

**JEL Classification:** O40, I32, J21

## 1. INTRODUCTION

"The economic growth that has not led to the creation of new jobs", has been a regional problem, but Albania prevails among the countries in transition with a low-level of new jobs creation, considering the strong growth of GDP. With the stabilization of the economies of Eastern Europe after the transition, employment generally lags far behind output growth. In many countries in the region, there has been virtually no net opening of new work places, but none has had the experience of Albania's economic development. If we make a comparison of Albania with a selected group of countries in the region (such as Serbia, Montenegro, Macedonia, Croatia, Bulgaria, Romania, Turkey, Slovakia, the Czech Republic, Poland, Hungary) in terms of the way how employment and GDP are ambled in recent years, employment growth has been stagnant for the region, where a number of countries have lost their work places in spite of economic growth. Most of the above countries have undergone changes in employment during the period, in terms of -1% and +1%; however there are significant differences in the trends of GDP between these countries. Albania occupies a somewhat unique place among them, with a modest opening of new places of work, but with sound rates of GDP growth.

The main concern about the situation of the labor market focuses on the effects of informal employment growth and high levels of migration. These are serious issues and are part of a wider problem of new jobs creation in the formal market. A significant part of the labor force is employed in the informal sector and informal employment is important both for the economy and for the well-being of many families. These workers are particularly vulnerable and are often poor.

Moreover, many Albanians have left the homeland to find gainful employment. Remittances from employment are seen as a vital source of income, but also represent immigrants phenomenon of "brain drain" for the country. Both informality and migration are consequences of the fundamental problem, which is that the employment is not generally increasing, and in particular this is true for the formal sector. These data on employment are particularly disappointing especially considering the context of a relatively healthy economic development. The Real GDP annual growth averaged around 6% during the period from 1998 to

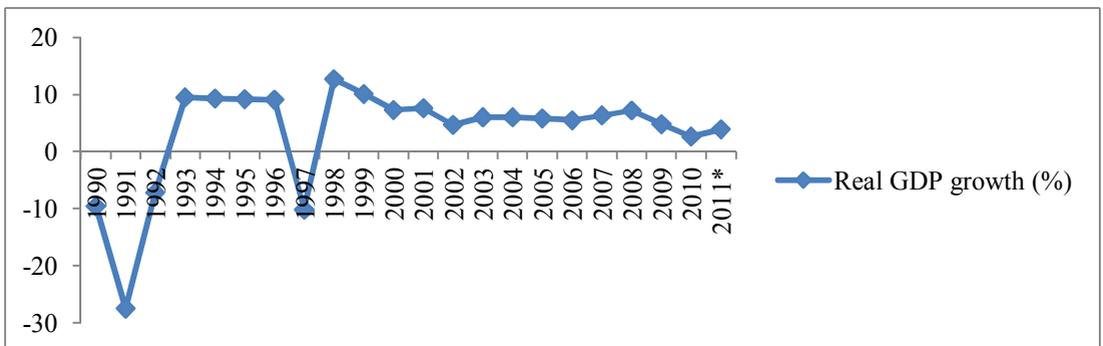
2009, so, when we talk about economic development, what we can say is that this economic development itself, brought no increase in the level of employment.

## 2. GDP EVOLUTION DURIN TRANSITION IN ALBANIA

Given that GDP is one of the indicators that highlight the performance of the economy and its development, we can say that the performance of GDP has followed the course of political events in the country, which proves once again the important role that political stability in developing economies. Thus, in the beginning of transition, during 1990-1992, a period of great social tension and changes of power, GDP recorded its largest decline. With the onset of political stability, GDP grew from year to year, even in the two-digit level (in 1995-13 percent). The 1997 crisis was reflected directly in the decline of this indicator. With the restoration of the political stability, GDP growth started again. Promoters of this growth have been the construction and services industries, which, during the period 1992-2003 increased respectively with an average annual rate of 18 percent and 8 percent, but the major share in this growth was maintained from remittances, which crossed the level of 600 million USD per year. If we refer to the official statistics, GDP per capita in 2005 was worth 2596.69 USD, while in 2010 there were 3694 USD.

The growth of GDP per capita has increased the standard of living, one of the components of human development indicators ("Human Development Index"), which is calculated by the UNDP and compares the health, education and standard of living between countries. Albania has entered the group of countries with a high level of this indicator in 2008.

**Figure-1: Real GDP growth in %**



Source: INSTAT, Bank of Albania, Ministry of finances: 2012

\* 2011 data are preliminary

Although this dynamic is quite positive, as a result of which before the end of the last decade was overcome the level of GDP and GDP per capita of 1990, we must not forget that this increase is based on factors with high flexibility and the level of GDP per capita, compared with other countries, is very low. Thus, the level of output per capita in our country is 20 times lower than in high-income countries, 5.4 times lower than the world average per capita production level and 50 percent of the production in low-income countries. Compared with other countries in the region, the situation is very critical. With the exception of Bosnia and Herzegovina, the index of GDP per capita is the lowest. These data clearly point to the urgent need to overcome the situation and to increase production and its effectiveness at high rates.

In achieving this difficult but necessary objective, short-term scientific strategies and medium-term socio-economic development of the country are needed, in which should be clearly defined the priority branches that will ensure sustainable development, the measures and policies that the state will apply to advance their progress according to a certain order.

### **3. EMPLOYMENT EVOLUTION DURING TRANSITION IN ALBANIA**

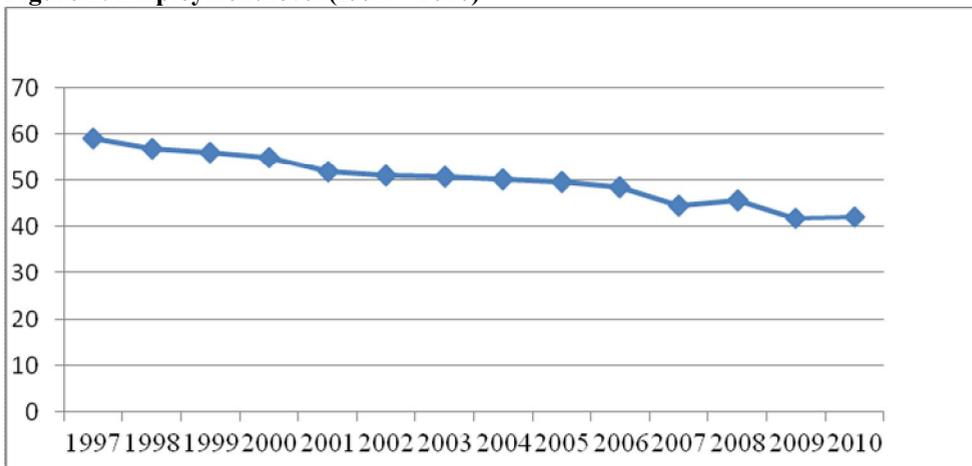
We cannot speak in real terms at what extend the economic growth has contributed in job creation as long as the informality in the labor market is too high. A part of the reduction in unemployment is attributed to the reduction of active efforts to find a work, as is clear from the large number of inactive people in working age, especially households and from the relatively low level of employment of people in working age. Macroeconomic reforms and the restructuring of the early 90's reduced the demand for labor in Albania, as well as in other countries in economic transition, the country suffered a decline in the labor force participation rate. Mass privatization of the closed state enterprises, as well as the increased competition for a reduced number of jobs, forced many people to withdraw from the labor force. In addition to the above reasons, the increasing level of enrollment, especially in secondary education in rural areas probably, could partly explain the declining level of participation in the labor force. A small percentage, (10-15%) of the unemployed were employed in the formal sector from 2002 to 2009 and only 10% of those who have been out of the labor force in 2002, made a similar transition. According to World Bank indicators, 38% of the unemployed have found informal wage employment.

Increasing levels of emigration abroad are a great testimony of insufficient creation of jobs.

The period during 1990-1993 represents the years in which are closed the largest number of state-owned enterprises and therefore are the years of drastic employment reduction. In 1990 employment fell by 2 percent, in 1991 by 4 percent, in 1992 by 25 percent, in 1993, by 30 percent. The decline in public sector employment was replaced with the newly created private sector employment. In 1992, the private sector had 60,000 employees, in 1994 this sector accounted for 46,000 private enterprises, especially small business, with 103,000 employees or self-employed, in 1996 with 59,000 private enterprise and 116,000 employees, and in 1999, 56,000 enterprises with 103,000 employees and self-employed. According to Labor Force Survey data and in accordance with the definition of EUROSTAT and the International Labor Organization on employment, about 1,123,000 employees aged 15 years and older or 1,103,000 employed aged 15 - 64 years, were employed until October 2008.

An important role in employment after the 90's, has played the agricultural sector. While the agricultural and non-agricultural private sectors are growing, the public sector is significantly reduced and it is most represented by employment in the local and central administration. According to figures from official sources of information in Table 2, show the evolution of employment after the collapse of 1997.

**Figure 2: Employment level (1997 – 2010)**



Source: INSTAT: 2012

Referring to the above data, we see that the trend of employment has been declining for the period 1997-2010. This reduction of the level of employment is justified by the reforms in order to increase the efficiency and to improve the service of the public administration, where the number of employees in the public sector has continued to pursue a slight downward trend, while the average wage has grown steadily. In the non-agricultural private sector, employment has followed a downward trend throughout the survey period 1997 - 2010, while the private agricultural sector trend has been the same as in the public sector.

We cannot leave without mentioning the informal employment, for which there are no accurate sources of information, but which is really important for the economy as a whole, as well as for families in particular, although it covers forms of work that are outside the formal systems of labor protection and outside the official social security system. Informal employment varies considerably from sector to sector, but the highest concentration is in the construction sector. High level of informality are noted in the private agricultural sector, especially among the self-employed or employees free of charge. In industry, employment is divided equally among formal and informal sector. In this sector, informal employment is characterized mainly by the paid unregistered work. Informality is more prevalent among men, young adults and individuals with low levels of education. Paid employees in the informal sector work much more hours than employees in the formal sector and the informal sector wages are lower than wages in the formal sector, especially when considering the working hours. Informal employment is closely linked to poverty and low income, and constitutes a significant portion of employment according to official sources of information.

#### **4. POVERTY CHANGES IN ALBANIA**

Poverty is almost related to incomes of people which are gained by different sources. The most important source for the income generation in Albania, is wage employment. Wages, as an important element of the labor market, have undergone different changes. Before the 90's, the level of wages in Albania was the lowest in Europe. The economic crisis in the early 90's worsened the situation. Market reforms were applied, in order to stimulate the economic growth. Restrictive policies on income were an important part of this program, which aimed to limit the inflation. Real wages fell by almost 50% during 1991-1993. In 1992, for the first time, the wage was linked to the consuming price index and was determined

the minimum wage. The justification of the minimum wage law, is the protection provided to low-paid workers. This policy tool must be particularly important in developing countries during periods of rapid adaptation to the global economy. But, in periods when the global competition is very strong, many policymakers argue for reduction, even and the elimination of minimum wages and other rules of the labor market in developing countries. These are in order to allow more flexibility and an increased competition. The main argument is that the lack of flexibility in the labor market, such as the lack of flexibility in the wage established by the minimum wage, can slow down the creation of jobs and thus contribute to unemployment and poverty (Kowa, Micco & Pages, 2004).

In general, there are certain criteria that are more commonly used for determining the minimum wage. Among the criteria used in our country are: social and moral criteria, e.g. needs of workers; demand and supply in the market for not having much deviation from other companies of the same type; solvency of employers who are part of the microeconomic and macroeconomic requirements related to the economic development of a country.

The minimum wage in Albania has economic consequences that can be considered from two points of view. First, the government's efforts to raise the minimum wage will lead to unacceptable decline in formal employment since employers generally prefer not to pay higher wages, because it would lead to increased labor costs. An increase in the minimum wage would result in discouraging employers for the creation of new jobs, in reducing the workforce paid formally and increasing informal employment. At the same time it would increase the public spending to compensate unemployment. Secondly, the economic consequences caused by the minimum wage are closely related to the workers standard of living, as by the increase of the minimum wage would benefit only those who are paid with this wage, while those who are paid little more than the minimum wage, could not improve their standard of living because they will not benefit the wage increase.

Poverty and inequality in Albania are calculated with the measurements based on consumption. There exists a large consensus regarding the advantages of the usage of measure based on consumption, especially for a rural economy and widely informal such as that of Albania. As main resources of information in this part, serve the survey for measuring the living standards level for the years (LSMS) 2002, 2005 and 2008. During the years 2002, 2005 and 2008 in Albania

there were organized a Living Standard Measurement Survey (LSMS) by INSTAT Albania with the assistance of World Bank.

The first LSMS was conducted in 2002 on a sample 3,600 households based in 2001 Population and Housing Census. In 2005 was the second survey following the same methodology and the third was in 2008. From the data processed for LSMS in the year 2002, the absolute poverty line was estimated equal to 4891 ALL per capita per month; the food poverty line has been 3047 ALL per capita per month. For 2005 and 2008 are the same absolute poverty line and the food poverty line. The percentage of population in Albania, the real consumption per capita per month of which it is under the poverty line, fell from 25.4% in the year 2002 to 18.5% in 2005 in 12.4% in 2008. The population with the highest percentage of poor people is concentrated more in the rural areas. Between 2002 and 2005 there has been a reduction of the percentage of poverty respectively 38.6% in the urban areas and 18% in the rural areas. For the period 2005-2008 this reduction was higher in the rural areas than in the urban areas, respectively 39.7% rural area and 17.7% urban area. An important point of poverty trends is the share of poor comparing with the share of the population.

According to these data, we can note the correlation of the poverty changes with the Albanian economic growth and employment. In the areas with the highest employment rate growth, we note better the poverty reduction.

The increase in the education expenditures and shares of real per capita consumption in 2008 and the decrease in food shares of real per capita consumption indicate a higher quality of life in Albania. Once certain satisfactory levels of consumption are reached, food shares of the per capita consumption are expected to decline, since once food requirements are satisfied, individuals will use the extra income for other activities.

## **5. CONCLUSION**

Promoting employment is a complex challenge for every government for the creation of new jobs. This is a phenomenon that involves many sectors and that includes mutually applicable policies in a number of areas. Sound macroeconomic policies and favorable business conditions are essential elements for economic growth that is needed to promote employment. The private sector can reduce poverty by contributing to economic growth, creating new jobs and increasing incomes of poor people. It can also empower the poor by providing a wide range

of products and services at lower prices. Small and medium enterprises can be engines of creation of new jobs, incubators for innovation and entrepreneurship.

The state has the responsibility to create the conditions that make possible the provision of adequate financial resources for investment. These conditions, such as: the state of governance, macroeconomic and microeconomic policies, public finance and other elements based on the economic environment of a country, are placed in a large-scale by national policymakers. Their challenges must be advances in macroeconomic stabilization and the undertaking of reforms that bring about further changes in the institutional framework to assist the growth and development of the private sector. We highlight the importance of attaining macroeconomic stability and obtaining an adequate social protection network as pre-conditions to growth and poverty reduction.

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