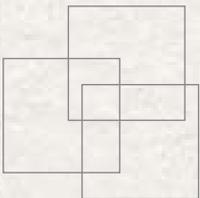
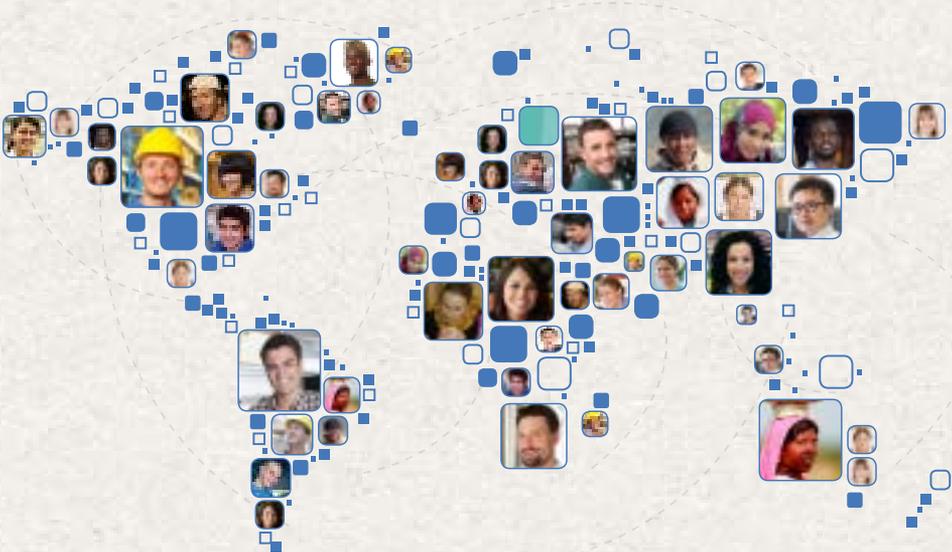




International  
Labour  
Office

# JOBS AND SKILLS FOR YOUTH: REVIEW OF POLICIES FOR YOUTH EMPLOYMENT OF THE RUSSIAN FEDERATION





# **JOBS AND SKILLS FOR YOUTH:**

REVIEW OF POLICIES FOR  
YOUTH EMPLOYMENT OF  
RUSSIAN FEDERATION

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# FOREWORD

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This review of the youth labour market in the Russian Federation and of the policies and institutions for youth employment is part of the work that supports the ILO member States in collecting information on, and analysing, the effectiveness of country policies and programmes, including those undertaken through voluntary multi-country peer reviews. More specifically, it is part of one of the areas of collaboration between the ILO and the government of the Russian Federation that revolves around the provision of technical support to address youth employment issues.

The review was conducted by the International Labour Office between 2013 and 2014 with the purpose of serving as an assessment of the current situation and supporting the development of a National Action Plan for Youth Employment.

This report was prepared by Valli' Corbanese and Gianni Rosas. Gratitude is expressed to Ms Olga Koulaeva, Senior Employment Specialist of the ILO Decent Work Team and Country Office for Eastern Europe and Central Asia for leading the youth employment consultations and the fact-finding missions of the ILO to the Russian Federation in 2012 and 2013. The valuable inputs and comments of Ms Alena Nesporova are acknowledged with thanks. Appreciation is expressed to the team of the University of Moscow, led by Ms Tatjana Razumova, for the collection of statistical data and the drafting of a background paper that was the starting point for the in-depth analysis.

Many thanks go to the officials of the Employment Department of the Ministry of Labour and Social Policy, as well as the representatives of other Federal Ministries and Agencies who contributed information and data to enrich the content of this report.



# EXECUTIVE SUMMARY

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This report reviews youth labour market developments in the Russian Federation over the past few years and assesses existing policies and programmes for youth employment. It suggests a number of short- and medium-term measures that the government may consider in its endeavours to tackle the youth employment crisis. The main messages stemming from the review are briefly highlighted in this executive summary.

*In the decade leading up to the 2008 crisis, the Russian Federation witnessed strong economic growth, increasing productivity and real wages, together with declining unemployment and poverty rates. Economic growth in the period 1999-2008 averaged nearly 7 per cent on an annual basis, while labour productivity increased at an average of 5.2 per cent. In the period 2001-2008, the country enjoyed macroeconomic stability with decreasing inflation and a series of current account and budget surpluses. The business climate improved thanks to reforms in the tax regime, the introduction of banking and competition policies and bankruptcy legislation. Fiscal policy was prudent, with windfall revenues stemming from oil and gas production saved in the Stabilization Fund.*

*Wealth however, remains unevenly distributed across both regions and population groups. The GDP per capita of the richest region remains 20 times that of the poorer region, while children (up to 16 years old) and young people (between 16 and 30 years old) account for half of the poor. Since 1998, absolute poverty has fallen significantly, while relative poverty has decreased only marginally, leaving behind a relatively large number of working poor (over 13 per cent of total employment in 2011) and low-paid workers (nearly 29 per cent). The relatively high costs of resettling in fast-growing areas still hinders workers from moving across regions in search of better employment and earning opportunities, while the convergence of incomes across regions recorded since the early 2000s makes income differentials less attractive.*

*Strong economic growth during the period 2001-2008, coupled with a decreasing working age population, led to significant improvements in the Russian labour market, which benefitted mostly adult workers (25-64). In the period 2001-2008, the labour force participation and the employment rate of the working age population increased, while*

unemployment decreased. Such positive employment developments also spilled over to the youth (15-24) labour market. The number of young people participating in the labour force increased (from 40.8 per cent to 43.1 per cent) as did employment (from 33.7 to 37 per cent), while youth unemployment rates declined (from 18 to 14.1 per cent). However, in relative terms, the labour market gains made by youth were much lower than those recorded among adult workers (25-64 years old). The youth-to-adult unemployment rate ratio actually deteriorated (from 2.3 in 2001 to 2.7 in 2008) and youth employment growth was twice as slow (3.5 percentage points for youth and 6.3 percentage points for adults). Even more importantly, working conditions among young workers did not improve, with young Russian workers increasingly exposed to low-paid work, atypical forms of employment, underemployment and persistent high levels of informal employment.

*The impact of the global economic crisis in the Russian Federation was severe in terms of output decline, but relatively mild in terms of job losses, with young people taking most of the brunt.* The crisis affected the Russian economy mainly through the trade channel and declining oil and commodity prices. In 2009, output growth declined by nearly 8 per cent of GDP, driven by contracting domestic demand. The large stimulus package deployed by the Russian Government (amounting to 6.7 per cent of GDP) managed to mitigate the negative impact of the economic crisis. Employment losses and unemployment surges were contained, as the labour market adjusted mostly through cuts in working hours and wages. In 2009, the employment-to-population ratio of the working age population dropped by less than 2 percentage points, while the unemployment rate increased from 6.3 per cent to 8.4 per cent of the labour force. In the span on just one year, the total number of hours worked declined by 5.5 per cent, while real wages decreased by 4 per cent..

*The distribution of young workers in economic sectors and occupations most affected by the downturn and the segmentation of the Russian labour market explain the larger job losses experience by youth.* Between 2008 and 2009 youth employment levels decreased by 10 per cent (compared to 1.2 per cent for adults), while the unemployment rate increased by 4.5 percentage points (1.8 percentage points for adults). This was caused by the drops in employment in the manufacturing (20 per cent), construction (20 per cent) and other service sectors (13.5 per cent) that had large numbers of young people employed. Similar to what occurred in OECD countries, the sectoral and occupational distribution of

youth employment also explains the higher employment losses of young men compared to young women and of urban workers compared to rural ones. The wider incidence of flexible contractual arrangements (service and fixed term contracts) and of informal employment among youth also played a role in their higher exposure to declines in labour demand. The combined analysis of data on informal employment, labour turnover and shift among labour market statuses points to a duality between formal (first-tier) and informal employment (second-tier) and a higher exposure of young people to the negative effects of labour market segmentation (wage gaps, lower access to training and social security, poor working conditions and tenure and limited opportunities to move to better jobs).

*Young people are more exposed than adults to working poverty, low-paid work and informal employment.* Although data disaggregated by age-group are not available, the concentration of youth employment in economic sectors that are more affected by working poverty and low-paid work (agriculture, trade, manufacturing and construction) makes one suspect that many young workers fall under these two categories, also taking into account the 15 per cent wage gap between young and adult workers. In 2012, the number of young people (between the ages of 15 and 24) employed in informal enterprises was 24.4 per cent (while it was 17.1 per cent for workers aged between 15 and 64). This share, however, does not include young individuals working under informal arrangements in formal enterprises nor those receiving part of their salary as envelope wages. Adding these two categories would increase the youth informality rate to approximately 50 per cent of total youth employment.

*Education and training pays a premium in the labour market and has a positive impact on the school-to-work transition, but does not protect against and over-qualification.* Educational attainment in the Russian Federation is high and has increased across generations. Educational achievement is positively related to labour market outcomes, as young people with lower educational attainment are more likely to be unemployed compared to youth with vocational and higher education. Young university graduates, however, have roughly the same probability of being unemployed as young people with initial and secondary vocational education. The coexistence of relatively high youth unemployment rates among graduates and employers reporting skills shortages suggests a significant mismatch in the demand and supply of skills. In part, this situation reflects a misalignment of higher educational outcomes with the requirements of an economic system still characterized by a relatively large

share of non-competitive firms able to survive in the market thanks to low wages, poor working conditions and outdated production assets. Having a tertiary educational attainment pays a wage premium (37 per cent higher wages compared to youth with basic education) and eases the transition to a stable and satisfactory job. Such returns, however, are undermined by high rates of over-qualification among young university-educated workers (38.8 per cent) and the prevalence of employment in occupations exposed to high job turnover, atypical forms of employment and lower wages (service and sales workers, crafts and workers in elementary occupations).

*The economic recovery – albeit at lower growth rates compared to the pre-crisis period – increased employment and brought unemployment to its lowest level in two decades. The effect of the recovery on youth employment, however, has been marginal.* In the period 2010-2012, the employment-to-population ratio for the working age population increased from 67.3 to 69 per cent, while the unemployment rate decreased from 7.4 to 5.5 per cent. Most of these gains, however, benefitted adults, as youth employment actually decreased (from 34.2 to 33.7 per cent) and the youth unemployment rate remained slightly higher than in the pre-crisis period (14.4 per cent in 2007 and 14.8 per cent in 2012). This may point to the fact that a part of youth unemployment has become structural (hysteresis). Capacity utilization is at 80 per cent, the same rate recorded prior to the economic crisis, when the economy was growing at over 7 per cent annually. This, together with adult unemployment at a record low, indicates that one means for the Russian Federation to exceed potential is to tap the pool of youth who are neither in employment nor in education and training (NEET), estimated at 12 per cent of the youth population in 2012.

*Tackling youth employment issues in the Russian Federation calls for the development of a national action plan for youth employment that addresses both its cyclical and structural nature.* The youth employment issues the Russian Federation faces require integrated and coherent strategies that address employment as a priority objective of economic and social policy and include explicit targets and policy outcomes for youth employment. A national action plan on youth employment – linked to the National Programmes developed under the long-term economic policy of the new administration – could provide the means to ensure coherence between the youth employment interventions contained in the various economic and social policies and identify clear and measurable outcomes to be achieved in a specific timeframe. Such an integrated framework

would promote action to: (i) increase the youth employment content of macroeconomic policies; (ii) support private sector development and especially small- and medium-size enterprises that have the potential to increase the demand for youth labour; (iii) enhance the relevance of education and training to labour market requirements, particularly through broader specializations and the inclusion of work-experience components; (iv) address labour market segmentation and improve workers' protection; and (v) improve the range and scope of employment services and active labour market programmes, so that they address the specific barriers that young people face in entering and remaining in the labour market. Such an action plan would play the important role of fostering inter-institutional coordination, by bringing together the various actors with a stake in youth employment, including representatives of employers' and workers' organizations.

*The employment-content of economic and fiscal policies could be increased without undermining macroeconomic stability by expanding the tax base, reducing the “regressivity” of the tax system and improving the efficiency of social spending.* Since the jobs gap stemming from the crisis has been largely closed in the Russian Federation, a decline in youth unemployment will require actual growth to exceed potential. The fiscal stance that the Russian Federation appears to be embarking upon is one of moderate, back-loaded fiscal tightening. For such a policy to succeed, it is necessary that credible structural reforms (on the investment climate, competition, trade liberalization, human capital and infrastructure development) become an integral part of the adjustment package. To maintain the fiscal deficit within the projected range, a redistribution across revenue and expenditure items is needed, with a focus on improving the efficiency of the respective systems, on the one hand, and balancing revenue and spending measures, on the other. On the revenue side, an expansion of the tax base and a more progressive tax regime would improve equity as well as the operation of the tax system as an automatic stabilizer. A better ratio of direct to indirect taxation would reduce the regressivity of the tax system, which places a larger burden on lower income earners. High taxes on salaries contribute not only to higher unemployment, especially among youth, but also to lower participation in the labour market, while the size and quality of the labour supply are key determinants of the competitiveness of the economy. On the expenditure side, the full phasing out of enterprise subsidies, combined with measures to improve the efficiency of social spending could open some space to increase investment for the modernization of infrastructure.

The effectiveness of the social protection system could be improved by streamlining and simplifying existing social protection programmes and enhancing targeting. Finally, the existence of a flat unemployment assistance benefit offers the opportunity to introduce an activation system for young jobseekers, whereby eligibility for unemployment assistance is conditional to active job searching and participation in active labour market programmes.

***The acceleration of reforms to foster private sector development would boost the demand for labour as well as improve the quality of jobs.*** A further improvement in the business environment – including the strengthening of competition rules, the simplification of administrative procedures and the improvement of the judicial system – would boost potential returns in the private sector, shift investment towards high value-added sectors and ease the reallocation of resources from unproductive to productive enterprises. This would provide good ground for the creation of more and better jobs. Strategies to increase the level of employment among young people are not likely to work unless enterprises invest in young people. It is by improving competitiveness and supporting investment in dynamic sectors that enterprises can maximize their capacity to create decent jobs. Policies that offer fiscal incentives, support the development of infrastructure, invest in research and development and provide enabling regulations for enterprises operating in competitive sectors with high youth employment elasticity can generate significant demand for labour in the medium to long term. Similarly, incentives granted to enterprises to provide training and work experience to young people can have a significant impact on easing the transition from school to work.

***Maintaining the country's competitive edge requires that the relevance of the education and training system be improved and that skills development opportunities be expanded to ease the transition of young people to decent jobs.*** The education reforms carried out to date have attempted to address both the quality and relevance of the education and training system. Some of the measures implemented, however had unexpected consequences. For instance, the financing mechanism reinforced – rather than levelled out – regional differences, with better-endowed regions and schools receiving more funds than those lagging behind. Similarly, the Unified State Exam, while attempting to improve the monitoring of educational outcomes, has created perverse incentives for teachers to focus on curriculum requirements, rather than on the capacity of students to apply the knowledge gained. Better cooperation

with enterprises, the revision of specializations on the basis of up-dated standards and the introduction of work experience as part of the curriculum would improve the alignment of education outcomes to enterprise requirements and reduce skills mismatches. On the labour demand size, measures are needed to increase innovation, business sophistication and the technological readiness of enterprises in general, so that the talent of highly-skilled youth can be maximized. The 2012 reform of the education and training system will yield labour market gains only in the medium to long-term. In the short term, the expansion of subsidized skill development programmes, apprenticeship and internship programmes would improve employment prospects for young workers with inadequate skill levels, address the erosion of competencies resulting from long unemployment spells and ease the transition to jobs of first labour market entrants. Promoting lifelong learning and training opportunities would foster enterprise competitiveness and enhance labour productivity, as well as improve job quality. As enterprises invest mostly in training workers with already higher skills, incentives to increase the human capital of low-skilled workers are warranted.

*A better balance between labour market flexibility and workers' protection may prove successful to address the duality of the Russian labour market.* During the last decade, employment protection legislation (EPL) has shown an easing of rigidity, owing to reforms in labour legislation. The incidence of temporary contracts has been increasing, with young people more exposed to these employment forms. The labour market data confirm the duality of the Russian labour market, i.e. one for “insiders” with stable, formal employment and security of tenure and another for “outsiders” who tend to be trapped in short-term and informal jobs with precarious attachment to the labour market. This second-tier market is the one that took the brunt of the economic crisis. Such differences in the levels of protection occur when EPL reforms are carried out at the “margins”, i.e. by increasing labour market flexibility mainly through the liberalization of temporary contracts, and when enforcement is weak. Such a situation calls for measures to review the current legislation in order to strengthen the protection of workers in atypical forms of employment, encourage enterprises to formalize, and for interventions aimed at strengthening labour inspection and the sanction system for non-compliance.

*Well-designed, properly targeted and adequately financed active labour market measures would facilitate young people's entry and re-*

***entry into the labour market.*** The GDP share invested in active labour market policies is still well below the average of OECD countries (0.3 and 0.6 per cent of GDP, respectively). As a consequence, the range and scope of active labour market programmes is rather limited. The current design, targeting and funding mechanisms appear to be ill-suited to a labour market situation characterized by youth unemployment rates that are three times those of adults. Funding allocations based on forecasted unemployment levels at district level fail to take into account the specific risk factors faced by the young unemployed and may limit the capacity of local employment offices to adjust the intensity of employment assistance according to the needs of the most vulnerable unemployed people. The types and coverage of programmes currently available – mainly public works and rather costly training programmes – fail to recognize the importance of work experience in the recruitment decisions of enterprises. Programmes that help the young unemployed gain this experience (such as the internship programme currently on offer) needs to be scaled-up and new ones (such as apprenticeship and traineeship) designed. The fact that placement rates of training programmes for young school leavers have increased over time, also due to the job guarantee attached to them, confirms the findings of impact evaluations carried out in a number of countries: multi-component interventions that combine training with work-experience programmes and job-search assistance, as well as incentives for employers to hire young workers, have demonstrated to be more cost-effective than single measures. Finally, monitoring and evaluation should be carried out regularly to assess the effectiveness and impact of active labour market programmes. A system to monitor both quantitative and qualitative indicators could help in assessing the performance of interventions targeting the young unemployed and in determining what works and for whom. The lessons learned from systematic impact evaluation would help to improve the cost-effectiveness of the measures taken and would provide policy-makers with information on how to optimize the use of the available funding.

***Modernising the delivery of employment services could help prevent long-term unemployment, bridge the regional divide and promote the inclusion of youth most at risk.*** The provision of employment services should be reviewed with the objective of offering a set of standard services to all young people and more intensive assistance to disadvantaged youth. Early interventions based on profiling techniques and outreach programmes should be developed at the local level to make the services more relevant to young people. Partnerships between employment offices and local

actors (municipal authorities, social services and community-based organizations) are required to improve service provision to those young people who are neither in employment, education nor training (NEETs), but are available to work, and to motivate them to actively search and take up jobs. As relocation assistance is one of the services to be deployed to increase labour mobility across regions, its design features would need to take account of the findings of international research, which shows that regional differentials in the ratio of house prices to earnings are the single most important determinant of regional migration flows, together with labour-related income differentials and regional labour demand growth. A key challenge for the employment service is to overcome the stereotype that the employment service deals only with low level jobs and to increase its penetration of the vacancy market and the coverage of unemployed youth (currently at only 16 per cent of all young unemployed). This will improve the functioning of the labour market and allow the employment service to capture better job vacancies for the registered unemployed. In this regard, the use of information and communication technologies has emerged in many countries as key tools to improve service delivery to employers.



## 1

OVERVIEW OF THE ECONOMIC  
AND SOCIAL CONTEXT

## 1.1 Macroeconomic framework

The initial years of transition to a market economy in the Russian Federation were characterized by falling output, soaring inflation rates and weak oil prices. Since the end of the 1998 financial crisis – which was marked by the collapse of the fixed exchange rate regime and a partial default on government debt – the country experienced a decade long of real Gross Domestic Product (GDP) growth, decreasing inflation, appreciation of the national currency and improved fiscal and balance of payment positions. The decade leading up to the global economic crisis of 2008-2009 saw increases in real wages and falls in unemployment and poverty rates. State finances improved markedly, with a sequence of budget balance surpluses and declining public debt (Table 1.1).

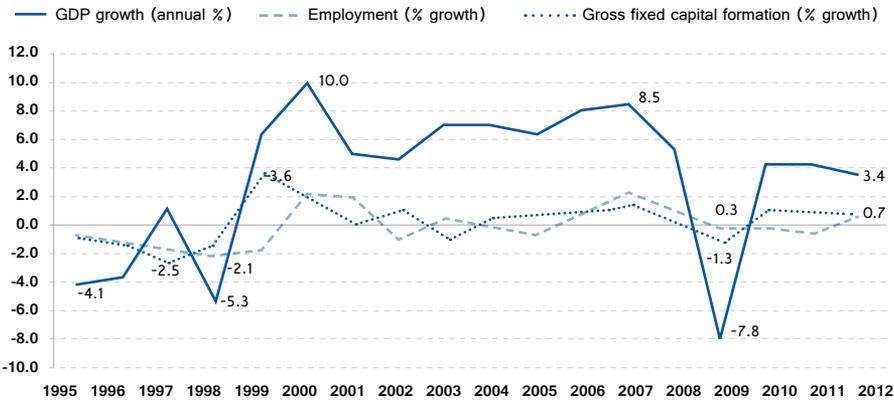
**Table 1.1. Key macroeconomic indicators, Russian Federation, 2002-2012**

	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
Real GDP growth rate	4.7	7.3	7.2	6.4	8.2	8.5	5.2	-7.8	4.5	4.3	3.4
Gross fixed capital formation (% GDP)	17.9	18.4	18.4	17.8	18.5	21.0	22.3	22.0	21.6	21.6	22.0
Central government balance (% GDP)	0.7	1.4	4.9	8.1	8.3	6.7	4.9	-6.3	-3.4	1.5	0.4
Central government debt (% GDP)	40.3	30.3	22.3	14.2	9.0	8.5	7.8	11.0	11.0	11.7	12.5
External balance (% GDP)	10.8	11.4	12.3	13.7	12.7	8.6	9.2	7.4	8.1	8.6	7.3
FDI net inflow (% GDP)	1.0	1.8	2.6	2.0	3.8	4.3	4.5	3.0	2.8	2.9	2.5
Government consumption (%GDP)	18.0	17.9	17.0	16.9	17.4	17.3	17.8	20.8	18.7	17.9	18.6
Household consumption (% GDP)	51.2	49.9	49.9	49.4	48.7	49.9	47.4	52.8	50.6	48.0	48.0
Exports (% GDP)	35.2	35.2	34.4	35.2	33.7	30.2	31.3	27.9	29.2	30.3	29.4
Imports (% GDP)	24.5	23.9	22.2	21.5	21.0	21.5	22.1	20.5	21.1	21.8	22.1
Current account balance (% GDP)	8.4	8.2	10.1	11.1	9.6	6.0	6.2	4.1	4.4	5.1	3.7
Inflation (y-o-y % change)	15.8	13.7	10.9	12.7	9.7	9.0	14.1	11.7	6.9	8.4	5.1

Source: World Bank, economic and social data at <http://data.worldbank.org/indicators>; OECD, *Economic Survey of the Russian Federation, 2011*; IMF, *World Economic Outlook database*.

Economic growth was fuelled by the developments of the oil industry and increases in world commodity prices that improved the country's terms of trade and expanded domestic demand. Economic growth in the period 1999-2008 averaged nearly 7 per cent annually, well above the 2.4 per cent average growth recorded in OECD countries. Output expanded despite fixed capital investment rates that, at around 20 per cent of GDP, were lower than those recorded by other fast-growing economies (30 per cent of GDP and over).<sup>3</sup> Figure 1.1 below shows the limited contribution of fixed capital formation and labour (employment between 1999 and 2008 increased by an average of 0.9 per cent per year) to GDP expansion. The correlation between changes in GDP and employment dynamics in the Russian Federation has been weak since the early years of transition, both in periods of recession (1991-1998) and recovery (1999-2008). For instance, between 1991 and 1998 GDP decreased by about 40 per cent, while employment declined by 13.5 per cent (i.e. each percentage point of output contraction was accompanied by approximately 0.35 per cent employment reduction).<sup>4</sup>

**Figure 1.1. Gross Domestic Product (GDP), employment and capital investment growth, 1995-2012**



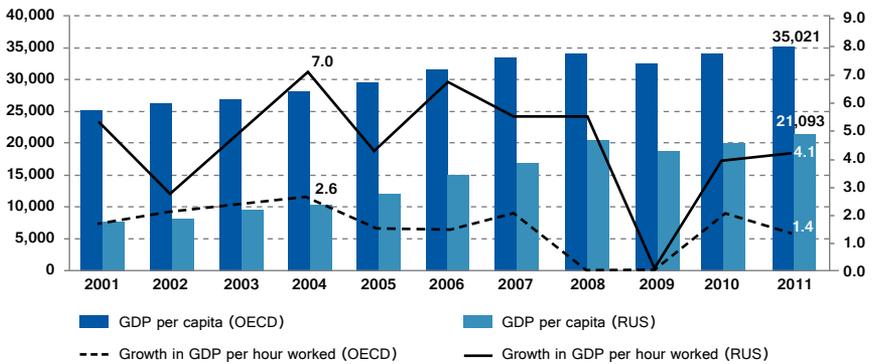
World Bank, *Economic and social indicators*, at <http://data.worldbank.org/country/russian-federation>; Employment-to-population ratios are for individuals 15+.

<sup>3</sup>OECD, *Economic Surveys: Russian Federation 2009*, Paris, 2009

<sup>4</sup>Kapelyushnikov R., Kuznetsov A., Kuznetsova O., "The role of the informal sector, flexible working time and pay in the Russian labour market model", *Post-Communist Economies*, Vol. 24, June 2012.

Labour productivity, measured as growth in GDP per hour worked, increased in the period 2001-2008 at an average of 5.2 per cent annually, well above the 1.7 per cent recorded in OECD countries.<sup>5</sup> Despite a three folds increase in the same period, GDP per capita remained at two thirds of the OECD average (Figure 1.2.). The overall labour productivity gap with OECD countries persists in economic sectors such as construction, real estate, wholesale and retail trade, machinery and equipment, as well as mining.<sup>6</sup>

**Figure 1.2. Labour productivity and GDP per capita, 2001-2011**



Source: OECD, Statistical abstracts, downloadable at <http://stats.oecd.org/>

Macroeconomic stabilization, prudent fiscal policies, the improvement of the business climate and increasing commodity prices all contributed to output expansion. Growth, however, was unevenly distributed across regions and economic sectors. Higher growth was recorded in the non-tradable sectors (construction, finance and wholesale and retail trade), while the tradable sectors (especially agriculture and industry) increased at a more modest pace.<sup>7</sup>

Since the early 1990s, the economic structure of the Russian Federation has shifted from a prevalence of heavy industry to services, thus converging towards the average economic structure found in OECD countries. Since 1992, the service sector has been increasing its value added to GDP from less than 50 per cent to over 60 per cent, while the value added of agriculture decreased from over 7 per cent to around 4 per cent.

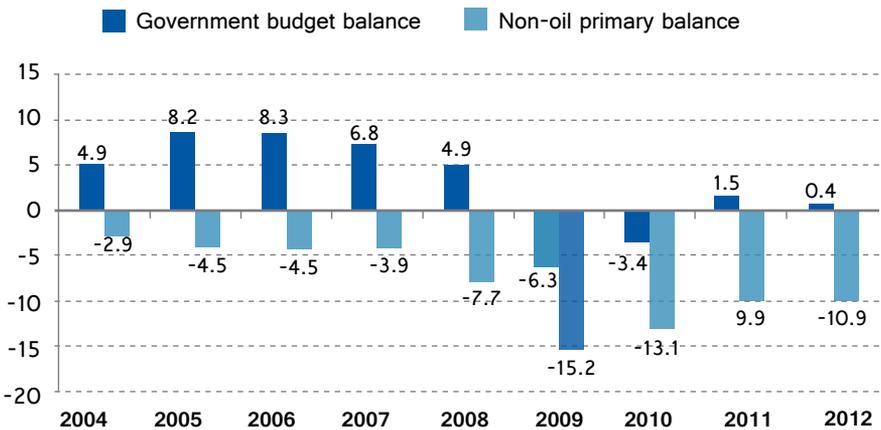
<sup>6</sup>For a detailed analysis of labour productivity gaps, see World Economic Forum, The Russia competitiveness report 2011, Geneva, 2011

<sup>7</sup>Between 2003 and 2008, average annual growth was 1.5 per cent in agriculture, 4.3 per cent in industry, 11.6 per cent in construction, 9.6 per cent in wholesale and retail trade and 12.4 per cent in financial intermediation and real estate, see OECD Statistical database at <http://stats.oecd.org/>.

The value added of industry has been more volatile, albeit on a decreasing trend since 1992 (from over 45 per cent to less than 36 per cent of GDP in 2010). The other large shift was the rapid rise of GDP generated by the private sector (from less than 40 per cent to approximately 70 per cent). Starting from 2004, the private sector share in GDP declined slightly (to 65 per cent) due to increasing public holdings in the energy sector.

In the 2000s, economic growth, the balance of payments and the government budget became increasingly reliant on oil and natural gas prices. The non-oil budget deficit, used as a proxy of the fiscal stance, started to widen sensibly in 2008 (Figure 1.3). Inflation also started to accelerate at the end of 2007 (12 per cent on an annual basis) driven by increasing household consumption.

**Figure 1.3. Government budget balance (percentage GDP)**



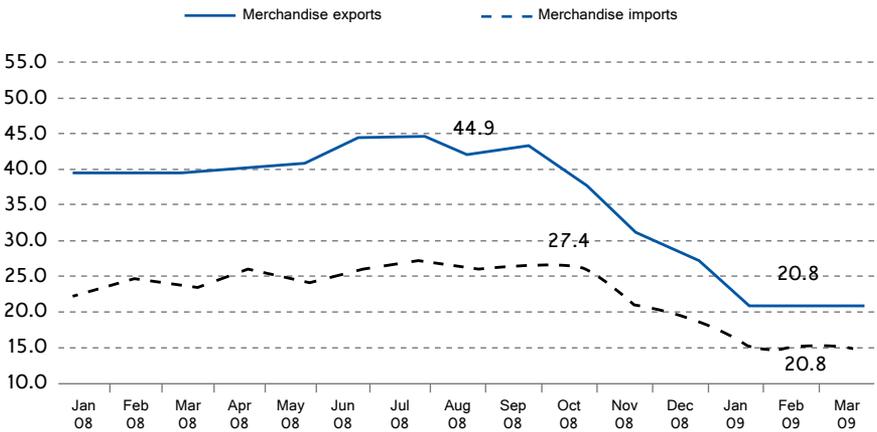
Source: OECD Economic Survey of the Russia Federation, Paris, 2014; IMF, World Economic Outlook database, October 2013.

The global economic crisis hit Russia in mid 2008. The culmination of asset price bubbles and decelerating bank lending in 2007, coupled with the unprecedented decline of oil and other commodity prices in 2008 – with oil and gas representing two thirds of Russian exports and generating roughly half of government revenues – caused a contraction of domestic demand and output growth. In 2009, the sharp decline of international trade, further aggravated by decreasing oil prices, led to a contraction

of GDP of nearly 8 per cent, well above the drop recorded in the EU27 and OECD countries (4.3 per cent and 3.8 per cent, respectively).<sup>8</sup>

Figure 1.4 shows the decline in the volume of merchandise exports and imports between July 2008 and February 2009 in the Russian Federation. Export volumes decreased by over 53 per cent and imports by nearly 47 per cent. As a consequence of decreasing world transactions, the trade-to-GDP ratio decreased from 53.2 in 2008 to 48.1 in 2009.

**Figure 1.4. Export and imports in US\$ billion, s.a., 2008-2009**



Source: OECD, *Economic Surveys: Russian Federation, 2009 op.cit.*

Output started to recover at the end of 2009, but the pace of GDP growth – roughly 4 per cent per year – has been slow compared to prior growth rates and despite increasing oil prices (see Table 1.1 at the beginning of the chapter). In 2010, economic growth was affected by the contraction of agricultural production, caused by adverse weather conditions, and the slow growth in construction and real estate. In the second half of 2011, the financial turmoil in the euro zone caused capital outflows and a weakening of the domestic currency.

<sup>8</sup>Real GDP growth (as compared to the previous quarter) was 0.8 per cent in Q2-2008, -1.2 per cent in Q3-2008, -4.3 per cent in Q4-2008, -4.7 per cent in Q1-2009 and -1.0 per cent in Q2-2009.

The Russian economy returned to pre-crisis growth rates in the third quarter of 2011 (5.3 per cent GDP growth compared to the same quarter of the prior year), mainly driven by recovering consumption (mostly private) and growth in the tradable sector. Growth in fixed capital investment, however, remained 3 percentage points below pre-crisis level, with Foreign Direct Investment (FDI) inflows also recording a subdued growth (2.8 per cent of GDP) compared to the 2008 peak of 4.5 per cent.<sup>9</sup> The overall government balance returned positive in 2011 (1.5 per cent of GDP). The non-oil fiscal deficit, however, remained at around 10 per cent of GDP.<sup>10</sup>

In 2012 economic growth decelerated to 3.4 per cent per year, despite oil prices that were near record levels. Growth slowed even more in the first half of 2013 (to 1.4 per cent), mainly due to weakening domestic demand, higher inflation, sluggish external demand and decreasing oil prices. In particular, the contribution of consumption to overall growth decreased from 4.8 per cent in 2012 to 3.4 per cent in 2013, despite low unemployment and real wages growth.<sup>11</sup>

## 1.2. Poverty and income distribution

Strong economic growth for almost a decade contributed to the reduction of the share of the population with an income below the subsistence level (from 27.5 per cent of the population in 2001 to 12.8 per cent in 2011)<sup>12</sup>. There was no significant increase in poverty during the economic slowdown of 2009, mostly due to the increases in pension payments and in the minimum wage level. In 2012, the share of the population living below the poverty line fell to 11 per cent, its lowest rate in two decades.<sup>13</sup>

Such growth, however, had a limited impact on relative poverty. This latter increased from 17 per cent in 1994 to 24 per cent in 2004, to then decline as of 2005. It is only in this latter year, in fact, that lower-income population groups started to make income gains compared to others, thus leading to a reduction of relative poverty.<sup>14</sup>

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<sup>9</sup>OECD, FDI in figures, Paris 2012, available at: <http://www.oecd.org/daf/internationalinvestment/FDI%20in%20figures.pdf>

<sup>10</sup>The non-oil balance excludes from the computation the revenues stemming from oil and gas,

<sup>11</sup>World Bank, Russian Economic Report. Structural challenges to growth become binding, Washington D.C., 2013

<sup>12</sup>The subsistence minimum level is established by law (Federal Law №134-FZ of October 24, 1997 “On subsistence minimum in the Russian Federation”). Since January 2013, the subsistence minimum is set at 7,306 roubles per month per capita (Federal Law № 233, 3rd December 2012 “ On Amending the Federal Law On the subsistence minimum in the Russian Federation”).

<sup>13</sup>Relative poverty measures the share of the population below 50 per cent of the median equivalised disposable income, while the poverty gap shows the deficit in income needed to reach the poverty threshold.

**Table 1.2. Income changes in the Russian Federation, in roubles, 2007-2012**

	2007	2011	2012 *
Median equivalised disposable income	9 309	15 603	17 032
Average income	12 540	20 780	22 880

(\*) Preliminary data

Source: Data of the All-Russian Living Standard Centre.

Income inequalities in Russia, as measured by the Gini coefficient, are above the average of OECD countries (0.42 and 0.31 in 2009, respectively). In the period 2001-2008 earnings inequality in Russia was higher than income inequality (see Table 1.3), due to the wage disparities recorded across Russian regions, which are determined by different costs of living.

**Table 1.3. Poverty and inequality in the Russian Federation, 2001-2011**

	2001	2003	2005	2007	2009	2011
Absolute poverty	27.5	20.3	17.7	13.3	13.2	12.7
Relative poverty (income-based)	21.0	23.0	16.0	17.0	13.0	...
Poverty gap	4.5	2.6	2.1	1.3	1.3	1.2
Gini inequality index	0.397	0.403	0.409	0.423	0.422	0.401
Gini coefficient (wage)	...	...	0.456	0.447	0.418	...

Source: I. Denisova, *Income Distribution and Poverty in Russia*, OECD, *Social, Employment and Migration Working Papers*, No. 132, 2012

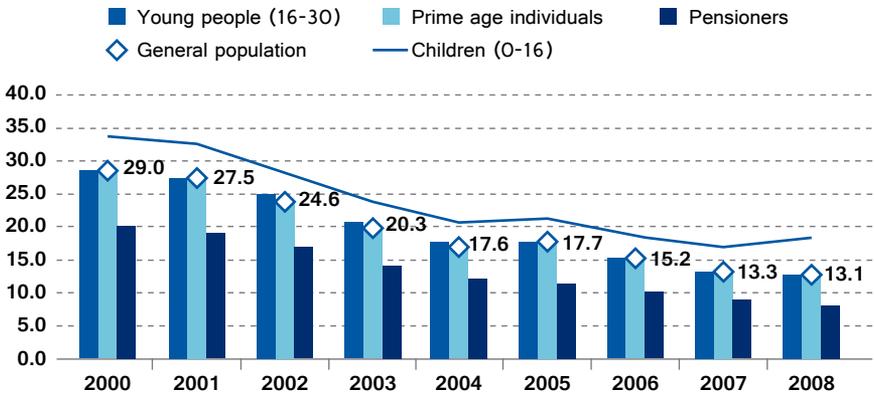
The factors that significantly reduce the poverty risk are labour market participation, the presence of pensioners in the households, engagement in subsistence farming and living in urban areas. Labour force participation and the presence of pensioners in the household have the largest poverty-reducing effect (20 percentage points). Unemployment increases the risk of poverty by 30 percentage points. Having a university degree also decreases the risk of being poor, but this effect has been decreasing over time. Research attributes this latter trend to wage growth in the informal economy of urban areas, where educational attainment pays a limited role.<sup>15</sup>

<sup>14</sup>Relative poverty measures the share of the population below 50 per cent of the median equivalised disposable income, while the poverty gap shows the deficit in income needed to reach the poverty threshold.

<sup>15</sup> OECD, *Review of labour market and social policies: Russia*, 2011, op.cit

Children up to 16 years of age are the most likely to be poor – they represented 26.3 per cent of all poor in the Russian Federation in 2011 – while young people (16 to 30 years old) show the same pattern of poverty probability of prime age individuals (see Figure 1.5), with women more likely to be poor compared to men.-(20.6 per cent and 18.6 per cent, respectively).

**Figure 1.5. Poverty profile of Russia, 2000-2008**



Source: OECD, *Review of labour market and social policies: Russia, 2011, op.cit.*

The share of working poor, e.g. individuals working but earning a wage below the subsistence level, was 13.1 per cent in 2011 (down from 16.5 per cent in 2007), with agriculture, education and other personal services being the sectors more exposed to working poverty. Another population group exposed to the risk of falling into poverty is that of low-paid workers, e.g. workers earning up to two times the minimum subsistence level (equal to 60 per cent of the average wage in 2011). This group accounts for 28.9 per cent of total employment.<sup>16</sup> Panel data on entry and exit from poverty shows that the working poor have lower chances to exit poverty compared to other groups. This points to the difficulty faced by low paid workers in increasing their income above the poverty threshold.

<sup>16</sup>The minimum subsistence level in 2011 was RUB 6,157.

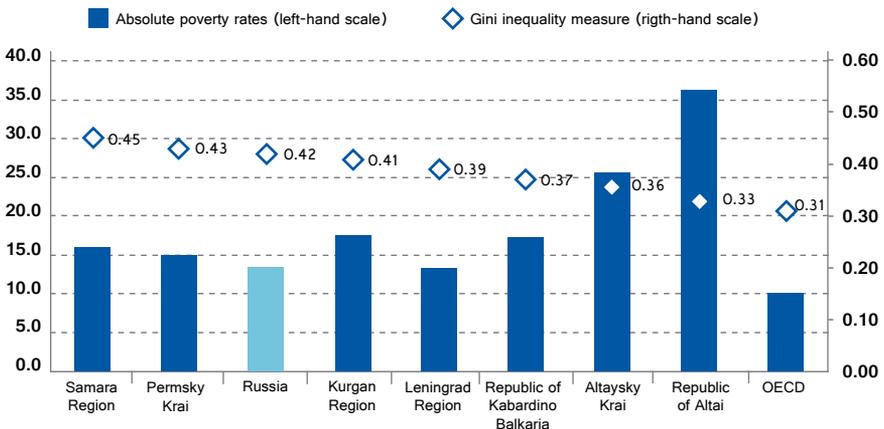
**Table 1.4. Working poor, Russian Federation, 1995-2011**

	1995	2000	2001	2002	2005	2006	2007	2011
Share of working poor	32.5	25.7	23.9	18.9	24.4	22.2	16.5	13.1

Source: Denisova, *Income Distribution and Poverty in Russia*, OECD, 2012, *op.cit.*

Inequality and poverty rates differ substantially across regions in the Russian Federation, given the large variation in per capita GDP, growth rates, wage levels and labour market outcomes (Figure 1.6). There are large differences across regions in activity, employment and unemployment rates due to unequal growth trends and concentration of jobs in the most prosperous regions. The rapid rise of the prices of oil and other natural resources contributed to widen the gap in regional output. By 2008, the per capita output of the richest region in the Russian Federation was 24 times the output of the poorest region. Income inequality, however, prevails in regions where economic growth is higher. The highest inequality index, compared to the national average of 0.42, is registered in Moscow (0.52) and the lowest in the Republic of Ingushetia (0.33), with 9 of the 83 entities of the Russian Federation having inequality indexes exceeding the national average.

**Figure 1.6. Inequality and poverty among selected Russian entities, 2009**



Source: I. Denisova, *Income distribution and poverty in Russia*, 2012, *op.cit.*; OECD, *Review of labour market and social policies in Russia*, 2011, *op.cit.*

Despite large regional differences in living standards and employment opportunities, internal migration is low and has been declining over time (from just over 3 per cent of the population in 1990 to 1.2 per cent in 2008).<sup>17</sup> As not all migrants register in the new place of residence, these figures are likely to be underestimated. Indeed, the school-to-work transition survey implemented in eleven entities of the Russian Federation in 2012 reveals that 16 per cent of young respondents (15 to 29 years old) changed their place of residence, mostly for family reasons (59.3 per cent) and education and training purposes (17.1 per cent). Only 9.5 per cent moved in search of better employment opportunities (12.5 per cent for young men and 6.5 per cent for young women).<sup>17</sup> There are a number of factors that may contribute to explain low internal migration flows, foremost the ability to afford the costs of settling in a fast-growing area and the difficulty to borrow the funds needed for migration.

Approximately 14 per cent of the total Russian migrants go abroad, mostly to countries of the Commonwealth of Independent States (CIS), e.g. Ukraine (hosting 31.9 per cent of the total Russian migrants stock in 2013), Kazakhstan (21.9 per cent) and Belarus (6.3 per cent). In 2013, young people aged 15-24 represented 10.2 per cent of the total stock of Russian migrants abroad.<sup>18</sup>

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<sup>17</sup>OECD, Review of labour market and social policies in Russia, 2011, op.cit; ROSSTAT, The demographic yearbook of Russia 2010, Moscow, 2011

<sup>18</sup>ILO, Labour market transitions of young women and men in the Russian Federation, Geneva, 2013 (forthcoming).

<sup>19</sup>United Nations, Department of Economic and Social Affairs, Trends in international migrant stock: Migrants by age and sex, United Nations database, 2013

# 2 THE YOUTH LABOUR MARKET

## 2.1. Socio-demographic characteristics of young people

The demographic figures of the Russian Federation show that in 2013 the population comprised approximately 143.3 million individuals (46.2 per cent men and 57.4 women), down from the 148 million recorded in 1990. The decline of the total population is the result of falling life expectancy at birth (74.2 years for women and 62 for men), due to high rates of mortality, especially among adult men; the low birth rates recorded as of the late 1980s (1.2 children per women); and international migration (with the stock of international migrants representing 7.6 per cent of the total population in 2013).

Demographic projections indicate that the population in the next decades will continue to decline and cause an increase of the old age dependency ratio (from 20 per cent in 2013 to 37 per cent in 2050). Such increase is lower than the projected rise of the old age dependency ratio in OECD countries (50 per cent in 2050). However, while in OECD countries the higher old age dependency ratio will be due to increasing shares of older people (and a relatively stable working age population), in the Russian Federation the changes are mostly driven by a decline in the working age population, estimated to drop by about 14.3 million individuals (equal to 14 per cent of the current working age population). The youth cohort (15-24 years old) is expected to decrease by 2.6 million individuals by 2050, while individuals in the age group 25-64 will decrease by approximately 11.6 million individuals.

**Table 2.1. Population estimates and projections, Russian Federation, percentage, 1990-2050**

	1990	2000	2005	2010	2013	2030	2050
0-14	23.0	18.1	15.2	15.2	16.1	15.7	17.3
15-24	13.3	15.9	16.8	14.6	12.2	12.3	10.5
15-29	21.3	22.9	24.4	22.9	20.9	17.7	16.4
15-64	67.0	69.6	70.9	72.0	70.9	65.1	61.8
65+	10.0	12.4	13.9	12.8	13.0	19.2	20.9
Old age dependency ratio (*)	17	20	22	19	20	33	37

(\*) Share of the population 65 and over on the total population aged 20 to 64 years old.

Source: United Nations Population Estimates and projections, [http://esa.un.org/wpp/unpp/panel\\_indicators.htm](http://esa.un.org/wpp/unpp/panel_indicators.htm)

Russia's demographic trends pose a number of unique education, labour market and social policy challenges. First, Russia has a history of rapid demographic changes, with large differences in the size of age groups from one period to the next. This characteristic of the Russian age structure requires flexibility in planning the delivery of education and employment services, in particular. Second, the unusual adult mortality pattern calls for increased efforts to improve the health of the population. Finally, fertility rates in the country could fall even further, if the ageing of fertility patterns follows the trends observed in Western Europe.

## 2.1.1 Trends in education

The educational attainment of the population of the Russian Federation is amongst the highest in the world.<sup>20</sup> Literacy rates are high for both men and women (99.7 per cent and 99.8 per cent, respectively), with no major difference between urban and rural areas (99.9 per cent and 99.5 per cent). The gross coverage ratio of primary and secondary (compulsory) education is also high, with 97.9 per cent of children aged 7-17 years old attending school.

The country made considerable progress in increasing the educational attainment between generations. In 2011, approximately 94 per cent of individuals aged 25-34 had attained upper secondary education,

<sup>20</sup> In 2011, Russia ranked 25th out of 139 economies on the indicator measuring the quantity of education calculated by the World Economic Forum Competitiveness Index, far ahead of Brazil (51st), China (96th), and India (108th).

compared to 91 per cent of the 55-64 cohort (the average for OECD countries is 82 per cent and 62 per cent, respectively), while 56 per cent of those aged 25-34 had tertiary educational attainment compared to 49 per cent of the age group 55 to 64 years old.<sup>21</sup>

Education data for young people aged 15-29 shows that in 2012 half of this age group had attained upper secondary education (34 per cent general and 16 per cent secondary vocational education) and 20.8 per cent had attained a higher education degree (higher professional or bachelor degree).<sup>22</sup> Young women are less likely to attend initial vocational education (9.3 per cent) compared to young men (15.3 per cent). Young women, however, perform better than men in higher education, with 24.8 per cent of them having attained a tertiary education degree compared to 16.8 per cent of young men (Table 2.2).

**Table 2.2. Educational attainment of youth (15-29), Russian Federation, 2012**

15-24 years old	Total	Men	Women
Less than basic education	1.9	1.8	2.1
Basic education	15.0	16.6	13.5
Secondary education	34.0	34.3	33.8
Initial vocational education	12.2	15.2	9.3
Secondary vocational education	16.0	15.3	16.6
Higher education	20.8	16.8	24.8

Source: Federal State Statistical Service (ROSSTAT), School-to-work transition survey, 2012

Due to the demographic decline registered in the period 2000-2010, the school-age population attending compulsory education decreased by 34 per cent (from 19.5 million to less than 13 million students). The re-organization of the basic education system that followed substantially reduced the overall number of basic education institutions (from over 66 thousands to just over 48 thousands). In the same period, the number

<sup>21</sup>In 2011, roughly 94 per cent of the adult population in the Russian Federation had attained at least upper secondary education (compared to 75 per cent in OECD countries) and over half the population had tertiary education (53 per cent compared to 32 per cent of OECD countries). The share of workers with tertiary educational attainment (51 per cent) is above that of many EU countries such as Finland (34 per cent), Germany (24 per cent) and Poland (20 per cent) and just below the United States (50 per cent). However, it has to be noted that most individuals with tertiary education have attended a level 5B educational stream. The share of workers with primary education only is around 7 per cent. OECD, Education at a glance 2013 (Russian Federation), Paris, 2013

<sup>22</sup>Federal State Statistical Service (ROSSTAT), figures of the Labour Force Survey (LFS), 2012.

of students attending initial vocational education and training (IVET) decreased by over 40 percent, whereas that of students attending secondary vocational education (SVET) dropped by approximately 10 per cent.<sup>23</sup> The number of students pursuing higher education nearly doubled in the period 1998-2010 (from 3.5 million to 7.1 million individuals) with increasing numbers of vocational school leavers enrolling into higher education.

The demand for higher education in the social field (education, art and humanities, social sciences, business and law) increased much faster than the demand for science subjects (natural science, engineering, agricultural disciplines, health care). Since 2000, the number of students applying to fee-based services (offered in the subjects that are most popular among students, but for which often there is lower labour market demand) had exceeded the number of students applying to state-funded places (which are made available on the basis of the prior year labour demand). Research estimates show that the returns to tertiary education rose from around 2-4 per cent before the transition to a market economy to 8-10 per cent in the early 2000s, which partly explains the increasing shares of youth enrolling into higher education and the expanding network of private education institutions. There are signals, however, that the labour market premium for workers with tertiary education is diminishing compared to individuals with vocational education. In 2012, in fact, the unemployment rate of youth aged 15-24 with higher educational attainment was above that of young individuals with secondary vocational education attainment (11.8 per cent and 10.4 per cent, respectively, see Table 2.3).

**Table 2.3. Youth (15-24) labour market indicators by education level, 2012**

15-24 years old	Labour force participation rate	Employment-to population ratio	Unemployment rate
Less than basic education	6.9	5.2	25.1
Basic education (grade 1-9)	12.4	9.4	24.7
Secondary education (grade 10-12)	24.6	19.6	20.3
Initial vocational education	86.5	76.7	11.3
Secondary vocational education	85.6	76.7	10.4
Higher education	88.7	78.3	11.8

Source: ROSSTAT, Labour Force Survey, 2012

<sup>23</sup>In 2010 the initial vocational education and training system was merged with secondary vocational education.

## 2.2 The youth labour market

Strong economic growth for almost a decade, coupled with a decreasing working age population, led to significant improvements in the Russian labour market. The figures of the Labour Force Survey (LFS) show that in 2012 most key labour market indicators, for both youth and adults, were better than those recorded in the EU27 countries (Table 2.4).

**Table 2.4. Key labour market indicators, by age group and sex, Russian Federation and EU27, 2012**

Age groups	Labour force participation rate	Unemployment rate	Employment to population ratio
<b>Total</b>			
15-64	73.0	5.5	69.0
15-24	39.5	14.8	33.7
25-64	80.7	4.4	77.1
EU27 (15-64)	71.8	10.6	64.2
EU27 (15-24)	42.6	22.8	32.9
EU 27 (25-64)	77.8	9.2	70.7
<b>Men</b>			
15-64	78.1	5.8	73.6
15-24	43.8	14.5	37.5
25-64	86.7	4.7	82.6
EU27 (15-64)	78.0	10.5	69.8
EU27 (15-24)	45.5	23.4	34.9
EU 27 (25-64)	84.9	9.1	77.2
<b>Women</b>			
15-64	68.2	5.1	64.7
15-24	35.1	15.1	29.8
25-64	75.3	4.1	72.2
EU27 (15-64)	65.6	10.6	58.6
EU27 (15-24)	39.6	22.0	30.9
EU 27 (25-64)	70.9	9.3	64.3

Source: ROSSTAT, Labour Force Survey, 2012 and EUROSTAT database at [http://epp.eurostat.ec.europa.eu/portal/page/portal/statistics/search\\_database](http://epp.eurostat.ec.europa.eu/portal/page/portal/statistics/search_database).

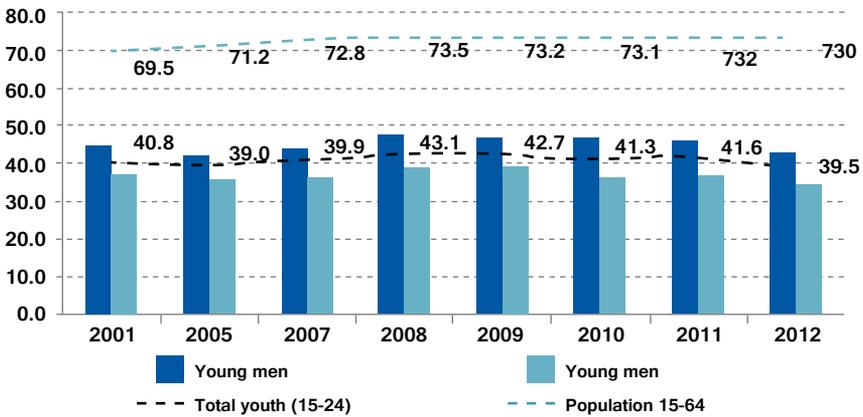
The labour force participation rate for the working age population (15-64 years old) increased from 69.5 per cent in 2001 to 73 per cent in 2012; while the employment-to-population ratio rose, in the same period, from 63.2 per cent to 69 per cent. The unemployment rate declined from the 13.2 per cent peak recorded in 1999 to 5.5 per cent in 2012, with long-term unemployment (i.e. the share of unemployed looking for work for one year or over) decreasing in the same period from 47 per cent to less than 31 per cent.

### 2.2.1 Youth labour force participation

In 2012, the youth (15-24) participation rate in the Russian Federation was 39.5 per cent, slightly lower than the participation rate recorded in the EU27 (42.6 per cent). Similarly to their European peers, young Russian men are more likely to be active in the labour market compared to women (43.8 and 35.1 per cent, respectively).

The labour force participation figures of the working age population show increasing activity rates in the period 2005 to 2008 to then flatten in the following years (Figure 2.1). The youth (15-24) labour force participation also increased in the same period, at a slightly faster pace for young men compared to women. The decline in youth activity rates recorded since 2009 was more pronounced for young women compared to men: young women's participation declined from 38.8 per cent in 2009 to 35.1 per cent in 2012, while that of young men decreased from 46.4 per cent to 43.8 per cent in the same period. The fact that the activity rate of young people is approximately 33 percentage points below those recorded for adults (25 to 64 years old) is mostly explained by high rates of school attendance, with approximately 51 per cent of youth 15 to 24 years old still attending school in 2012. For the age group 15-29 years old, the labour force participation rate in 2012 was 58.5 per cent (63.5 per cent for men and 53.4 per cent for women), higher than the 57 per cent activity rate recorded for the same age group in the EU27 (60.9 per cent for men and 53.1 per cent for women).

**Figure 2.1. Youth (15-24) labour force participation, by sex, 2001-2011**



Source: ROSSTAT, Labour Force Survey, 2001-2012

The economic crisis of 2008-2009 had a limited impact on the labour force participation rates of both young (15-24) and adult (25-64) individuals. In the period 2008-2010, the adult activity rates decreased by 0.8 percentage points (0.6 percentage points for men and 1.1 percentage points for women), while for youth the decrease was in the range of 1.8 percentage points (equally distributed between young men and women). The decline in labour market participation was highest among elderly individuals (55 to 64 years old), and especially among men (4.4 percentage points decline in activity rates compared to a 2.2 percentage point drop for women in the same age group).

## 2.2.2 Youth employment

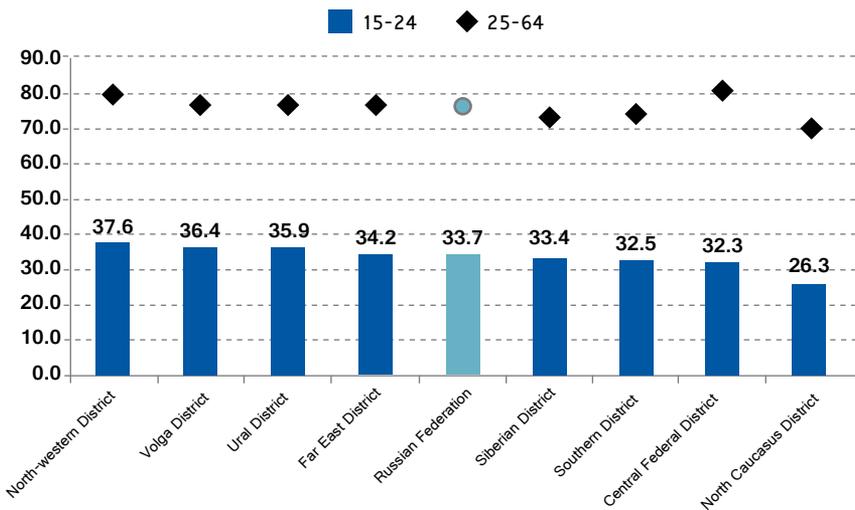
In 2012, the youth (15-24) employment-to-population ratio was 33.7 per cent, two times lower than the employment-to-population ratio recorded for adults (77.1 per cent), with young men more likely to be employed compared to young women (37.5 and 29.8 per cent, respectively). The employment-to-population ratio of Russian youth is above the ratio recorded in the same year in the EU27 (32.9 per cent), but slightly lower than the OECD average (39.7 per cent).<sup>24</sup> The employment ration changes

<sup>24</sup>The higher youth employment to population ratio recorded in OECD countries is due to ratios exceeding 50 per cent in countries such as Australia, Austria, Canada, Denmark, Iceland, the Netherlands, New Zealand, Norway, Switzerland and United Kingdom. See <http://stats.oecd.org/>.

when young people in the age cohort 25 to 29 years old is added to the definition of youth (to 52.9 per cent, which is way above the 46.7 per cent recorded in EU27 countries). This indicates that many of the difficulties young people face in the Russian labour market are overcome as individuals get older (and gain work experience).

Figure 2.2 below shows that, on average, the highest youth employment-to-population ratios are recorded in the North-Western District – due to youth employment rates exceeding 40 per cent in the Murmansk, Vologodsk, Novgorod and Pskov regions as well as in the Republic of Komi – and the lowest in the North Caucasian District, mainly due to the extremely low youth employment-to-population ratio recorded by the Republic of Ingushetia (3.9 per cent). The Central Federal District shows the largest youth-to-adult employment gap (2.6 times), with below average youth employment-to-population ratios in the Moscow (26.3 per cent) and Tatarstan regions. In the Republic of Udmurtia (Volga District) and in the Vladimir region (Central Federal Districts) youth employment-to-population ratios are over ten percentage points higher than the national average (45.8 and 44 per cent, respectively).

**Figure 2.2. Youth and adult employment-to-population ratios across Russian Districts, 2012**

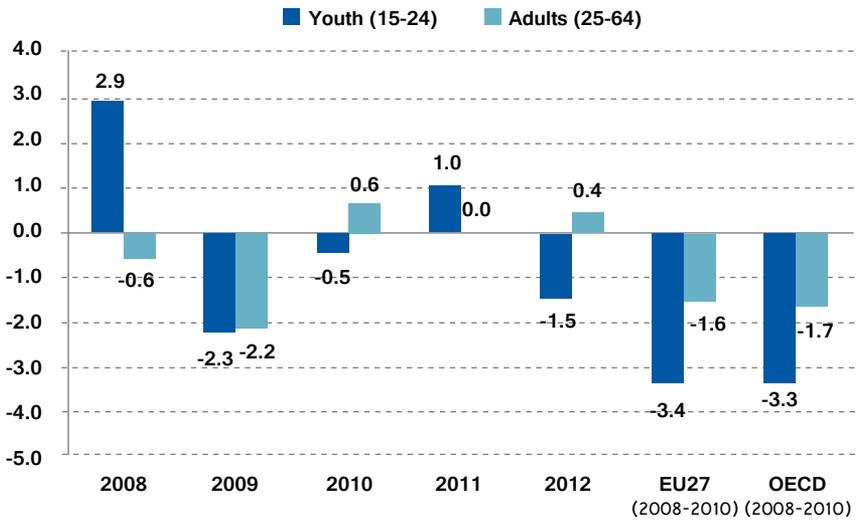


Source: ROSSTAT, Labour Force Survey, 2012

Similarly to activity rates, the youth employment-to-population ratio showed an increasing trend in the years 2005 to 2008 and a drop in 2009 and 2010. The effect of the economic crisis on youth employment in Russia, as shown by Figure 2.3 below, was milder compared to the decrease experienced in the EU27 and OECD countries (3.4 and 3.3 percentage points drops between 2008 and 2010, respectively).

In 2009, the employment-to-population ratio of the working age population dropped by 1.8 percentage points, much lower than the fall in output recorded in the same year (7.8 per cent). Between 2010 and 2011 employment started increasing again, albeit at a modest pace. Youth employment, conversely, recovered slightly in 2011, to then decline again the following year. This latter drop, however, was due, at least in part, to the 6.2 per cent decrease in the 15-24 population.

**Figure 2.3. Changes in employment, youth and adults, Russian Federation, EU27 and OECD countries, 2008-2011**



Source: ROSSTAT, Labour Force Survey, 2001-2011.

Slow employment growth in 2011 was due to a negative balance between job creation and job destruction in the manufacturing (loss of 28,800 jobs) and electricity and gas sectors (loss of 8,500 jobs).<sup>25</sup> In 2012, conversely, the vacancy rate increased to 2.2 per cent (compared to 1.6 per cent in 2011), driven by higher vacancies in the finance, transport and communication and energy sectors.<sup>26</sup>

In the years of the economic crisis (2008-2010), the number of young people employed decreased by 13.5 per cent.<sup>27</sup> Similarly to EU and OECD countries, employment losses in the Russian Federation affected particularly men, urban workers and low-skilled individuals. The fact that employment losses were higher for young men compared to adult men (-3.2 percentage point and -1.3 percentage points in 2009), is due to the structure of youth employment in the country and the concentration of young male workers in the economic sectors most affected by the crisis (e.g. manufacturing, construction and certain service sectors). For instance, youth employment in manufacturing and construction declined by 20 per cent, while the drop recorded in services amounted to 13.5 per cent. Employment in public health and services, which are female-dominated sectors, actually increased during the downturn (by 4.5 per cent between 2008 and 2009). The sectoral composition of employment (Figure 2.4 below) shows that young workers (15-24) are mostly engaged in wholesale and retail trade, manufacturing, public administration, transport and communication, construction and agriculture.

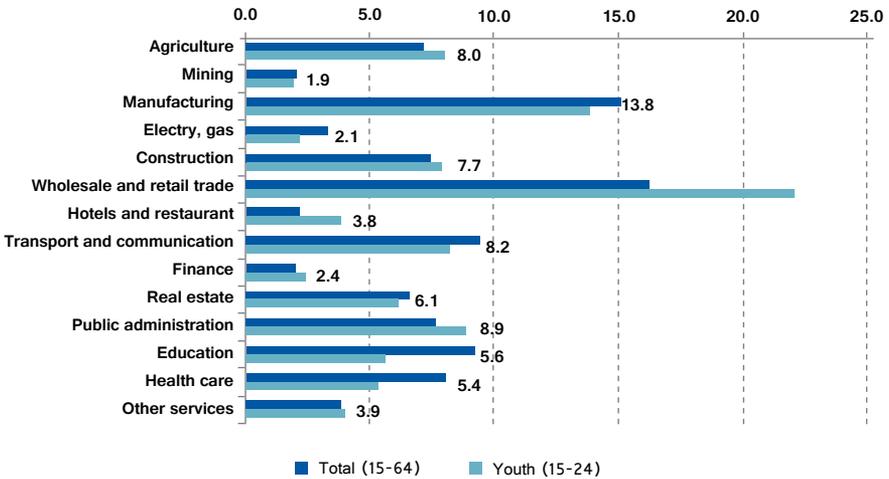
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<sup>25</sup>ROSSTAT, Survey of organizations, 2011.

<sup>26</sup>The vacancy rate is the share of vacant jobs over total jobs (number of individual employed). See World Bank, Russia Economic Report No 29: Recovery and beyond, Washington D.C. 2013.

<sup>27</sup>Overall employment for the cohort 25-49 years old in the same period increased by less than 1 per cent, while for the older age group (50 years old and over) the increase was over 8 per cent.

**Figure 2.4. Total and youth employment by economic sector, Russian Federation, 2012 (percentage)**



Source: ROSSTAT, Labour Force Survey, 2012

The sectoral composition of youth employment, however, varies substantially across and within Districts. For instance, the share of youth (15-24) employed in agriculture in the North Caucasian District is three times the national average (25.4 and 8 per cent, respectively), with roughly 45 per cent of all young workers employed in agriculture in the Republic of Dagestan. But the share of young people working in the agricultural sector exceeds 20 per cent also in Altaysky Krai (Siberian District) and in the Tambov Region (Central District). The share of youth employed in manufacturing is 1.5 times the national average in the Vladimir and Kaluga regions (Central Federal District), in the Novgorod region (North-Western District) as well as in the Republic of Karachaevo-Cherkessia (North Caucasian District) and in the Ulyanovsk region (Volga District). In the Chechen Republic (North Caucasian District) the share of young workers employed in construction is over four times the national average (29.7 per cent and 7.7 per cent respectively). In Kamchatsky Krai (Far East District), the Republic of Tyva (Siberian District) and the autonomous okrug of Evreysky (Far East District) the share of youth employed in the state administration is twice the national average. Finally, in the Republic of Altay (Siberian District) the share of youth employed in the education sector is well over twice the national average (12.1 per cent and 5.6 per cent).

The structure of youth (15-24) employment by educational attainment shows that youth with vocational educational attainment are over-represented among those employed compared to other groups (see Table 2.2). In 2012, over 20 per cent of young workers had tertiary education (27 per cent for women and 15.2 per cent for men) and over half (52.2 per cent) had secondary educational attainment. But young workers with secondary vocational attainment comprised 24.8 per cent of total youth employment (although only 16 per cent of the total youth population has this level of education) and those with initial vocational education represent 20 per cent of all young workers (although only 12.2 per cent of the total youth population had that educational level in 2012).

The education and occupation mismatch figures (29 per cent of all young workers, see the shaded area of Table 2.5 below) disaggregated by sex, show that young men are much more likely than women to be over-qualified (33 per cent of men are overqualified compared to 24.1 per cent of women). A combined analysis of these data and those relating to youth employed by educational attainment, points to low labour market rewards of high educational attainment among young men.<sup>28</sup> The overall mismatch, in fact, is mostly accounted for by secondary and tertiary education graduates working in elementary occupations, and tertiary university graduates working as craft and related trades workers, plant and machine operators and service and sales workers. In all these categories— except for service and sales workers – young men are proportionately more represented than women. Elementary occupations account for 17.8 per cent of total men’s employment (6.5 per cent for women), while 21.8 per cent of all men workers are employed as craft and related trades workers (compared to 4.3 per cent of women) and 15.9 per cent are employed as plant and machine operators (1.9 per cent for women). For young women, nearly 15 per cent of the mismatch is due to young women with high educational attainment working as clerical and administrative support workers and as services and sales workers.

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<sup>28</sup>Over-qualification is slightly lower when one considers the cohort 15-29 years old (27 per cent). The sex distribution of over-qualification, however, remains similar with 30 per cent of young men workers overqualified compared to 22 per cent of young women workers.

**Table 2.5. Education and occupation mismatch as a function of ISCO and ISCED, 2012 (thousands)**

ISCO-08 Major Groups		ISCED-97 Educational attainment					
		0	1	2	3	4	5
1	Managers	...			30.1		138.4
2	Professionals	0.1			36.1		923.9
3	Technicians and associate professionals	0.3			252.8		803.3
4	Clerical support workers	0.7			105.0		136.7
5	Service and sales workers	4.3			893.4		<b>452.2</b>
6	Skilled agricultural, forestry, fishery workers	15.0			257.0		36.9
7	Craft and related trades workers	1.5			661.6		<b>256.7</b>
8	Plant and machine operators and assemblers	2.3			449.5		185.6
9	Elementary occupations	13.9			<b>707.2</b>		115.3

Source: ROSSTAT, Labour Force Survey, 2012

Most young individuals aged 15 to 24 work as wage employees (93.2 per cent of all young workers in 2012), with only minor differences between young men and women (Table 2.6). In 2012, young own account workers comprised 6.8 per cent of youth employment, with young men slightly more likely to be self-employed compared to young women (7.1 and 6.4 per cent, respectively). Such distribution, and especially for the 20-24 cohort, follow closely that of adults (25+) with the overwhelming majority of workers engaged in wage employment.

The sex distribution of youth own-account work over the years shows that at the beginning of the decade the share of young women in own account work was higher than that recorded for young men (9.6 and 8.3 per cent, respectively in 2001). By 2007 the distribution of youth own account work was similar (7.8 per cent) across the sexes, while since 2008 young men have been more likely to be own account workers compared to young women. Adult men, conversely, show consistently higher rates of own account work compared to adult women through the years (7.7 per cent and less than 6 per cent, respectively). The disaggregation of self-employment figures shows that most young people are engaged in own account work (87.1 per cent in 2012); 8.7 per cent are contributing family members; 0.4 per cent work in cooperatives and 3.8 per cent are employers. Interestingly, over two thirds of young contributing family members are young men (66.8 per cent), most likely engaged in farm activities.

**Table 2.6. Structure of youth employment, Russian Federation, 2001-2012**

	2001	2007	2012
Economic sector			
Agriculture	12.7	10.4	8.0
Industry	26.5	26.0	25.6
Services	60.8	63.6	66.4
Status in employment			
Employees	91.1	91.9	93.2
Own account workers	8.8	7.8	6.8
Type of contract			
Full-time	96.9	97.3	97.2
Part-time	3.2	2.8	1.8
Involuntary part-time	27.3	27.7	21.2
Permanent	82.2	76.9	82.7
Fixed term	12.1	12.5	8.0
Civil contract	1.5	3.5	1.8
Oral contract	4.2	7.0	7.4

Source: ROSSTAT, Labour Force Survey, various years

Since 2002, there has been a notable increase in the use of service and fixed term contracts as well as oral agreements. In particular, the number of workers employed with a fixed term contract increased two folds in the period 1999-2008, to then decrease sharply during the 2009 economic crisis, as these workers were the first to be dismissed during the negative business cycle.<sup>29</sup> The figures of Table 2.5 above show that atypical forms of employment among youth increased from 17.8 per cent in 2001 to 23.4 per cent in 2007, to then settle at 17.2 per cent in 2012. Such a decline is due to the fact that in the crisis years (2007-2010) temporary employment among young workers decreased by over 21 per cent, while the decrease in permanent employment amounted to 2.6 per cent.

The number of young women in temporary work decreased much faster than men's (34 per cent decrease in the period 2007-2010, compared to 16.6 per cent decrease for young men), but the number of young women who gained permanent work was twice that of men. As a result,

<sup>29</sup>OECD, Review of labour market and social policies of the Russian Federation, 2011, op.cit

the 2010 figures show that young men were more exposed to temporary work compared to young women (14.4 and 5.5 per cent, respectively); they were also more likely to hold an oral arrangement (7.9 per cent and 4.9 per cent, respectively). By 2012, temporary work had decreased for both young men and women (to 10.7 and 4.5 per cent, respectively), but the share of those employed under an oral agreement had increased for both young men (9.1 per cent) and women (5.3 per cent).

The distribution of youth employment by type of work contract and educational attainment (see Table 2.7) shows that the lower the educational level, the higher the probability to be exposed to atypical work arrangements, with over one third of youth with no basic education working with an oral contract and another 16 per cent employed in temporary work.

**Table 2.7. Youth employment by type of contract and education level, Russian Federation, 2012**

Education level	Type of contract			
	Permanent contract	Fixed-term contract	Civil contract	Oral contract
Less than basic education	45.4	16.1	5.8	32.6
Basic education	62.7	10.9	2.9	23.6
Secondary education	72.5	11.6	3.2	12.7
Initial VET	83.2	8.3	1.6	7.0
Secondary VET	88.2	6.4	1.2	4.2
Higher education	92.3	5.0	0.8	1.9

Source: ROSSTAT, *Labour Force Survey, 2012*

Young, less educated employees, workers in the construction, trade and agricultural sector tend to be more exposed to temporary contracts than other groups. Being married, living in an urban area or in a region with high unemployment rates also increases the probability of temporary work.<sup>30</sup> Not only the sector of economy, but also the size, the ownership structure and the age of enterprises matter for the use of atypical labour contracts. In the Russian Federation, these types of contracts are more

<sup>30</sup>Karabchuk T., “Temporary employment in Russia: why mostly men?”, *The European Journal of Comparative Economics*, Vol. 9, n. 2, 2012.

often used by large- and medium-size enterprises (compared to small companies) and by state-owned enterprises (compared to private ones). This is due to two main reasons. First, the choice of non-standard employment contracts is connected with restructuring processes that affect mostly old, large and medium-size enterprises that are still state-owned. Second, large- and medium-size enterprises are often characterized by labour hoarding inherited from the past. When these enterprises face specific labour demands, they hesitate to hire under standard labour contracts, due to their higher separation costs.<sup>31</sup>

Part-time employment in the Russian Federation represents only 1.1 per cent of total employment (compared to over 22 per cent for the working age population in EU27 countries). Part-time employment among youth is also low, accounting for 1.8 per cent of total youth employment in 2012, with involuntary part-time accounting for 21.2 per cent of the total. Approximately one third of involuntary part-time among young people is due to the reduction of working hours by the employer, a four-fold increase compared to the share recorded in 2007 (approximately 6 per cent).<sup>32</sup> In 2012, over a third (32.2 per cent) of part-time workers in the age-group 20-24 years old was combining school with work.

### 2.2.3 Young workers in the informal economy

In 2012, employment in unregistered enterprises accounted for 17.1 per cent of overall employment (15-64), with men more likely to be working in informal enterprises compared to women by roughly 4 percentage points.<sup>33</sup> In the same year, youth working in informal enterprises accounted for 24.4 per cent of total youth employment, almost equally distributed between young men and young women (Figure 2.5). Employment in informal enterprises, however, decreased from the peak registered in 2005 (18.4 per cent of overall employment and 25.3 per cent of youth employment). Such a decrease is, for the most part, due to the job losses

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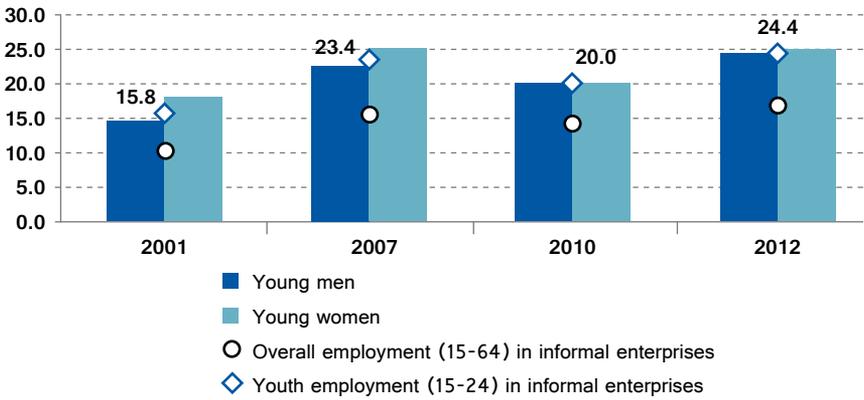
<sup>31</sup>Smirnykh L., Wörgötter A., “Why do Russian Firms use fixed term and agency work contracts?” Economic Department Working papers No 1014, 2013.

<sup>32</sup>In 2008, the number of workers engaged part-time due to the reduction of working hours by the employer increased 10 times compared to the prior year. See Kapelyushnikov R., Kuznetsov A., Kuznetsova O., “The role of the informal sector, flexible working time and pay in the Russian labour market model”, *Post-Communist Economies*, Vol. 24, June 2012, op.cit.

<sup>33</sup>The Federal State Statistics Service (ROSSTAT) accounts as informal workers those who have their main job in entities that are not legally registered.

recorded among young workers in informal enterprises between 2008 and 2010. The data, in fact, show a decrease of over 570 thousand young individuals working in informal enterprises in the period, with roughly 60

**Figure 2.5. Employment in informal enterprises, Russian Federation, 2001-2012**



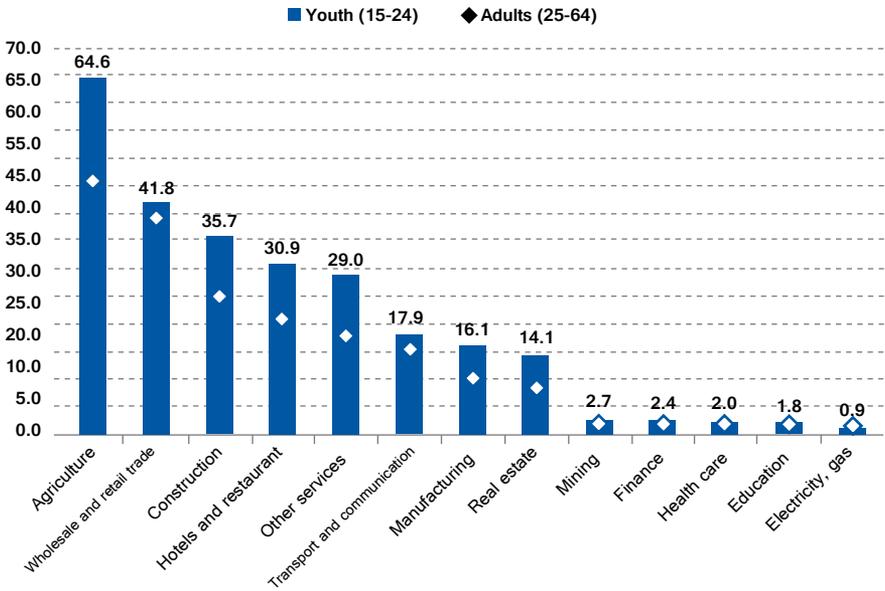
Source: ROSSTAT, Labour Force Surveys, 2001-2012, op.cit

per cent of these being young women. As the economy started to recover, youth employment in informal enterprises increased again (by roughly 14 per cent in 2011 compared to 2010).<sup>34</sup>

The distribution of young workers in informal enterprises by educational attainment shows that in 2012 over half (56.8 per cent) had secondary (general) education, 12.8 per cent had vocational education and 13.4 per cent had higher educational attainment. Informality prevails among young workers at the lower end of the educational attainment scale: nearly 67 per cent of young workers with less than basic education were informally employed in 2012, compared to 49.2 per cent of young workers who had attained basic education. The lowest incidence of informality was found among workers with secondary vocational (17.3 per cent) and tertiary educational attainment (10.4 per cent). For many, work in the informal economy is a means to acquire job related skills and work experience. In fact, the figures show the highest peak of informality occurring for young workers aged 20 to 24 years old to then progressively decline at workers age.

<sup>34</sup>Between 2010 and 2011, informality increased across all age groups, but more markedly for youth (2.5 percentage points against 1.7-1.8 percentage points for the other age groups).

**Figure 2.6. Youth and adult employment in informal enterprises\*, by sector, 2012**



(\*) Main job Source: ROSSTAT, Labour Force Surveys, 2001-2012, op.cit

Figure 2.6 above illustrates the large variation in the incidence of youth and adult employment in informal establishments by economic sector, with agriculture, wholesale and retail trade, construction and the food and accommodation industry showing by far the largest shares of informality. Agricultural workers, service workers, workers in crafts and related trades as well as elementary workers also show higher shares of work in informal establishments (ranging from 25 to 35 per cent of total workers) than other occupations.

The figures on informality reported above, however, do not include young individuals working under informal employment arrangements in formal enterprises, and therefore underestimate the overall extent of informal employment in the Russian Federation.<sup>35</sup>

<sup>35</sup>According to international statistical standards, informal employment includes: i) employment in informal enterprises (not registered); and ii) individuals working under an informal employment relationship (i.e. the relationship is not, in law or in practice, subject to national labour legislation, income taxation and social protection). See ILO, Resolution on the measurement of employment in the informal sector, adopted by the Fifteenth International Conference of Labour Statisticians (ICLS), Geneva, 1993, and Guidelines concerning a statistical definition of informal employment, adopted by the Seventeenth ICLS, Geneva, 2003.

An analysis conducted on the Russian Longitudinal Monitoring Survey (2003-2011) and its 2009 Supplement on informality reveals that the incidence of informal employment varies considerably depending on the definition used. For instance, the share of employees working under an oral agreement (main job) in 2009 represented 11.2 per cent of all workers; adding workers in unregistered enterprises, self-employed workers and employees with an oral contract, those working in an unregistered establishment (second job), those receiving part of the salary as “envelope” wages as well as workers with unpaid contributions raised the level of informality to 20.4 per cent of total employment.<sup>36</sup> Irrespective of the definition used, however, the analysis found that younger workers, men, workers with primary education or less, low-skilled individuals, as well as workers in the construction and trade industry had a substantially higher likelihood of being informally employed.

The higher incidence of informal employment among young workers is confirmed by the findings of the 2012 school-to-work transition survey. Informal employment among young respondents (15-29) accounted for 50.9 per cent of total youth employment (26.9 per cent employed in informal enterprises and 24 per cent holding informal jobs in formal enterprises), nearly equally distributed between the sexes (51.9 per cent of young men and 49.7 per cent of young women workers).

## 2.2.4 Wages and conditions of work for young people

In the Russian Federation young workers earn approximately 15 per cent less than adult workers.<sup>37</sup> The gap between teenagers and young adults is around 50 per cent, while the gender wage gap among young workers is 26 per cent, lower than the wage gap found among adult workers (33 per cent). Education pays a premium in terms of wage levels, with highly educated individuals in the working age earning on average 46 per cent more than workers with less than basic education. Such wage premium, however, is much lower for young workers (27 per cent). In addition, higher educational attainment does not help young women bridge the wage gap with young men, which remains at around 26 per cent also at higher levels of education. One key feature of the Russian labour market is

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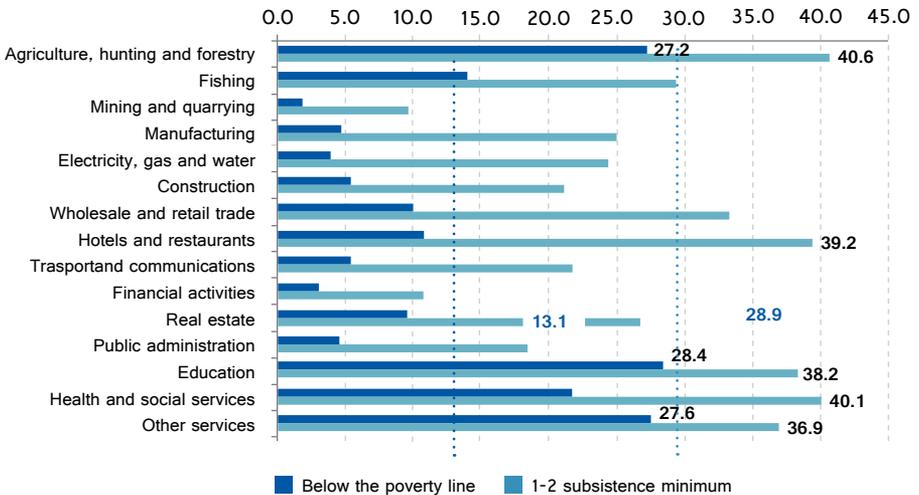
<sup>36</sup>Lehmann, H., Zaiceva A., Informal employment in Russia: Definitions, incidence, determinants and labour market segmentation, OECD Economics Department Working Papers, No. 1098, 2013

<sup>37</sup>Such wage gap may in part be explained by the higher incidence of informal employment among young workers compared to adults. The data of the 2009 Supplement to the Russian Longitudinal Monitoring Survey show an informal-formal wage gap ranging between 7.5 and 12.2 per cent.

wage flexibility that derives from: i) the absence of indexation, ii) the relatively high median share of performance pay on workers' wage (ranging from 24 to 58 per cent of total wage according to economic sectors), iii) the widespread use of wage arrears; and iv) the practice of using informal payments (shadow salaries), estimated at 50 per cent of the official wage. These mechanisms allow firms to reduce the cost of labour quickly, without having to dismiss workers.<sup>38</sup>

Another worrying aspect of the Russian labour market is the share of working poverty (13.1 per cent of workers earn below the poverty line) and low-paid work (28.9 per cent of workers earn between once and twice the minimum subsistence level). Although data disaggregated by age group and sex is not available, the figures on low wage work by economic sectors make a suspect that many young workers may fall into this category, given their prevalence in the trading, manufacturing, construction and agricultural sectors (Figure 2.7).

**Figure 2.7. Working poor and low-wage workers by economic sector, 2011**



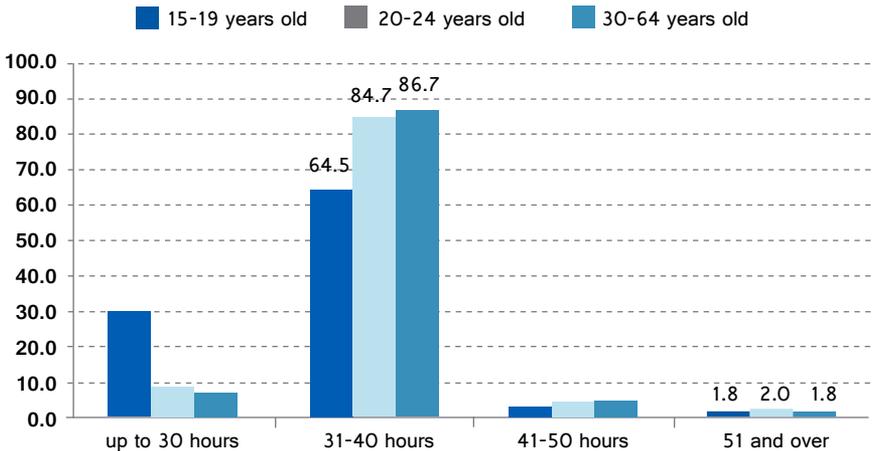
Source: ROSSTAT, Sample survey of organizations, 2011

<sup>38</sup>Kapelyushnikov R., Kuznetsov A., Kuznetsova O., “The role of the informal sector, flexible working time and pay in the Russian labour market model”, *Post-Communist Economies*, 24:2, 2012. See also OECD, *Economic Survey of the Russian Federation*, Paris 2013.

Average monthly wages differ widely across Districts, as do their trends over time. In 2010, four districts had average monthly wages below the national average, namely Siberia, Volga, the Southern District and especially the North Caucasus, where average wages accounted for less than 60 per cent of the national average. Nominal wage growth was strong until 2008 (averaging over 26 per cent increase on an annual basis), with wages in the Central Federal District and North Caucasus District growing faster. Wage growth slowed in 2009, with growth above the national average recorded in the Southern, Far East and especially in the North Caucasus districts (wages increased in this latter district by 15 per cent compared to a national average of 7.8 per cent growth on an annual basis). Such double digit growth, however, was unable to bridge the gap between the North Caucasus and national average wages, which remained at around 40 per cent.

The figures on hours of work show that in 2012 most individuals – youth and adult alike – were working between 31 and 40 hours per week. The share of youth working excessive hours (i.e. over 50 hours per week) was around one per cent, similarly to the share found for adult workers.

**Figure 2.8. Weekly hours actually worked, by age group, 2012**



Source: Labour Force Survey, 2012

Young women (20-24) are less likely to be working excessive hours compared to young men (0.9 per cent and 2.8 per cent, respectively), but are also more likely to work less hours than men (36.2 hours per week on average compared to 39.4 hours a week worked by young men). Teenagers also work shorter hours (32.4 hours per week, on average), compared to young adults (38 hours per week on average).

As mentioned in the paragraph on part-time employment, many young workers were exposed to a reduction of working hours by employers during the economic downturn, which also affected their wage levels. The labour market adjustment in the Russian Federation occurred through a combination of decreasing employment, reduction of working hours and lower wage levels, which was more pronounced for young workers compared to adults.<sup>39</sup> Whereas this limited the overall decline of youth employment in the country as a whole (compared for instance to countries in the European Union), it had a negative impact on youth wage levels and other conditions of work.

## 2.2.5 Youth unemployment

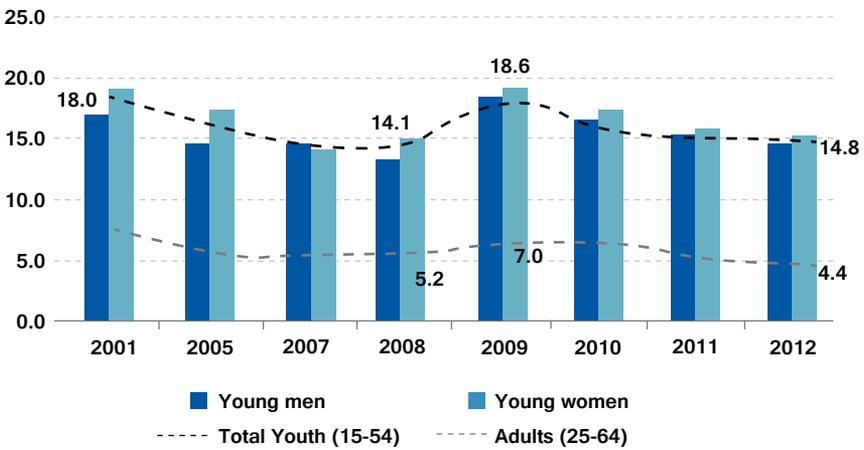
Since 2001, the unemployment rate of young people (15-24) has constantly been well over twice the unemployment rate recorded for adults (25-64 years old). The ratio of the youth-to-adult unemployment rate shows an increasing trend until 2007, when it peaked at 2.9, to then stabilize at around 2.7 (in the period 2008-2010). By 2012, however, the youth-to-adult unemployment rate ratio had reached 3.3, caused by the faster decrease of the adult (25-64) unemployment rate compared to that of youth (one percentage point vs. 0.7 percentage points).

Figure 2.9 shows the youth and adult unemployment trends in the period 2001-2012, which display a remarkably similar pattern. The highest youth unemployment rate is recorded among teenagers (31.9 per cent compared to a rate of 15.1 per cent for young adults), and especially among young girls (37.1 per cent) and teenagers living in urban areas (34.2 per cent).

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<sup>39</sup>In the span of just one year (2008-2009) the total number of hours worked decreased by 5.5 per cent for the whole economy. Similarly, the share of workers who experience an involuntary reduction of working hours in the same period increased from 0.5 per cent of total employment to 5.7 per cent and real wages declined by 4 per cent. See Kapelyushnikov R., Kuznetsov A., Kuznetsova O., "The role of the informal sector, flexible working time and pay in the Russian labour market model", *Post-Communist Economies*, 24:2, 2012

**Figure 2.9. Youth unemployment rate, by sex, 2001-2012**



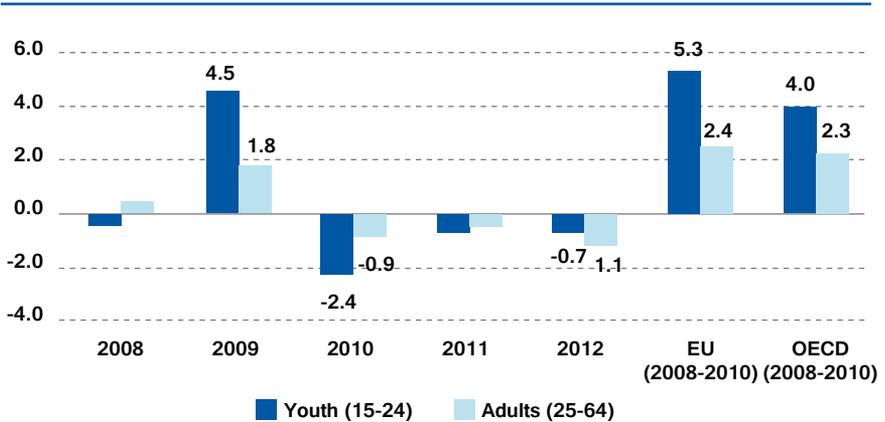
Source: ROSSTAT, Labour Force Survey, 2001-2012

In 2012, the youth unemployment rate was 14.8 per cent (14.5 per cent for men and 15.1 per cent for young women), lower than the rate recorded across OECD countries (16.3 per cent).<sup>40</sup> As already mentioned, labour market outcomes improve as young individuals become older: in 2012 the unemployment rate of the extended youth group (15-29) was 9.6 per cent (9.5 per cent for men and 9.8 per cent for women). The youth unemployment rate in the Russian Federation peaked in 2009 at 18.6 per cent (18.3 per cent for young men and 19 per cent for young women) due to the contraction of the economy.

In that year, youth unemployment rose by over 25 per cent, causing an increase of the youth unemployment rate of 4.5 percentage points, well over twice the increase recorded in the adult unemployment rate (1.8 percentage points).

<sup>40</sup>Such a rate is also below that recorded in the same year for youth in the EU27 (22.8 per cent), where the youth unemployment rate increased by 5 percentage points between 2008 and 2010.

**Figure 2.10. Changes in the youth and adult unemployment rate, 2008-2012**



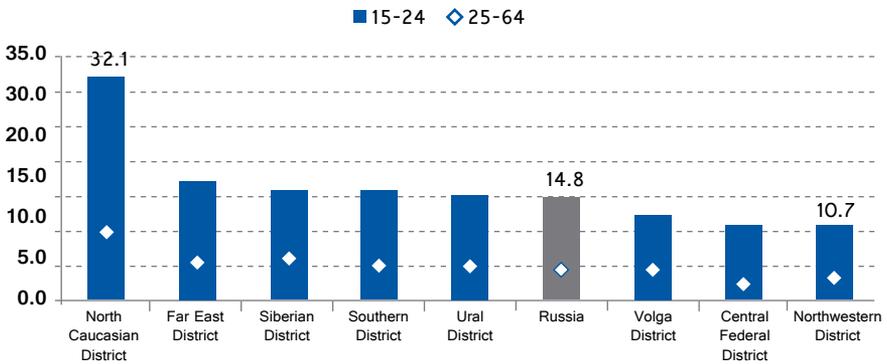
Source: ROSSTAT, Labour Force Survey, 2008-2012

Similarly to what occurred for youth employment, increases in unemployment were more pronounced for young men compared to young women (28.7 per cent and 22.2 per cent increases, respectively).

As the economic recovery started to take hold in 2010, both the youth and the adult unemployment rates started to decrease, initially at a faster pace for young workers compared to adults. After four years of positive economic growth, however, the youth (15-24) unemployment rate appears to have settled at around pre-crisis levels (14.8 per cent in 2012 and 14.5 per cent in 2007), while the adult unemployment rate has reached its lowest level in the last two decades (4.4. per cent in 2012). This may signal that part of the cyclical increase in youth unemployment has become structural, with serious implications in terms of loss of skills and labour market detachment among young people.

There are striking differences in unemployment rates across entities of the Russian Federation. Figure 2.11 below shows that youth unemployment is concentrated in the North Caucasian (32.1 per cent), Far Eastern (17.3 per cent) and Siberian Federal Districts (16.0 per cent).

**Figure 2.11. Youth (15-24) and adult (25-64) unemployment rates across Russian**



Source: ROSSTAT, Labour Force Survey, 2012

Moscow and San Petersburg have the lowest youth unemployment rates (4.7 and 3.2 per cent, respectively), while the highest are found in the Republic of Ingushetia (91 per cent) and the Chechen Republic (52.8 per cent).<sup>41</sup> The changes in unemployment associated with the economic crisis, however, occurred mostly in the North Western and Ural Districts, where industrial production – and especially manufacturing – accounts for a larger share of GDP.

An analysis of the determinants of youth unemployment, carried out for the period 2000-2009 in 75 Russian regions, found a stable spatial correlation for youth unemployment (negative for distance and positive for bordering regions). This means that each Russian region is surrounded by regions with similar youth unemployment rates and that the greater the distance between regions, the greater the difference between youth unemployment rates (core-periphery pattern).<sup>42</sup> The relationship between youth unemployment and level of regional output and import-export activity (used as a proxy of economic development), as expected, was found to be

<sup>41</sup>Across districts, the largest gap between youth and adult unemployment was recorded in the Central Federal District (with a ratio of 4.4) and the lowest in the Siberian District (with a ratio of 2.6). In 2012, the Moscow and Lipetsk regions in the Central Federal District had the highest youth-to-adult unemployment rate ratio (8.3 and 5.9, respectively), followed by the Samara region (Volga District) and Kamchatsky Krai (Far East District) at 5.6, and the Omsk region (in the Siberian District) at 5.4.

<sup>42</sup>Demidova O., Signorelli M., “Determinants of youth employment in Russian regions”, *Post-Communist Economies*, Vol. 24, June 2012. This research found no significant effect on youth employment of the share of the youth population in the region, the share of the urban population and net migration rate.

significant and positive. As Table 2.8 below shows, the districts with the lower share in national output (namely North Caucasus and the Far Eastern District) are also those with the highest youth unemployment rates.

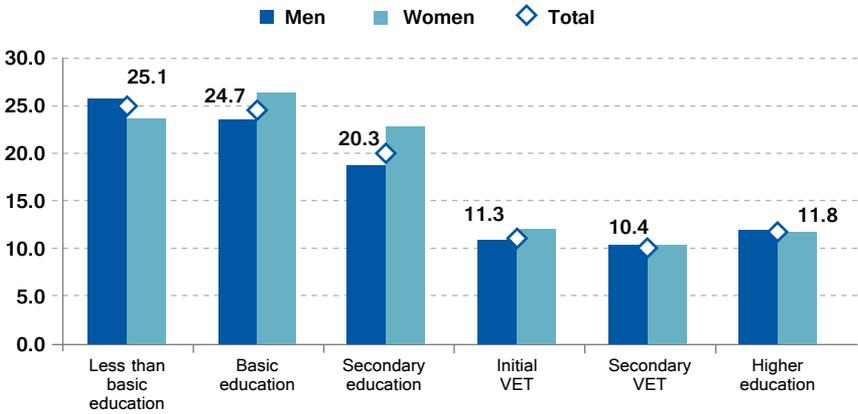
**Table 2.8. Key features of Russian Districts, percentages ca 2011**

District	Share of territory	Share of population (2012)	Share of output (2010)	Share of firms (2011)	Share of total jobs (2010)	Youth unemployment rate (2012)
Central Federal District	3.8	26.9	35.7	39.7	27.5	10.8
North-western Federal District	9.9	9.5	10.4	12.8	10.2	10.7
Southern Federal District	2.5	9.7	6.1	6.4	9.2	15.5
North Caucasian Federal District	1.0	6.6	2.4	2.7	5.2	32.1
Volga Federal District	6.1	20.8	15.1	14.9	21.2	12.1
Ural Federal District	10.6	8.5	13.6	8.5	8.8	15.3
Siberian Federal District	30.1	13.5	10.9	11.1	13.4	16.0
Far Eastern Federal District	36.1	4.4	5.6	3.8	4.6	17.3

*Source: Federal State Statistics Service, Labour and Employment in Russia, Statistical Compendium, 2012*

The youth unemployment rate by educational attainment shows that the lower the educational attainment, the higher the likelihood of being unemployed. Young people with less than basic, basic and secondary (general stream) educational attainment have unemployment rates exceeding 20 per cent (see Figure 2.12 below), while young people with secondary vocational education have the lowest (10.4 per cent). The unemployment rate among young people with high educational attainment is 11.8 per cent. One possible explanation for the relatively high unemployment rate among young university graduates is that this group may spend more time looking for a job that is aligned to their level of education (see paragraph below) and/or pays a better salary compared to other groups of young workers. But it may also point to a mismatch between the skills acquired while at school and enterprises' requirements.

**Figure 2.12. Youth (15-24) unemployment rate by educational attainment, 2012**



Source: ROSSTAT, Labour Force Survey, 2012

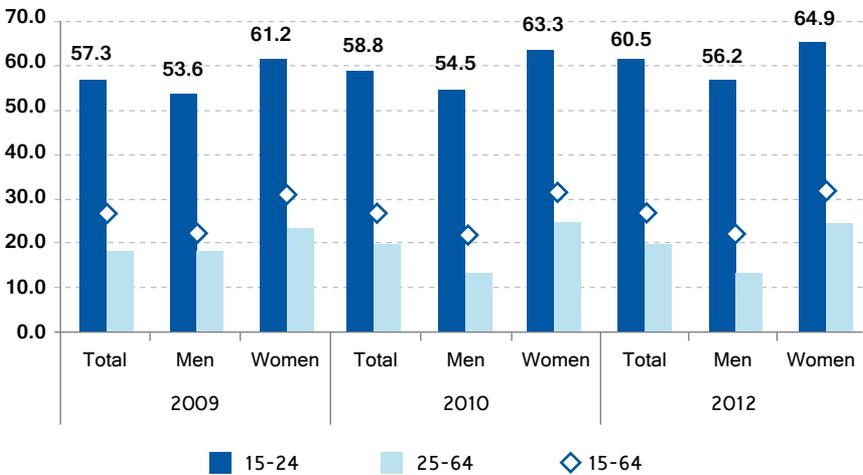
The share of youth (15-24) looking for a job for one year or more in 2012 was 20 per cent of total youth unemployed, compared to 36.6 per cent of adults. Over 63 per cent of young unemployed had unemployment spells shorter than 6 months, with nearly 17 per cent looking for a job for less than one month. The highest share of long-term youth unemployment in the same year was recorded in the Republic of Ingushetia in the North Caucasus District (61.2 per cent), and the lowest in the Leningrad region (2.2. per cent), in the North-Western District.

The preferred method of job search among young people is through family and friends (means used by over 62.4 per cent of young unemployed), followed by advertisement (36.7 per cent) and registration with the Public Employment Service (29 per cent).

### 2.2.6 Youth inactivity and discouragement

Between 2009 and 2012 overall inactivity rates remained fairly stable for the working age population (at around 27 per cent), with women more inactive than men throughout the period (Figure 2.10). The disaggregation by age-group shows increasing youth inactivity rates (from 57.3 per cent in 2009 to 60.5 per cent in 2012), slightly more pronounced for young women (3.7 percentage point increase) compared to young men (2.6 percentage point increase).

**Figure 2.13. Inactivity rates by sex and age-group, 2009-2012**



Source: ROSSTAT, *Labour and employment in Russia, 2012*

This trend has been driven by higher participation of the youth cohort in education. This is confirmed by the figures relating to the reasons for inactivity, available for 2011 (see Table 2.9). The overwhelming majority of inactive youth were attending an education institution (men more than women), while nearly 6 per cent of all inactive youth were engaged in household and care duties (mostly young women).<sup>42</sup>

The share of young discouraged workers, at less than one per cent of all inactive youth, is much lower than the discouragement rate found among adults (3.6 per cent). In 2011, detached youth (e.g. inactive youth, but willing to work) represented three per cent of total inactive youth. Discouragement is highest among young people with initial vocational education (5.5 per cent of all inactive youth with that level of education) and lowest among young people with low educational attainment (only 0.5 per cent of all inactive youth with less than basic education were discouraged).

<sup>43</sup>The school to work transition survey (2012) reports that among inactive individuals aged 15-29, about 18 per cent were inactive due to care and household duties. Of these 25 per cent were youth with tertiary education, 22 per cent had secondary vocational education and 29 per cent had general secondary educational attainment. As over one third of inactive youth with those levels of education are willing to work, this represents a large pool of unutilized human resources.

**Table 2.9. Distribution of youth inactivity by main reason, Russian Federation, 2011**

Reason of inactivity	2011		
	Total	Men	Women
In school	86.3	90.6	82.5
Own illness, disability	1.2	1.5	0.8
Engaged in household/care duties	5.9	0.3	10.8
Discouraged workers	0.9	1.1	0.8
Other reasons	5.7	6.5	5.1
<b>Youth available for work</b>	<b>3.1</b>	<b>3.5</b>	<b>2.8</b>

*Source: ROSSTAT, Labour Force Survey, 2011*

In 2012, the share of young Russians (15-24) not in employment, education or training (NEET) represented 12 per cent of the youth population, with young women more likely to be in this status compared to young men (14.4 per cent and 9.7 per cent, respectively). Most young NEETs are in the cohort 20 to 24 years old (over 66 per cent of the total), with young women 20-24 representing over 36 per cent of the total. The distribution by educational attainment shows that youth with initial vocational education and those with higher education are more likely to be NEETs (19.9 and 19 per cent, respectively) compared to youth with only basic education attainment (7.8 per cent).



# 3

## TRANSITION FROM SCHOOL TO WORK

Traditional labour market indicators often fail to reflect all the difficulties young people face in their transition from school to work. To determine the degree of ease or difficulty experienced by youth in getting stable and satisfactory work, the ILO developed a survey-based methodology to identify the paths to transition young people take once they leave school. Such an approach goes beyond the traditional binary concept of quantity of employment and unemployment and measures the share of the youth population that has stable jobs that provide personal satisfaction.

The school-to-work transition is divided into three major stages according to whether the young person: 1) has “not yet started” the transition (this includes all young people who are still in school or are inactive with no intention to work in the future); 2) is “in transition” (this category encompasses all unemployed youth, those who are working, in unsatisfactory self-employment or temporary work, as well as youth who are inactive and not in school, but plan to work at a later date); and 3) has “transited” to work (this category includes all young people working in a stable and/or satisfactory job). The following table summarizes the key transition indicators for youth aged 15 to 29 years in the Russian Federation, as detected by the ad hoc module attached to the Labour Force Survey (LFS) carried out the Federal Statistical Service in July 2012.<sup>44</sup>

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<sup>44</sup>The survey was implemented in eleven regions of the Russian Federation, namely the regions of Bryansk, Voronezh, Novgorod, Volgograd, Rostov, Nizhny Novgorod, Sverdlov, Chelyabinsk, Irkutsk and in the Republics of Dagestan and of Bashkortostan.

**Table 3.1. Key transition indicators, youth 15-29, Russian Federation, 2012<sup>44</sup>**

School-to-work transition indicators			
Transition not started	31.6	In school	29.7
		Inactive youth, not willing to work	1.9
In transition	15.1	Unemployed youth (relaxed definition)	10.8
		Young workers in unsatisfactory temporary work	0.3
Transition completed	46.2	Youth in unsatisfactory self-employment	0.3
		Inactive, not in school, willing to work in future	3.7
		Young workers in stable, satisfactory wage employment	46.2
		Young workers in stable, but unsatisfactory wage employment	4.1
		Young workers in satisfactory temporary work	1.1
		Youth in satisfactory self-employment	2.0

Source: ILO, *Labour market transitions of young women and men in the Russian Federation, Work4Youth Publication series, No 4, Geneva, 2013*

In 2012, the share of young Russians (15-24) not in employment, education or training (NEET) represented 12 per cent of the youth population, with young women more likely to be in this status compared to young men (14.4 per cent and 9.7 per cent, respectively). Most young NEETs are in the cohort 20 to 24 years old (over 66 per cent of the total), with young women 20-24 representing over 36 per cent of the total. The distribution by educational attainment shows that youth with initial vocational education and those with higher education are more likely to be NEETs (19.9 and 19 per cent, respectively) compared to youth with only basic education attainment (7.8 per cent).

Table 3.1 above shows that at the time of the survey over one third of young people aged 15 to 29 years old (31.6 per cent) had not yet started their transition to work, as they were still attending school (50.9 per cent young women and 49.1 per cent young men). A small share of respondents (1.9 per cent of the total) was inactive with no intention to work in future, with young women more likely to be in this latter category compared to men (72.9 per cent and 27.1 per cent, respectively).

<sup>45</sup>The transition rates presented here exclude those young respondents that could not be classified. The rates are, therefore, slightly different from those reported in the School-to-Work Transition research. See ILO, *Labour market transitions of young women and men in the Russian Federation, Work4Youth Publication series, No 4, Geneva, 2013*

Young people still in transition represented 15.1 per cent of total youth respondents, mostly young adults aged 20 to 29 years old (77 per cent of all youth still in transition). Young women were more likely than men to be in this transition phase (55.1 per cent young women and 44.9 per cent young men), as 18.3 per cent of total youth in this category were inactive young women, not enrolled in education, but willing to work at a later date (mostly in the age-group 25 to 29 years old). The overwhelming majority of young people in this transition stage were unemployed youth and discouraged workers (71.4 per cent), while young workers in self-employment and temporary work that was unsatisfactory represented 4 per cent of all young people still in transition

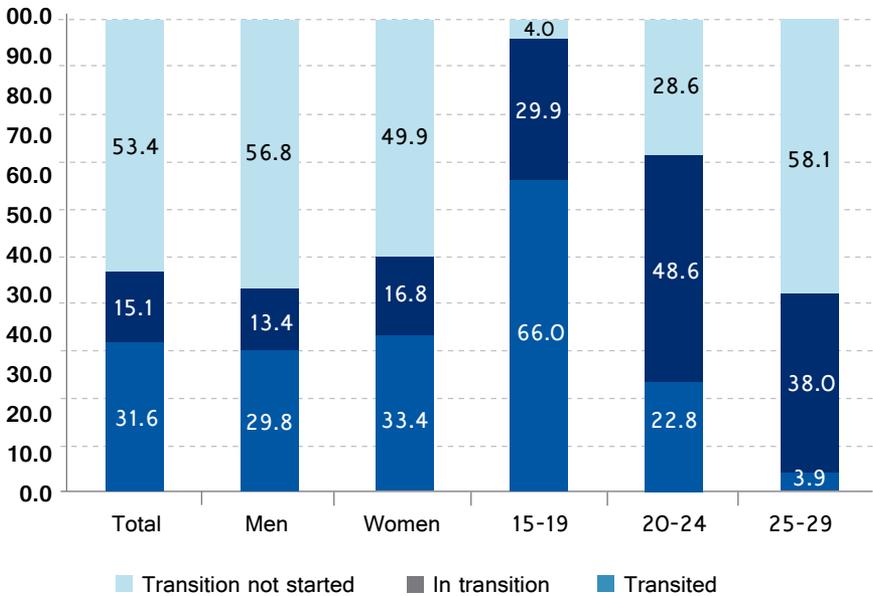
Nearly half of young respondents (49.3 per cent) had a job they were satisfied with, with young men representing 52.8 per cent of all “transited” youth. As expected, nearly two thirds (58.1 per cent) were young adults in the age-cohort 25 to 29 years old and another 38 per cent was youth aged 20 to 24. Teen-agers (15-19 years old) represented less than 4 per cent of all youth that had transited to the world of work.<sup>46</sup>

Figure 3.1 below offers a snapshot of young Russians by sex, age group and stage of transition. The paragraphs that follow examine in detail the characteristics of young respondents in each of the three transition stages identified above.

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<sup>46</sup>The disaggregation of respondents by age and labour market status shows that the highest peak of inactivity is among youth aged 15 (due to school attendance), the highest level of employment is found among youth 27 years old (i.e. those who have completed higher education and had the time to gain work experience) and the peak of unemployment at age 22, which is the average age of graduation from a higher education institution.

**Figure 3.1. Stages of transition by sex and age-groups, Russian Federation, 2012**



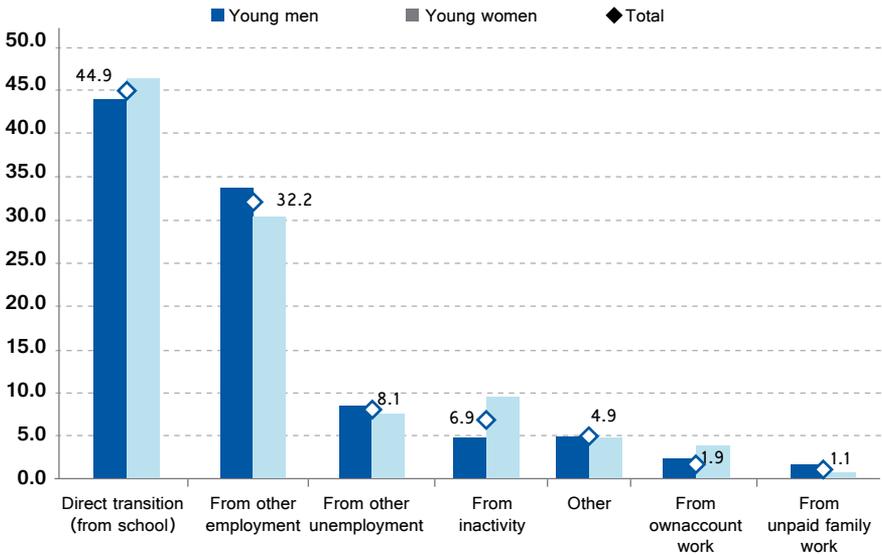
Source: ILO, *Labour market transitions of young women and men in the Russian Federation*, Geneva, 2013, op.cit

In terms of length of transition, the survey reveals that on average it takes a young Russian nearly two years (23.4 months) to gain a job that offers relative stability or is personally satisfying. The transition is longer for young men compared to young women (25.5 months vs. 21.5 months). This is due in part to the fact that young women tend to have higher levels of educational attainment compared to young men. Over 31 per cent of young people who have transited to the world of work, in fact, have a university degree (19.3 per cent are young women and 12.3 per cent are young men).

Figure 3.2 below shows that approximately 45 per cent of young respondents experienced a direct transition from school to work, young women slightly more than young men (46.2 per cent and 43.8 per cent). When young people who experienced a direct transition are excluded from the count, the average duration of transition lengthen to nearly four years

(45.2 months).<sup>47</sup> This means that approximately one third of all young people in the Russian Federation faced difficulties in gaining a foothold in the labour market. Moreover, the school to work flow data show that the transition from inactivity and unemployment to stable or satisfactory work is rather low (only 6.9 and 8.1 per cent of the total, respectively), with the bulk of transition (32.2 per cent) occurring from other forms of work.

**Figure 3.2. Transition to stable/satisfactory employment, Russian Federation, 2012**



Source: ILO, *Labour market transitions of young women and men in the Russian Federation*, Geneva, 2013, *op.cit*

<sup>47</sup>The socio-economic differences among the countries where the school to work survey was carried out (Benin, Cambodia, Former Yugoslav Republic of Macedonia, Togo, Malawi, Liberia and Zambia) are too wide to compare the figures on the duration of transition. For instance, the average length of transition in the Former Yugoslav Republic of Macedonia was 26.3 months (including direct transition), while in Cambodia it was 9.8 months. The latest figure available for European Union countries refers to 2009, when the average duration of transition from school to the first significant job was of 6.5 months).

### 3.1. Young people not yet in transition

The overwhelming majority of young people who had not yet started their transition (94.1 per cent) was still attending school, with young women slightly more likely than young men to be still in education (51 per cent and 49 per cent, respectively). Young people still attending school were mostly teenagers (66.1 per cent); roughly a third (29.9 per cent) was represented by young adults (20-24 years old) and 4.1 per cent were young individuals 25 to 29 years old. Interestingly, the share of women in this latter age group still in education was twice that of their male peers. The higher percentage of young adult women still in education confirms, on the one hand, the fact that they are more likely to enrol into higher education compared to young men, but also that it may take young women longer to complete their studies due to family and household responsibilities.

Young people who were inactive, not in education and had no intention to work represented less than 2 per cent of youth in this transition category. Many were young women (nearly 73 per cent) and in the older age group (around 60 per cent), e.g. the age at which many of them start a family and engage in child rearing.

### 3.2. Young people still in transition

Young Russians at this stage of the school to work transition represented just over 15 per cent of the total youth population, with young women more likely than men to be still in transition (17.5 per cent of young women and 13.9 per cent of young men). Table 3.2 below shows the figures disaggregated by sex and sub-category of transition.

**Table 3.2. Youth 15-29 still in transition, by sex Russian Federation, 2012**

	Total	Men	Women
Young unemployed (relaxed definition)	71.5	36.0	35.5
Unemployed (strict definition)	50.1	27.2	22.9
Discouraged workers	21.3	8.8	12.6
Inactive, not in school, intending to work	24.5	6.1	18.4
Youth with a temporary, but not satisfying, job	2.0	0.8	1.1
Self-employed youth, but dissatisfied	2.1	1.9	0.2

Source: ILO, *Labour market transitions of young women and men in the Russian Federation*, Geneva, 2013, op.cit

Approximately half of all young people still in transition were unemployed (54.3 per cent young men and 45.7 per cent young women), according to the ILO strict definition.<sup>48</sup> Of these, half were in the age group 20 to 24 years old and another third were in the age group 25 to 29. When young discouraged workers are included in the count, jobless youth represented over 71 per cent of all youth still in transition.<sup>49</sup> Young discouraged workers represented 3.2 per cent of all young respondents, with young women – especially those 20-29 years old – more likely to be discouraged workers compared to men (58.9 per cent young women and 41.1 per cent young men).

Slightly over 16 per cent of all unemployed youth had been looking for a job for one year or more (equally divided between the sexes). Lack of work experience and shortages of jobs were the most commonly cited obstacles faced by young unemployed in their job search (28.3 per cent and 24.3 per cent of unemployed respondents, respectively). Job search intensity among young unemployed, however, was rather low, with only 36.6 per cent of the unemployed enquiring about jobs three or more times in the previous year and just about 36 per cent able to gain more than two job interviews on an annual basis.

The second most common status for youth at this stage of transition was inactive, not in school, but willing to work (24.5 per cent of all youth still in transition). The majority of young people who were inactive, but willing to work, was found among those 25 to 29 years old and among young women. Over 38 per cent of youth in this category, in fact, were young women aged 25 to 29 and another 26 per cent were women aged 20 to 24 years old, most likely engaged in care and household duties, but available to (re) enter the labour market.

Young people who were either self-employed or in a temporary job, but were not satisfied with their current situation represented a small minority (2.1 and 2 per cent of all youth still in transition, respectively). However, it is interesting to note that most unsatisfied temporary workers were in the age cohort 20 to 24 years old.

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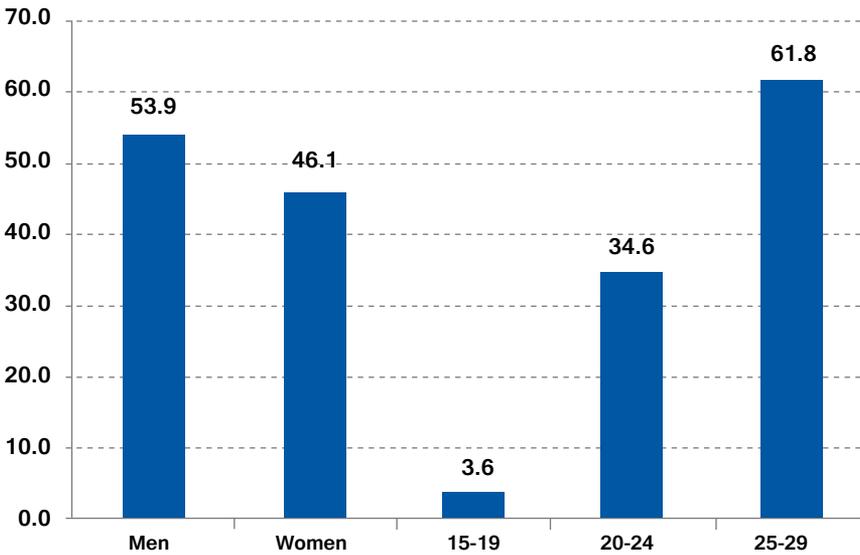
<sup>48</sup>The strict definition of unemployment comprises all those who did not work in the reference period, were currently available for work and actively searching for a job.

<sup>49</sup>The relaxed definition of unemployment includes all those who are not actively searching for a job, but are available to work should a job be offered to them.

### 3.3. Young people transitioned to the world of work

This transition category distinguishes among young people who are in permanent jobs, those employed in temporary work and those who are self-employed. Young workers – either self-employed or wage employees – who had jobs that gave them personal satisfaction represented 48.1 per cent of the total youth population, over 62 per cent of whom were in the age cohort 25 to 29 years old (Figure 3.3).

**Figure 3.3. Young people with a satisfactory job, by sex and age group, Russian Federation, 2012**



Source: ILO, *Labour market transitions of young women and men in the Russian Federation*, ILO; Geneva, 2013, *op.cit*

Young men were more likely to be in this subcategory compared to young women (53.9 and 46.1 per cent, respectively) – even though it typically took young men longer to get a satisfactory job compared to young women.

Young workers engaged in a permanent, but unsatisfactory job represented 7.8 per cent of all young transitioned to the world of work. Young women are slightly more likely to be working in a job that is not satisfying (51.9 per cent) compared to young men (48.1 per cent). The shares of young adults (20 to 24 and 25 to 29 years old) with unsatisfactory jobs

were fairly similar (at around 46 per cent).

Over 86 per cent of all youth who had completed their transition to work (see Table 3.3 below) were employed in a permanent job that gave them personal satisfaction. Young men were more likely than women to have achieved this stage of transition (52.8 per cent and 47.2 per cent) as well as individuals in the older cohort compared to youth aged 20 to 24 years old (62 per cent and 35 per cent, respectively). The figures disaggregated by sex show that young men were over-represented among those who had a temporary job and among the self-employed (65 per cent and 82 per cent, respectively) compared to young women.

**Table 3.3. Youth (15-29) transitioned to the world of work, by sex Russian Federation, 2012**

	Total	Men	Women
Young workers in stable and satisfactory job	86.5	45.7	40.8
Young workers in stable, but unsatisfactory job	7.8	3.7	4.0
Youth in temporary and satisfactory work	2.0	1.3	0.7
Youth in satisfactory self-employment	3.7	3.0	0.7

Source: ILO, *Labour market transitions of young women and men in the Russian Federation*, Geneva, 2013, *op.cit*

There are a number of factors that appear to ease the transition to work. First, educational attainment, with young people having attained a university degree or a vocational qualification more likely to have completed the transition and be in a stable and satisfactory job compared to youth with general secondary or basic educational attainment. Given the strong relation that exists between educational attainment and labour market performance, it would be key to address the main reasons that drive young people to leave school early, namely lack of interest in education and training (mentioned by 29.6 per cent of young early leavers) and economic reasons (mentioned by 26.1 per cent of early leavers).

The second factor relates to household income, with young people belonging to less affluent families more likely to be still in transition compared to youth from middle and high-income households. In addition, young people belonging to households with higher income are more likely than other groups to achieve stable employment.

Third – and as already mentioned – individual characteristics such as sex, age and geographical location also play a role. Young men, young adults 25-29 years old and youth living in urban areas are more likely to gain a stable and satisfactory job compared to other groups. The cumulative data indicate that young women are at a disadvantage compared to young men: they were more likely to be inactive, albeit willing to work, and less likely to find a satisfactory job, be it permanent, temporary or as own account workers. Transition to a stable job correlates with age, with the group 25-29 more likely to have achieved a stable job in the formal economy, compared to other groups. Finally, young people living in rural areas are more likely to be engaged in temporary jobs, or be own account workers because they could not find a wage work compared to their urban peers.

The fact that a good share of young Russians had transitioned to the world of work and had a job that was subjectively satisfactory (48.1 per cent of the youth population), however, sheds little light on the quality of jobs available to youth. To address this issue, the school to work transition survey also investigated the prevalence of informal employment, deficiency of entitlements among young workers and wage levels.

The data collected on informal employment reveals that 50.9 per cent of all young workers were employed informally, 26.9 per cent working in an informal enterprise and 24 per cent holding an informal job in a formal enterprise.<sup>50</sup> Young women were slightly less likely than men to be employed informally (44.6 per cent and 55.4 per cent, respectively), with the younger cohorts (15-24) more exposed to informality compared to young adults. This means that the actual share of youth aged 15 to 29 years old that at the time of the survey had a job that was stable, satisfactory and granted them the protection of labour law, represented at most 28 per cent of the total youth population.

Approximately 34 per cent of all young workers earned below the average wage (25 per cent of young own account workers and 35.3 per cent of young wage employees). Young women in wage employment were twice more likely to be earning below the average wage compared to young men (42 per cent and 28 per cent, respectively), while young own-account men were nearly four times more likely than women to have earning below the average wage (34 per cent and 9 per cent, respectively).

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<sup>50</sup>The figure of youth employment in informal enterprises detected by the school-to-work survey is in line with the figure reported by the labour force survey, whereby 24.4 per cent of total youth employment (15-24) is in informal enterprises.

At the time of the survey, the share of young people earning below the subsistence minimum (i.e. young working poor) comprised 8.5 per cent of total employment, while low-paid young workers accounted for 38.9 per cent.<sup>51</sup>

In terms of entitlements, young workers often lack access to overtime pay, occupational safety and protective equipment, but also medical insurance coverage and payment of social security contributions. Lack of overtime pay was the most frequently mentioned breach of entitlements, slightly more common among women and adult young workers, compared to other groups. Occupational health and safety and failure to provide protective equipment was the second most cited infringement, especially among young women. These figures are in line with the figures of the Labour Inspectorate that show that the most common labour law violations in the country revolve around occupational health and safety and hours of work.

The survey also collected other indicators that help shedding light on young people situation in the labour market. For example, the share of young self-employed workers who entered this form of work because they could not find wage employment is nearly one third of all self-employed (29 per cent), with youth living in rural areas over twice as likely to be in this status compared to their urban peers (44 per cent and 17.1 per cent).

The data collected by the school-to work transition survey indicates that the main youth employment challenge that the Russian Federation needs to address is the quality of jobs for youth, more than just the creation of new jobs for the 10.8 per cent of the youth population that is jobless. In fact, the overall rate of labour under-utilization – i.e. the share of unemployed youth, discouraged workers, youth in irregular employment and youth who are inactive, but not in school over the total population – represents roughly one quarter (24.9 per cent) of the whole 15-29 population.

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<sup>51</sup>These percentages have to be taken with some caution as many youth with higher educational attainment refused to answer earnings-related questions. However, these figures are in line with those reported in Chapter 2 on working poverty (13.1 per cent in 2011 for the working age population) and low-paid work (28.9 per cent of the working age population). The fact that young workers were found less likely to be working poor compared to the overall working population is due to their generally higher educational attainment, on the one hand, and the decline of poverty recorded after the 2009 economic crisis (with the poverty rate settling at its historical low of 11 per cent of the population in 2012), on the other. See also World Bank, Russian Economic Report. Reinvigorating the economy, October 2012.



# 4 POLICIES AND INSTITUTIONS FOR YOUTH EMPLOYMENT

As mentioned in Chapter 1, the strong economic growth recorded by the Russian Federation between 2000 and 2008 is the result of a number of factors, not least the management of economic policies. In this period the country enjoyed greater macroeconomic stability compared to the previous decade, with decreasing inflation and a series of current account and budget surpluses spanning over a number of years. Fiscal policy was prudent, with windfall revenues stemming from oil and gas production saved in a stabilization fund.<sup>52</sup> The business environment also improved, thanks to the reforms of the tax regime, the introduction of banking and competition policies and bankruptcy legislation. The positive economic outcomes recorded throughout the last decade, however, mask large regional variations in terms of economic development, per capita income, employment and poverty levels.

Although the impact of the crisis in the period 2008-2009 was rather severe in terms of output contraction (7.8 per cent of GDP), it was relatively mild in terms of overall job losses (with an increase of the overall unemployment rate of 2.1 percentage points), as the labour market adjusted mainly through a decrease of hours worked (5.5 per cent between 2008-09) and a decline in real wages (4 per cent in the same period). Young people (15-24) took the brunt of the crisis: the youth unemployment rate increased from 14.1 per cent in 2008 to 18 per cent in 2009, with job losses affecting mostly young men, youth with low educational attainment and young workers engaged under atypical forms of contracts. The response of the federal government to the 2008 economic crisis was swift and wide ranging, thanks to the resources accumulated in the Reserve Fund. These resources

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<sup>52</sup>The Reserve Fund replaced in 2008 the Oil Stabilization Fund, set up in 2004 to insulate the federal budget from oil price instability.

allowed the authorities to support the banking sector, defend the currency and undertake expansionary fiscal policies. The labour market recovered already in 2010 with increasing employment and declining unemployment, except for the younger cohort whose unemployment rate was still above pre-crisis levels in 2012 (14.8 per cent).

The slowdown of output growth recorded in 2012 (3.4 per cent) continued in 2013 (2.5 per cent) due to a decline in consumption, lower investment and a still weak external environment that affected net exports. Capacity utilization is at about 80 per cent, the same rate recorded prior to the economic crisis, when the economy was growing at 8 per cent annually. This, together with overall unemployment at a record low, may indicate that the economy of the Russian Federation is running close to potential.<sup>53</sup>

The main challenges facing the country in the next decade are decreasing trends in the working age population; raising both the quantity and the quality of youth employment; bridging regional development gaps; diversifying the economy and reducing the dependence from oil and gas; and improving the quality of educational outcomes at all levels to maintain a competitive edge.

## 4.1 Macroeconomic and sectoral policies

Since the beginning of the transition to a market economy, the Russian Federation has built modern fiscal institutions, reformed its tax system and budgetary rules and introduced fiscal decentralization mechanisms. Such mechanisms are estimated to reduce the fiscal gap between the poorest and richest regions from 47 to 7 times (see Box 4.1).

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<sup>53</sup>World Bank, Russian Economic Report No 30, World Bank, Washington D.C., 2013; IMF, Russian Federation, 2013 Article IV Consultation, IMF Country Report 13/301, 2013, OECD, Economic Survey: Russian Federation 2013, OECD Paris 2014.

### Box 4.1 Fiscal decentralization in the Russian Federation

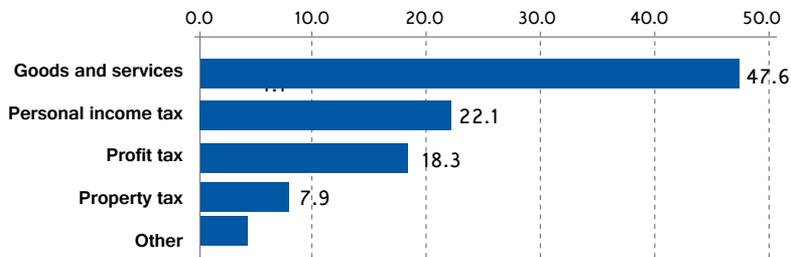
In 2012, the federal budget spending on transfers to the regions amounted roughly 5 per cent of total expenditures (approximately one per cent of GDP). There are two main categories of transfers to the regions: unconditional grants (equalization and fiscal balancing grants), and subsidies, which can be spent only on specific programmes agreed in advance. Some forms of subsidies also require co-financing from regional government budgets.

Federal equalization transfers are aimed at reducing the gap in fiscal capacity across regions, with fiscal entitlements varying inversely with regional capacity and directly with fiscal needs. The transfers are computed using a set of federal equalization formulae that adjust for differences in wages, utility prices, share of the population living in areas with less than 500 inhabitants and/or in mountainous areas, access to transport, prices of goods and services, share of children (less than 17 years of age) and pensioners in the total population.

Source: World Bank, *Social expenditures and fiscal federalism in Russia*, Washington D.C., 2011; Ministry of Finance, *Key Economic Indicators (2011-2013)* downloadable at <http://www.eeg.ru/pages/425>

The wide-ranging tax reform of the early 2000s considerably broadened the tax base, reduced marginal rates and simplified the tax structure. Key measures included: i) the introduction of a 13 per cent flat rate personal income tax, the mineral extraction tax and the Unified Social Tax; ii) the elimination of some sale taxes and the reduction of the Value Added Tax (VAT) rate to 18 per cent; and iii) the reduction of the corporate income tax.

Figure 4.1. Composition of tax revenues, 2013



Source: Federal Tax Service of Russia, at <http://analytic.nalog.ru/portal/index.en-GB.htm>

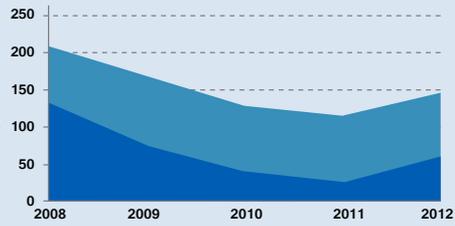
As Figure 4.1 shows, the Russian tax system relies mostly on indirect taxation (VAT, excise duties and mineral extraction tax) while the property tax accounts for 7.9 per cent of total revenues. In 2013, revenues accrued from these taxes equalled 20.8 per cent of GDP, while

the revenues from social security contributions equalled 7 per cent.<sup>54</sup> The establishment of an Oil Stabilization Fund in 2004, with specific rules on the accumulation and spending of its resources, reversed the negative fiscal position inherited from the 1990s. The Fund’s resources were initially used to reduce the external debt and later for macro-economic stabilization.<sup>55</sup> In 2007 a new fiscal framework was introduced to offset spending pressures and redistribute the wealth stemming from oil revenues. Such framework was further amended in 2012 (Box 4.2).

**Box 4.2. The Reserve and National Welfare Funds**

The 2007 fiscal framework limited the spending of oil and gas revenues to 3.7 per cent of GDP, while the limit for the non-oil balance was set at 4.7 per cent of GDP.

The Stabilization Fund was split into two new funds: the Reserve



Fund and the National Welfare Fund. Revenues in excess of the threshold oil price were accumulated in the Reserve Fund until they reached 10 per cent of GDP; thereafter revenues could be saved in the National Welfare Fund. By 2008, the combined assets of the two funds amounted to roughly 6 per cent of GDP.

The GDP-anchored fiscal rule was suspended at the end of 2009, to allow the introduction of expansionary fiscal policies to counter-act the effects of the economic crisis. By the end of 2010 the resources of the Reserve Fund had decreased to 2 per cent of GDP, while those of the NWF remained relatively stable at 6 per cent.

At the end of 2012, a new fiscal rule was introduced to limit government spending to the projected sum of non-oil revenues, oil and gas revenues (calculated at a 5-year backward-looking benchmark price for Ural oil), plus a net financing of one per cent of GDP. When oil prices are above the benchmark price, savings are accumulated in the Reserve Fund until they reach 7 per cent of GDP. Fifty per cent of any additional savings are allocated to the NWF and the remaining 50 per cent allocated to infrastructural projects. When oil prices are below the benchmark price, the Reserve Fund is tapped to maintain the level of spending and finance the deficit.

According to preliminary projections, the Reserve Fund, replenished in early 2013 to 4 per cent of GDP, is expected to increase to 4.4 per cent by 2016, while the NWF, currently at 4.3 per cent of GDP, is expected to decline to 3.2 per cent of GDP.

Source: Ministry of Finance, at <http://www.minfin.ru/en/>; World Bank, Russian Economic Report No 12, 2012, op.cit; World Bank, Russian Economic Report No 30, Washington D.C., 2013; IMF, Russian Federation, 2013 Article IV Consultation, IMF Country Report, 2013 op.cit.

<sup>54</sup>International Monetary Fund (IMF), Russian Federation, 2013 Article IV Consultation, IMF Country Report 13/310, Washington D.C, 2013.

<sup>55</sup>The central debt decreased from just over 99 per cent of GDP in 1999 to less than 12 per cent in 2010

Fiscal policy has been the main macroeconomic stabilization tool used by the Russian Federation throughout the 2000s. The policy was counter-cyclical until 2005, using taxes and spending cuts to moderate demand in periods of soaring commodity prices. Such policy, however, was relaxed even before the onset of the crisis, as shown by the increasing government expenditures (especially on housing, health and subsidies to enterprises) in 2006 and 2007 (Table 4.1).

**Table 4.1. Structure of government expenditure, percentage of GDP, 2006-2010**

	2006	2007	2008	2009	2010
<b>Total expenditures, general government</b>	<b>31.1</b>	<b>34.2</b>	<b>33.9</b>	<b>40.9</b>	<b>38.5</b>
Interest	0.8	0.5	0.5	0.6	0.6
State administration	2.3	3.0	2.7	2.7	2.6
Defence, law and public order	5.2	5.2	5.1	6.3	5.8
National economy	3.5	4.7	5.5	7.2	5.2
Housing and utilities	2.3	3.3	2.8	2.6	2.4
Education	3.9	4.0	4.0	4.6	4.2
Health and sport	3.6	4.2	3.8	4.3	3.8
Social policy	8.8	8.6	8.7	11.7	13.0
Pensions	6.2	5.9	6.2	8.3	9.9
Other	0.8	0.8	0.8	0.9	0.8

Source: OECD, *Economic Survey of the Russian Federation, Paris, 2009*

In 2009, the non-oil fiscal deficit increased to 14.9 per cent of GDP, due to the increase of expenditures planned in the three-year budget approved in 2008, and those of the anti-crisis package. The cost of the anti-crisis measures (see Table 4.2.) amounted to 6.7 per cent of GDP, higher than the average spent by OECD countries (roughly 2.5 per cent of GDP).<sup>56</sup>

<sup>56</sup>For the size of the fiscal stimulus package in OECD countries see OECD, *Economic Outlook 2010, Interim Report* at <http://www.oecd.org/economy/economicoutlookanalysisandforecasts/42421337.pdf>

**Table 4.2. Structure of anti-crisis measures, percentage of GDP, 2008-2009**

	2008	2009	Total
<b>Support to the financial sector</b>	<b>1.9</b>	<b>1.4</b>	<b>3.3</b>
Recapitalization and other direct support	0.8	0.2	1.0
Subordinated loans	1.1	1.2	2.3
<b>Promotion of economic growth</b>	<b>0.7</b>	<b>1.8</b>	<b>2.5</b>
Public spending on goods and services	0.1	0.1	0.2
Fiscal stimulus aimed at firms	0.5	1.7	2.2
Fiscal stimulus aimed at household	0.1	...	0.1
<b>Protection of vulnerable groups</b>	<b>...</b>	<b>0.3</b>	<b>0.3</b>
Of which labour market policies	....	0.3	0.3
<b>Transfers to regions</b>	<b>...</b>	<b>0.7</b>	<b>0.7</b>
<b>Total</b>	<b>2.6</b>	<b>4.1</b>	<b>6.7</b>

Source: World Bank, *Long-term fiscal risk and sustainability in an oil-rich country: The case of Russia*, Policy Research Working Paper, Washington D.C. 2010

Such sizeable fiscal stimulus was justified in light of the sharper decline of economic growth in the Russian Federation, the amount of resources accumulated in the Reserve Fund and the weaker performance of automatic stabilizers.

In 2011, the central government balance turned positive (1.6 per cent of GDP), with revenues contributing about 70 per cent of the improvement. Spending declined by 1.5 per cent of GDP, due to the phase-out of main anti-crisis measures and below-than-planned expenditures outlays (Table 4.3). The non-oil deficit, however, remained rather high (at 9.6 per cent of GDP).<sup>56</sup> In 2012 and 2013 the fiscal balance turned mildly negative, due to the slowing pace of economic growth. This in turn was mainly due to a deceleration of consumption, stagnating terms of trade and low investment levels as many infrastructural projects came to an end.<sup>57</sup> In 2013 economic growth was also negatively affected by declining oil prices.

<sup>56</sup>World Bank, Russian Economic Report No 12, 2012, op. cit.

<sup>57</sup>The annual growth of consumption declined from 6 per cent in 2011 to 4 per cent; investment declined from 12 per cent growth to less than one per cent and exports from 4 per cent growth on an annual basis to one per cent. See OECD, Economic Surveys: Russian Federation 2013, OECD Paris, 2014.

**Table 4.3. Federal and Government balance, 2011-2014 (actual and projected)**

	2011	2012	2013(e)	2014(p)
<b>Federal budget</b>				
Revenues	20.9	20.5	19.3	18.2
Expenditures	20.1	20.6	19.8	18.7
Balance	0.8	-0.1	-0.5	-0.5
Non-oil balance	-9.6	-10.4	-9.6	-8.5
<b>General budget</b>				
Revenues	38.4	37.0	36.9	35.1
Expenditures	36.8	36.6	37.9	35.8
Balance	1.6	0.4	-0.7	-0.7
Urals oil price (US\$/barrel)	109.3	110.4	105.0	101.0

Source: World Bank, *Russian Federation Economic Report No 27, Washington D.C. 2012* and *Russian Economic Report No 30, 2013, op.cit*

In the next few years, additional expenditures –estimated at 6.3 per cent of GDP – are envisaged for defence, road maintenance and social protection (especially pension payments). Such spending is to be partly offset by revenue increases accruing from higher social security contribution rates and higher taxes on alcohol, tobacco and vehicle registration, as well as savings (equal to 4.2 per cent of GDP) on transfers to the regions (which levelled at one per cent of GDP in 2013), enterprise subsidies and public services.<sup>59</sup>

Such projections, however, are only in part factoring in the spending required to achieve the long term economic policy targets established in 2012 (see Box 4.3).

<sup>59</sup>Savings on expenditures equal to 1 per cent of GDP per year could materialize through the transfer of responsibility for delivery of certain public services (public administration, health, education, municipal services and housing) to extra-budgetary agencies. Under this reform, the budget of service delivery agencies would be based mostly on the revenues stemming from the sale of services to the federal government, based on an annual performance agreement. This is to be accompanied by the reform of the budget planning system, whereby budget funds are linked to specific (priority) programmes reflecting the development objectives of the country. World Bank, *Russia public expenditure review*, World Bank, Washington D.C., 2011.

### Box 4.3. Long-term economic policy of the Russian Federation

In May 2012, the President of the Russian Federation signed an Executive Order on the Long-term State Economic Policy aimed at strengthening economic growth, increase incomes and make Russia a technological leader. The Order establishes the following economic and social policy targets to be achieved by 2020:

- Create/modernize 25 million highly productive jobs;
- Increase the rate of investment to 25 per cent of GDP by 2015 and 27 per cent by 2018;
- Increase 1.3 times the number of high-technology and science intensive sectors in GDP by 2018;
- Increase labour productivity 1.5 times by 2018;
- Increase the ranking of Russia in the World Bank Doing Business from 120th place to 50th place in 2015 and 20th place in 2018.

By the end of 2012, new national programmes were developed on health, education, employment, social policy, science and technology, and transport. New fiscal rules are to be formulated for the spending of oil and gas revenues and the management of resources accumulated in the Reserve and National Welfare Funds.

The Order also envisages: a) the preparation of a privatization plan and the running of a performance analysis of State-owned companies; b) the reduction of administrative requirements for doing business and the introduction of State guarantees for investment projects; c) the design of national programmes for industrial development, competitiveness and the promotion of priority sectors (aircraft and ship building, electronic industry and agriculture); and d) the design of proposals to accelerate social and economic development in Siberia and the Far East.

Source: Executive Order of the President of the Russian Federation on long-term state economic policy, 7 May 2012 at <http://eng.kremlin.ru/acts/3758>

The fiscal stance that the Russian Federation appears to be embarking upon is one of moderate and back-loaded fiscal tightening – i.e. fiscal adjustment is to be gradually achieved starting from 2016. Such a policy could succeed if structural reforms (improving tax compliance, the business climate and public investment in health, education and scientific research) become an integral part of the adjustment package.<sup>60</sup> However, to maintain the fiscal deficit within the target of one per cent of GDP – lacking further increases in the price of oil and natural gas in world markets – both revenue and expenditure adjustments will be needed, mainly centred on improving the efficiency of the respective systems on the one hand, and mindful of the larger multiplier on aggregate demand stemming from expenditure cuts compared to tax increases, on the other. The relatively undiversified economic structure, coupled with the below-target resources

<sup>60</sup>International finance institutions suggest that the Russian Federation needs a bold, front-loaded fiscal adjustment (of 1.5 per cent of GDP per year in the period 2012-2015) to decrease the non-oil fiscal deficit faster (to take advantage of high oil prices) and replenish the resources of the Reserve Fund.

accumulated in the Reserve Fund, in fact, puts the country in a vulnerable position to external shocks and the risk of pro-cyclical fiscal adjustments in the event of large and persistent oil price drops.<sup>61</sup>

***On the revenue side, an expansion of the tax base and a more progressive tax regime would improve equity as well as the operation of the tax system as an automatic stabilizer.***<sup>62</sup> Tax revenues could be increased by improving overall tax compliance, streamlining a number of VAT exemptions and increasing further the tax rates on alcohol, tobacco and real estate to bring them nearer to OECD levels. ***On the expenditure side, the phasing out of enterprise subsidies, combined with measures to improve the efficiency of social spending and transfer to the regions may accrue additional savings, which would increase the space for growth-enhancing investment programmes.***

Fiscal adjustment would be more growth-friendly, if it were to include re-distribution across revenue and spending items, with a view to reduce distortionary taxes and increase productive spending (especially public investment, as envisaged in the long term economic policy).<sup>63</sup> Finally, key to the success of a back-loaded fiscal tightening is the relative weight of revenues increases compared to spending cuts (Box 4.4), the credibility of the measures to be undertaken (to raise confidence), and an expansionary monetary policy to cushion part of the adjustment.<sup>64</sup>

#### **Box 4.4. Macroeconomic effects of fiscal consolidation**

The historical analysis of fiscal consolidation in advanced economies shows that adjustment typically reduces output and raises unemployment in the short term. A fiscal consolidation of 1 per cent of GDP may reduce output by 0.5 per cent and raise unemployment rates by 0.3 percentage points in 2 years. As youth unemployment is twice that of adults and is more sensitive to the business cycle, a fiscal consolidation of 1 per cent of GDP may increase the youth unemployment rate by 0.6 percentage points.

<sup>61</sup>IMF, Russian Federation, 2013 Article IV Consultation, IMF Country Report, 2013 op.cit.

<sup>62</sup> If tax rates are progressive (linked to the level of income and profit, rather than accrued at a flat rate), revenues adjust automatically downward in a crisis and expand during a period of growth. <sup>63</sup>Fixed capital investment in the Russian Federation at the end of 2011 still remained 3 percentage points below the pre-crisis level, while overall investment was 4.4 percentage points below the rate achieved in 2008, World Bank, Russian Economic Report, No 27, April 2012.

<sup>63</sup>Fixed capital investment in the Russian Federation at the end of 2011 still remained 3 percentage points below the pre-crisis level, while overall investment was 4.4 percentage points below the rate achieved in 2008, World Bank, Russian Economic Report, No 27, April 2012

<sup>64</sup>Much will also depend on the difference between actual international oil prices and the base price set in the Russian budget. If oil prices are higher than planned, the overall budget balance will improve (but not necessarily the non-oil budget balance).

#### Box 4.4. Macroeconomic effects of fiscal consolidation (continued)

Spending-based adjustments are found to be less contractionary (-0.3 per cent of GDP and 0.2 percentage points in the unemployment rate) than tax-based adjustments (-1.3 per cent of GDP and 0.6 percentage points in the unemployment rate), as they typically benefit from monetary stimulus and an expansion of exports. Monetary authorities provide less monetary stimulus during tax hikes, particularly when they involve indirect tax increases (such as the VAT) which raise inflation.

As important as the choice of the fiscal consolidation tool (revenue increases vs. expenditure-cuts) is the distribution of cuts within different types of expenditures. Many countries are undertaking fiscal adjustment by cutting the public wage bill and reducing social transfers, with little attention paid to the positive relation that exists between investment and employment. Policy simulations show that an exogenous increase of investment by 17.8 per cent decreases unemployment levels by 8.9 per cent over the subsequent 4 years.

Source: International Monetary Fund, *World Economic Outlook: Recovery, Risk, and Rebalancing*, October 2010, Chapter 3, at <http://www.imf.org/external/pubs/ft/weo/2010/02/index.htm>; International Labour Office, *World of Work 2012: Better Jobs for a better economy*, Geneva 2012.

Over the past decade Russian monetary policy pursued two main policy objectives: reduce inflation and limit the real appreciation of the currency, with interventions in the foreign exchange market as the main means to attain both objectives. One of the implication of this policy was that the real appreciation of the currency – in response to positive increases of the terms of trade – materialized through higher inflation rates in Russia compared to its main trading partners. In the years leading to the economic crisis, the exchange rate policy gradually shifted toward greater exchange rate flexibility, with inflation pressures being countered through a mix of interest rates and reserve requirements.<sup>65</sup> This strategy goes in the direction of an inflation targeting regime, expected to be established in the Russian Federation in the next few years. Such a monetary policy stance may cause the authorities to resist expansionary measures during a fiscal adjustment, if the inflation rate remains above the established target range (set at 5-6 per cent in 2013).

The Russian Federation became a member of the WTO in August 2012.<sup>66</sup> In the next few years, accession will have an impact on

<sup>65</sup>During the economic crisis, worsening terms of trade and capital inflows caused strong depreciation pressures that the Central Bank counteracted with large interventions in the foreign exchange market. The strategy to allow the rouble to depreciate in small, pre-announced steps was rather costly, with the Central Bank using approximately one third of its foreign reserves between August 2008 and January 2009.

<sup>66</sup>Russia applied for membership to GATT (which was succeeded by WTO) in 1993.

a wide range of policies and institutions (tariffs, custom administration, production subsidies). In the medium term, the overall gains deriving from accession have been estimated at 3.3 per cent of GDP per year (11 per cent in the long run, when also the gains deriving from the improvement of the investment climate materialize).<sup>67</sup> Household gains are mainly reflected in the positive effect trade liberalization and increasing Foreign Direct Investments (FDIs) will have on workers' wages (estimated at 4-5 per cent in the medium term), especially for skilled workers in urban areas.<sup>68</sup> The sectors that are more likely to expand are export-intensive sectors (non-ferrous and ferrous metals, chemicals) and sectors more open to foreign investment (namely telecommunications, banking and insurance). However, ***increased import competition will displace workers in sectors that are unable to compete (declining sectors). The negative impact of trade liberalization on displaced workers can be offset by adequately designed trade adjustment packages (mainly training and re-training for higher skills jobs and relocation assistance).***

The expected benefits of trade liberalization mentioned above, however, may be lower than projected, or take longer to materialize, as demand in advanced economies continues to falter. Since exports to the EU27 represents over half of all Russian exports (52.2 per cent), subdued consumption in these countries may negatively affect the trade prospects of Russia in the short to medium term.<sup>69</sup>

Despite the progress made in the last decade to improve the business environment, there are still a number of factors than hamper private sector development.<sup>70</sup> These factors relate to the government involvement in the production of goods and services, where several state-owned enterprises enjoy a dominant position; administrative and procedural barriers to the setting up and running of firms; weak enforcement of competition rules; a non-conducive climate for FDIs (at least in some regions); weak corporate governance; inadequate human capital and poor infrastructure.<sup>72</sup> ***The fact that the business environment in the Russian Federation is less conducive***

<sup>67</sup>World Bank, Russian Economic Report, April 2012, op.cit.

<sup>68</sup>The increased competition exerted by foreign direct investment is expected to result in labour gaining more than capital. This is why rich households will gain less than lower income households.

<sup>69</sup>See the statistical trade profile of Russia made by the World Trade Organization at <http://stat.wto.org/CountryProfile/WSDBCountryPFView.aspx?Language=E&Country=RU>

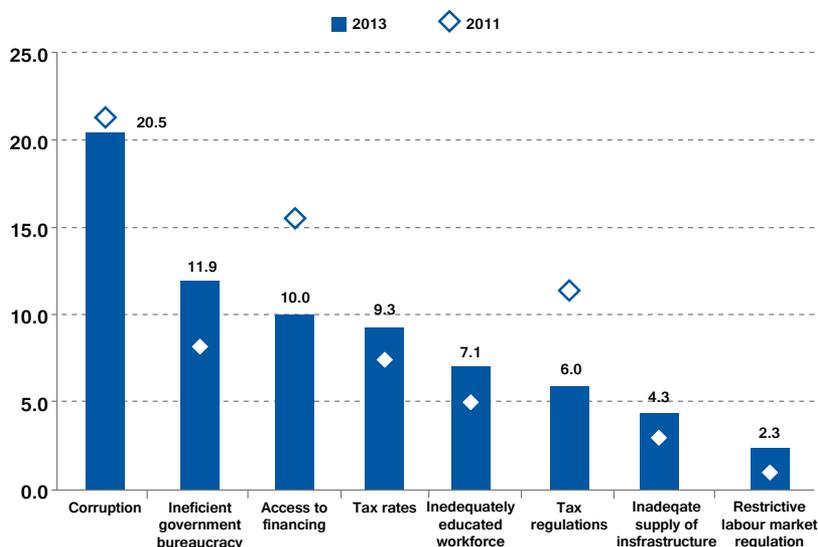
<sup>70</sup>A number of reforms were introduced in the early 2000s on inspection, licensing, registration, simplified taxation, land and custom regulations.

<sup>72</sup>See OECD, Economic Survey, Russian Federation, 2009 and 2011, op.cit; World Bank, Enterprise Survey: Russia, 2009; World Economic Forum, The Russia Competitiveness Report, 2011.

than the average of OECD countries is evidenced by several indicators of economic performance, namely the low share of economic activity generated by small and medium size enterprises (SMEs); the still high proportion of total employment accounted by state-owned companies (30.9 per cent); the low rate of enterprise entry/exit in the market; the concentration of exports in commodities (and especially the oil and gas industry); the lower level of foreign direct investment in the Russian Federation compared to countries in Eastern and Central Europe (1.6 per cent of GDP and 5 per cent, respectively) and its round-trip, offshore features; and the low share of innovation among manufacturing firms compared to the OECD average (13.3 per cent and 57 per cent of all manufacturing firms in the period 2008-2010, respectively).<sup>73</sup>

The data on the main obstacles for doing business (Figure 4.2) show that in 2013 inefficient government bureaucracy and tax rates had become a constraint for a larger share of enterprises compared to 2011, but access to finance and tax regulation had improved.

**Figure 4.2. Most problematic factors for doing business, selected indicators, 2011-2013**



Source: World Economic Forum, *Global competitiveness report 2010-2011 and 2012-2013*, Geneva.

<sup>73</sup>Round-trip, offshore foreign investment represents 60 per cent of all FDIs, it is attracted to resource-rich regions and it is less technological advanced than other types of investment. See Ledyeva S., Karhunen P., Whalley J., “If foreign investment is not foreign: Round-trip versus genuine foreign investment in Russia”, CEPII Working Papers, 2013. For the rates of innovation among Russian manufacturing firms see OECD, *Economic Surveys: Russian Federation 2013*, OECD, Paris 2014.

Firms of all sizes put tax rates among the top barrier for doing business, while the skills of the workforce remained a constraint mostly for medium and large-size enterprises. Taxation and financing constraints for small and medium-size enterprises are being addressed by a set of policy measures put forward since the mid 2000s (Box 4.5).

#### **Box 4.5. Small- and medium-sized enterprises in the Russian Federation**

Small and Medium-size Enterprises (SMEs) in the Russian Federation are categorized into micro businesses (firms with less than 15 employees or a turnover of less than 60 million roubles), small (16 to 100 employees or a turnover of less than 400 million roubles) and medium firms (101 to 250 employees or a turnover of less than 1,000 million roubles). In 2011, SMEs represented 9.4 per cent of all businesses registered in the Russian Federation.

The preliminary findings of the SME census conducted in 2011 show that of the total number of registered SMEs (4.6 million) only 69.5 per cent are in actual operation (two thirds are individual entrepreneurs, 31.2 per cent micro-enterprises, 7.2 per cent small firms and less than 1 per cent medium enterprises). SMEs in Russia account for just over 27 per cent of total employment (compared to 67 per cent in the European Union). Small enterprises accounted for 37.9 per cent of all individuals employed by SMEs, while 27.8 per cent were individual entrepreneurs. Another 20.5 per cent is employed in micro enterprises and 13.6 per cent in medium-size enterprises. In terms of sale revenue, small enterprises take the lion's share (43.1 per cent of all SME sale revenues), followed by medium-size businesses (23.6 per cent). The largest share of SMEs operate in the wholesale and retail sector (38 per cent), real estate and other services (21 per cent), construction and electricity, gas and water (11 per cent each). Over 57 per cent of individual entrepreneurs operate in the wholesale and retail sector, followed by transport, communications and manufacturing (9 per cent each).

The SME policy of the Russian Federation is framed by Law No 209 of 2007 (on the Development of Small and Medium Businesses), a number of implementing regulations, and the Federal Programme to support SMEs launched in 2009.

The Federal Programme comprises four pillars: i) a start-up subsidy of RUB 300,000 (up to RUB 5 million in priority regions, up to RUB 1 million for young entrepreneurs and up to RUB 2.5 million for innovative projects) co-financed 70-30 with regions; ii) interest rates subsidies on commercial credits; iii) the establishment of micro-credit financing institutions (loans up to RUB 1 million), and iv) the establishment of regional funds providing credit guarantees (up to 50 per cent of the credit amount, and 70 per cent for priority areas). In 2010, the Federal budget channelled RUB 15.4 billion (down from the RUB 18.6 billion allocated in 2009) mostly to innovative and export-oriented manufacturing SMEs, businesses in mono-industrial regions/towns and in the North Caucasus. The Ministry of Economy estimates that the public funds made available between 2005 and 2012 created over 170,000 new jobs and maintained over 445,000 existing workplaces.

#### Box 4.5 Small- and medium-sized enterprises in the Russian Federation (continued)

The policy also includes the establishment of business incubators and industrial parks, the offering of business advisory and training services, the re-organization of the inspection system, the implementation of special tax regimes, the simplification of tax reporting and accounting, and the regular monitoring of SMEs trends. Such a policy is expected, by 2020, to increase the SME share in GDP and employment to 30 per cent and the share of SME in total enterprises to 80 per cent.

Source: SME Statistics in Russia - New Facts and Figures, 2011, at <http://www.rcsme.ru/eng/common/totals.asp>; OECD and ILO, G20 Country Policy Briefs, Russian Federation, <http://www.oecd.org/els/48724704.pdf>; ROSSTAT, Statistical review of economic and social indicators, 2011

The achievement of the target set by the Long-Term Economic Policy (e.g. improving the rank in the ease of doing business from 120th to 50th position by 2018), will require further progress in the procedures to start a business, obtain construction permits and electricity connections, as well as in trading across borders. The target is attainable, as Russia's rank in the ease of doing business of the World Bank improved from 120<sup>th</sup> to 111th position in the last two years.<sup>74</sup>

***The improvement of overall competitiveness of the Russian Federation, however, will require additional efforts in areas such as institutional capacity, efficiency of the goods and labour markets, financial market development, business sophistication and innovation.*** A comparison of the indexes relating to these policy areas reveals that Russia's competitiveness has been sliding since 2011 (Table 4.4), especially with regards the level of competition (inefficient and inadequately enforced competition policies and restriction on trade and foreign ownership); the quality of road infrastructure; the sophistication of production processes; firm-level technology absorption; and enterprise spending on research and development.

<sup>74</sup>There are, however, large variations in the ease of doing business rankings across regions. This is mostly due to the different level of implementation of national regulations at regional level, as well as the fact that regions have primary responsibilities for a number of key public services (social, health and education). See European Bank for Reconstruction and Development (EBRD), *Diversifying Russia: Harnessing regional diversity*, 2012.

**Table 4.4. Changes in the competitiveness ranking, Russian Federation, 2011-2013<sup>75</sup>**

	2011	2013
<b>Overall ranking</b>	63	67
<b>Basic requirements</b>	65	53
Institutions	118	133
Infrastructure	47	47
Macroeconomic environment	79	22
Health and primary education	53	65
<b>Efficiency enhancers</b>	53	54
Higher education and training	50	52
Goods market efficiency	123	134
Labour market efficiency	57	84
Financial market development	125	130
Technological readiness	69	57
Market size	8	7
<b>Innovation and sophistication factors</b>	80	108
Business sophistication	101	119
Innovation	57	85

Source: World Economic Forum, *Global Competitiveness Report*, Geneva, various years.

***Even more importantly, it will be necessary to address the issues of non-competitive enterprises, e.g. low profitability firms that owe their continued existence to low wages, poor working conditions and the use of outdated production assets.*** The findings of a research conducted among manufacturing enterprises, make a suspect that a substantial share of Russian enterprises falls within this category.<sup>76</sup> These are mostly medium size firms (100 to 250 workers), located in small or medium size towns in underdeveloped regions and focused mainly on the local market. Such finding is indirectly confirmed by the share of working poor and low-

<sup>75</sup>The Global Competitiveness rankings of this table show the position of the Russian Federation compared to other 139 economies in 2011 and 144 economies in 2013. Contrary to ranking, the competitiveness indexes, measured on a scale from 1 (lowest) to 7 (highest), changed only marginally. This means that compared to the other countries assessed, the Russian Federation did not improve performance in the related areas. World Economic Forum, *The Global Competitiveness Report*, Davos, 2013.

<sup>76</sup>Golikova V., et al., *Russian manufacturing at a crossroad: What prevents firms from becoming competitive*, Moscow State University, 2007. The research calculates that 35-40 per cent of manufacturing enterprises are not competitive and that productivity is the lowest in the textile industry as well as in timber and wood processing.

paid workers in total employment (roughly 40 per cent of all employment) and the share of workers with at least upper secondary education (76 per cent of all workers). These figures indicate that at least one third of secondary educated workers earn low wages, a ratio that cannot be explained only by the poor responsiveness of the education system to labour market requirements, but has to do also with enterprise efficiency, capacity to innovate and productivity.

A recent research conducted on the concentration of industrial production and firm survival in the Russian Federation indicates that volatility of manufacturing growth is higher than in other comparable countries and that firms in sectors where competition is less intense are less likely to exit the market, irrespective of their relative inefficiency.<sup>77</sup> The fact that volatility is more pronounced in small sectors means that firms in these sectors are more likely to exit the market because they are less resilient to longer slumps compared to older enterprises operating in larger sectors. In addition, the fact that older enterprises employ fewer workers and generate lower revenues could indicate that under-performing enterprises survive longer in Russia than elsewhere, preventing resource re-allocation.<sup>78</sup> An additional worrying aspect is the sharp decline in enterprise entry rates (i.e. the share of recently established enterprises over total enterprises), which decreased from 21 per cent in the late 1990s to 8 per cent in 2008 and the low share of exporting firms (3 per cent in 2009 compared to 15-17 per cent in France and the United States) despite the high premium for exporting firms in Russia.<sup>79</sup>

The importance of economic diversification for long-term growth and the bridging of the regional divide is widely acknowledged in the country. Available figures show an increasing concentration since the late 1990s in exports of natural resources and an overall contraction in manufacturing, with oil and gas currently accounting for roughly two thirds of total exports. At regional level, however, data on production and labour specialization show that regional specialization patterns have remained stable between 2002 and 2010, with a positive relationship between specialization and growth. This suggests that diversification efforts should be centred on helping regions leveraging on their comparative advantage and developing new, emerging areas of specialization.<sup>80</sup>

<sup>77</sup>World Bank, Russian volatility:Obstacle to firm survival and diversification, Policy Research Working Paper No. 6605, Washington D.C. 2013.

<sup>78</sup>See World Bank, Russia Economic Report No 23, 2012 op.cit and Russia Economic Report No 30, 2013.

<sup>79</sup>European Bank for Reconstruction and Development (EBRD), Diversifying Russia: Harnessing regional diversity, 2012.

<sup>80</sup>See European Bank for Reconstruction and Development (EBRD), Diversifying Russia: Harnessing regional diversity, op.cit.

## 4.2. Education and training policy

### 4.2.1. Education

The education system of the Russian Federation has been under reform since the early 1990s. Initially, the reform was centred on the transition from a unified and standardized education system to a differentiated and open one, aimed at consolidating national identity and easing the transition to a market economy. The new stage of the reform – which started with the adoption in 2000 of the National Concept of Education (up to 2025) – includes the establishment of a new education management system, the introduction of the Unified State Examination, a revised financing mechanism and the adoption of new standards for general education, giving schools more autonomy in designing curricula. This was accompanied by increasing public spending (from 3.6 per cent of GDP in 2003 to 4.3 percent in 2010). Such investment, however, is still below the average spending recorded by OECD countries (6.3 per cent of GDP in 2010). Box 4.6 below summarizes the key features of the Russian education system.

#### **Box 4.6. The education system in the Russian Federation**

In the Russian Federation the pre-primary education level includes children from the ages of 1 to 6 years and, since 2013, it is part of the general education system. Compulsory education starts at the age of 6 and continues up to the age of 17. It comprises 9 years of basic general education (primary and lower secondary education) and 2 years of upper secondary education, typically provided in single-structure schools.

Upper-secondary education is divided into the general education stream that prepares students for higher education, and the vocational stream that prepares pupils both for the labour market and for higher education. Until 2010, the secondary vocational stream included initial vocational education (IVET) lasting 2-3 years and secondary vocational education (SVET) lasting additional 1-2 years and giving access also to tertiary education. According to the reform approved at the end of 2012, IVET is part of vocational education and provides training for skilled workers; SVET is divided into two streams, one for skilled workers and one for middle-level managers.

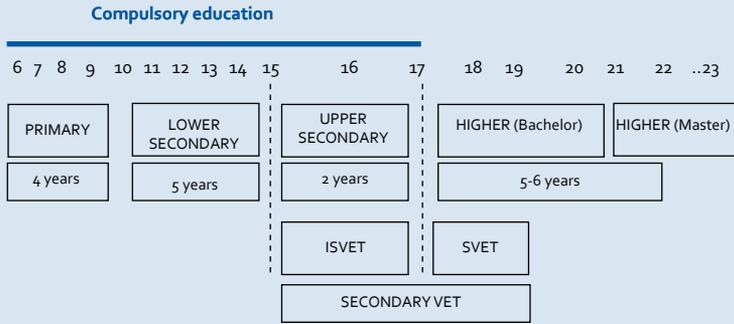
Since 2001, students undergo the Unified State Examination (USE) at the end of general education, which also serves as an entry exam for university. The USE is aimed at measuring the quality of education across schools and regions; verifying compliance with common standards; decreasing the practice of informal payments to enter university; and increasing access to higher level education for students from rural areas and low-income families.

Based on the Bologna Declaration, signed by Russia in 2003, the five-year tertiary education model was replaced by a two-tier system of bachelor and master

### Box 4.6. The education system in the Russian Federation (continued)

studies. The figure below presents the structure of the education system in the Russian Federation, including the most recent reforms.

#### Russian education at a glance



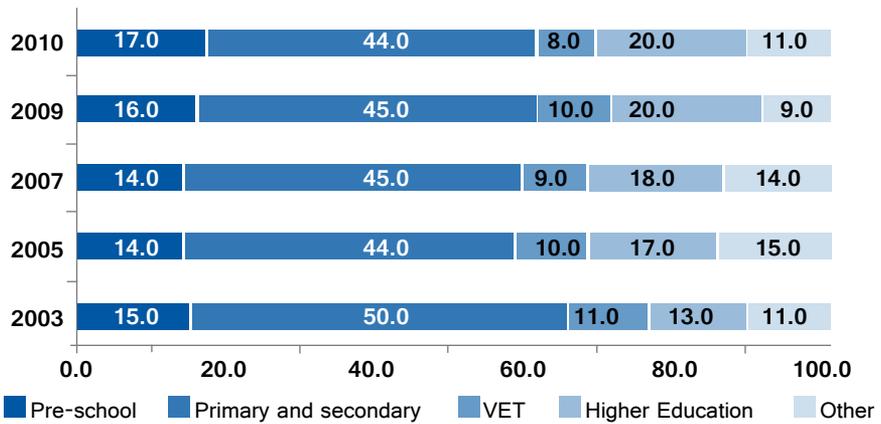
Source: World Bank, The education system in the Russian Federation, World Bank, Washington D.C. 2012; OECD, Economic Surveys: Russian Federation 2013, Paris, 2014.

Since 2004, the management of the education system is a responsibility shared among federal, regional and municipal authorities. At federal level, the Ministry of Education and Science is responsible for the development of national policies on education, research, technology and innovation. The Federal Service for Supervision on Education and Research is responsible for monitoring the implementation of education policies; licensing and accreditation of education and research institutions; and recognition of degrees awarded abroad. The Federal Institute for Education Development provides methodological support to the strategic directions of education policy, while the Federal Institute for Education Measurement is responsible for the development of standardized testing (Unified State Examination). At regional level, education management is provided by territorial authorities (departments, committees for education or offices of local administration), which administer education services in their jurisdiction. Local authorities are responsible for the implementation of education policies; financing of compulsory education; establishment, re-organization and closure of education institutes; school construction and maintenance; and the definition of national and regional components of educational standards.<sup>81</sup>

<sup>81</sup> UNESCO, World data on education 2010/11, Russian Federation, 2011.

The structure of education financing changed dramatically in the last few years, due to a decreasing number of students (Figure 4.3). Expenditures remained fairly stable for pre-school and vocational education. Primary and secondary education, conversely, experienced a sharp decrease of financing, while the resources invested in tertiary education in 2010 accounted for 20 per cent of all education spending

**Figure 4.3. Structure of education financing, 2003-2010**



Source: World Bank, *The education system in the Russian Federation*, Washington D.C., 2012

Since 2006, the Federal Government has been allocating funds to education policies under the aegis of Federal Target Programmes for the Development of Education, the latest one being for the period 2001-2015.<sup>82</sup> The purpose of the Target Programme is to ensure access to quality education and the relevance of education services. The main objectives are to modernize preschool and general education, as well as bring the content and structure of vocational education in line with labour market requirements. The funds of the Target Programme are allocated in three ways: i) through direct subsidies to all regions; ii) through subsidies allocated on a competitive basis (used, for example to remunerate best teachers and innovative schools); and iii) through matching (co-financed) grants.

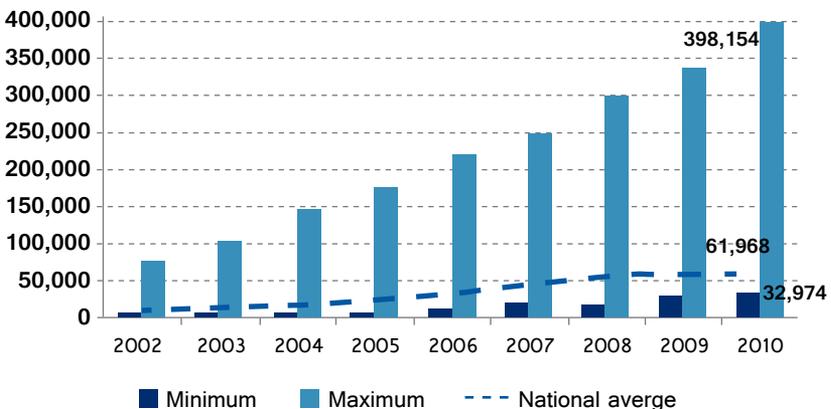
<sup>82</sup>The fact that education is a target programme (together with agriculture, housing and health) point to its importance among all State policies.

Since 2008, general education has been financed on a per capita (student) basis in all regions with the aim to increase the efficiency of budget spending and improve the quality of education. However, funding allocation rules differ from region to region, with three approaches being prevalent: i) funding based on minimum education standards, ii) on average unit cost (the most common approach), and ii) on category of education service. Performance-based salaries for teachers were introduced to increase wages and enhance incentives.

*As primary and secondary education is entirely financed from regional budgets, there are large differences in spending per student, with poorer regions spending only half the national average and richest regions spending up to six times the average (Figure 4.4). Such regional disparities in funding have led to large differences in the distribution of material resources to schools across the country, and therefore, the quality of outcomes.*

One of the results of disbursing funds through competitive subsidies (to support best performing schools) and matching grants is to widen differences between regions that can invest more resources and schools that started off in a better position compared to others.

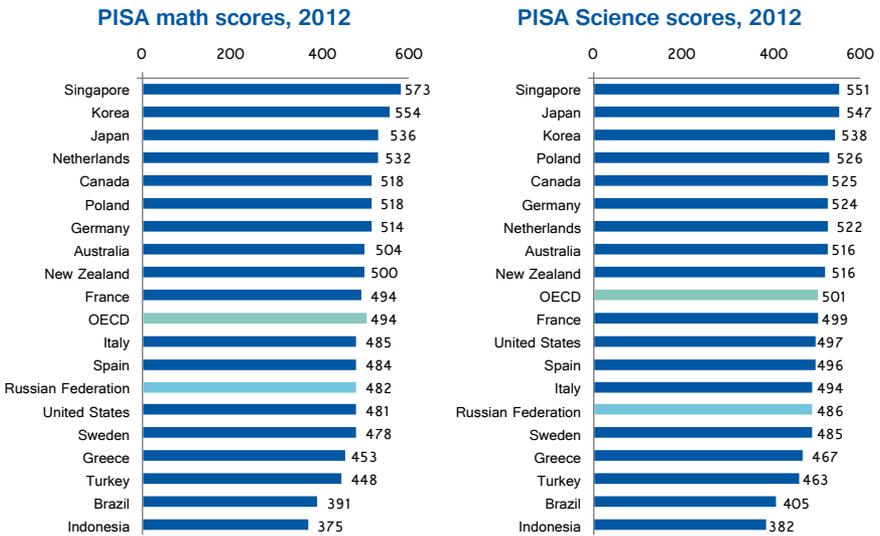
**Figure 4.4. Regional spending on general education per student, 2012 (RUB, current prices)**



Source: World Bank, *The education system in the Russian Federation, 2012 op.cit.*

The weakening of the quality of education in Russia in the last few years is confirmed by the scores obtained by Russian students in the Programme for International Student Assessment (PISA), still below the OECD averages despite the improvement recorded since 2009 (Figure 4.5).

**Figure 4.5. PISA scores for math and science, Russian Federation, 2012**



Source: OECD, PISA 2012 Results: What Students Know and Can Do: Student Performance in Reading, Mathematics and Science, Paris, 2013

Low performance in the PISA scores suggests that curriculum content and teaching methods are not effective in helping Russian students apply their knowledge to new situations. A number of factors may have contributed to this situation.

First, a recent study on the efficiency of education expenditures in Russia reveals that spending is significantly correlated with the volume of educational inputs (e.g. number and size of schools, student-teacher ratios and the average wage paid in the education sector, which reflects the average wage paid at local level). Higher spending per student, however, does not necessarily lead to better educational outcomes – measured in terms of the share of students failing the Unified State Exam and that scoring highest in the same exam. Other factors –such as the share of students in second shifts, proportion of students with pre-primary education, the share of tea-

chers in pension age, and the level of educational attainment of parents – have a stronger and more significant correlation to educational outcomes.<sup>83</sup> In addition, one of the challenges of the education spending reform is the limited autonomy given to municipalities and schools on how to spend resources. There are persistent problems associated with under-funding of education infrastructure, but the present system of allocations, regulations, and incentives leave little for capital investments and development (only 5-6 percent of the regional educational budgets goes to capital expenditures and investments), when nearly 23 per cent of schools are in need of capital repair and reconstruction.

Second, the introduction of the Unified State Examination may have reinforced the tendency of teachers to focus more on textbooks and curriculum requirements (e.g. encyclopaedic knowledge), rather than on improving student's ability to apply the knowledge acquired, problem solving and innovative thinking. This may, in part, be remedied by the greater autonomy granted to schools in designing curricula as of 2009 and the introduction in 2012 of new standards for primary and secondary education.

Third, quality may be related to the shorter duration of studies. In Russia education begins at 7 years of age compared to 4-5 years in OECD countries, implying that the number of years in which 90 per cent of the population is enrolled is 8 years compared to the 12 years in OECD countries. The average time spent on learning at primary level is also about half that recorded in OECD countries (450 hours 800 hours from age 7 to 10).

Finally, the country spends two times more on education per student at the tertiary level than at lower levels. Contrary to what occurs for primary and secondary education institutions, state tertiary institutions are mostly financed by the federal budget. The volume of government spending on higher education increased six-fold in the last years (from US\$2 billion in 2003 to US\$12.3 billion in 2010) to meet increasing demand. Between 2000 and 2010, the number of students paying tuition to study in higher education increased both in public and private institutions (by 22 and 34 percent, respectively). But being demand-driven, fee-based courses respond more to the requirements of students and families, rather than labour market needs.

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<sup>83</sup>World Bank, Social expenditures and fiscal federalism in Russia, World bank, Washington D.C., 2011

Before the transition to a market economy, the rates of return to higher education were relatively low (in the range of 2 to 3 per cent). Education returns rose to about 7 to 8 per cent in the first five years of transition and by an additional 2 to 3 per cent later on, stabilizing at 8 to 10 per cent per additional year of study.<sup>84</sup> When returns are differentiated by level, vocational education tends to yield higher payoffs than general education (by about 5 per cent). Tertiary professional and technical colleges enjoy a wage premium of 13 per cent for men and 20 per cent for women. The fact that education returns stayed high despite the increasing supply of educated workers indicates that the demand remained strong beyond the transition period. However, there are signals that returns are decreasing, due to the over-supply of graduates in certain disciplines (with over 50 per cent of university students enrolled in economics and humanities) and the limited innovation, business sophistication and technological readiness of enterprises, which limit their absorption capacity of highly educated workers. This situation leads to high rates of over-qualification among university graduates (38.8 per cent of young tertiary graduated workers as shown in Table 2.5 in Chapter 2).

#### 4.2.2. Vocational training and lifelong learning

Between 2000 and 2010, the number of students attending initial vocational education and training (IVET) decreased by 41.4 percent, lowering the coverage ratio from 22.3 per cent in 2000 to 21.5 per cent in 2010. Coverage, however, has been increasing since 2008 due to negative demographic trends. Young women enrolled in initial VET represent 35.8 per cent of the total. The number of students attending secondary vocational education and training (SVET) also declined, but by only 10 per cent. The secondary VET coverage ratio, as a result, increased from 33.5 per cent in 2000 to 38 per cent in 2010.<sup>85</sup> Young women represent 50.4 per cent of the total enrolled in secondary vocational education.

The share of GDP per capita earmarked for vocational education increased from 14.4 per cent in 2003 to almost 20 per cent in 2009, to then drop to 17.3 per cent in 2010. The share of public expenditure on vocational education in total education spending also decreased (from 11 to 8 per

<sup>84</sup>World Bank, Skills shortages and training in Russian enterprises, World Bank Policy Research Paper 4222, Washington D.C. 2008

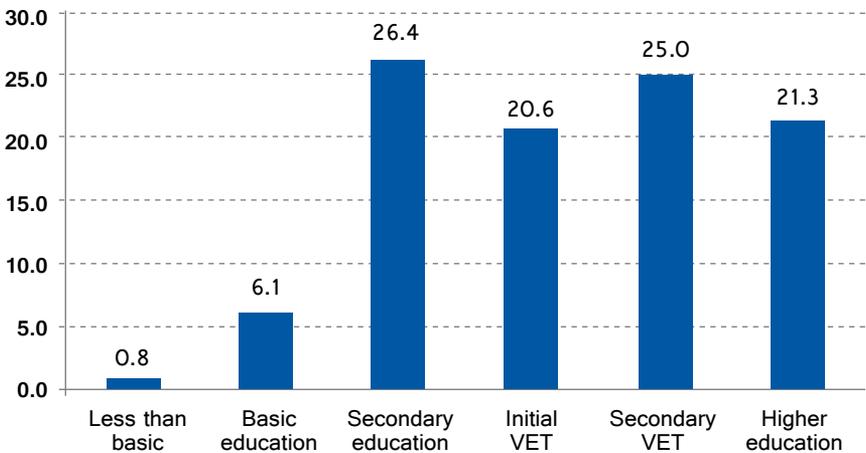
<sup>85</sup>World Bank, The education system in the Russian Federation, Washington D.C. 2012, op.cit.

cent of total education spending), reflecting the decline in the number of students and the closure of a number of schools.

The vocational education system is still characterized by narrow specializations that do not respond to labour market requirements. Although many regions are trying to adjust VET offering to labour market needs, resources are often insufficient to arrest the decreasing attractiveness of this stream among young people. The underperformance of the system can be attributed to two main factors. *First, VET institutions have been underfinanced for the last two decades. This caused significant delays in the modernization of the system in comparison to the emerging requirements of regional labour markets. Second, there is a mismatch between the number of students studying in educational institutions, their specializations and the real needs of the regional economy.*

*This mismatch is evidenced by the share of youth with initial and secondary vocational education who are unemployed (nearly 45.6 per cent of total youth unemployed in 2011, see Figure 4.6) and by the distribution of secondary vocational education students across streams (with one quarter attending economics, health and education courses).*

**Figure 4.6. Distribution of youth unemployment by educational attainment, 2011**



Source: ROSSTAT, Labour Force Survey, 2011

*Finally, the 25.5 per cent share of university students that are graduates of vocational schools indicates that young people use this education stream more as a step to higher education – rather than the labour market – but also the relatively low value of a vocational education diploma.<sup>86</sup> In addition, national figures reveals that employers prefer to hire university graduates, even for jobs that do not require higher education, fuelling the relatively high rates of over-qualification among youth.*

*Better cooperation with enterprises, revising the system of specializations on the basis of updated vocational standards and introducing in the curricula a mandatory period of enterprise-based learning– currently being considered by the authorities – would improve the alignment of vocational education outcomes to enterprise requirements and would ease young people’s transition from school to work.*

The share of Russian adults (aged 25 to 64) engaged in non-formal education in 2011 was around 13 per cent, much lower than the share recorded in the EU27 countries in the same year (around 30 per cent). The low share of participants in lifelong learning is attributed to the lack of technological innovation in many economic sectors and to the limited number of training programmes able to provide the competencies required by enterprises.

Enterprise based data show that in 2011 the spread of in-service training was higher among larger, export-oriented firms, in enterprises that were mature and that invested in research and development. The skill groups more likely to receive in-service training were managers, professionals, and skilled workers (10, 11 and 8 per cent, respectively). To summarize, enterprise data show that i) the educational and training system at vocational secondary level continues to be characterized by deteriorating quality and lack of response to labour market needs; ii) export-oriented and competitive enterprises invest more in workforce development, compared to less productive enterprises, where high labour turnover inhibits training; and iii) most enterprises do not responded to skill shortages by training their employees in-house or by training more of them, despite the productivity and wage gains resulting from such investments and the tax exemption introduced; and iv) firms have to invest significant amounts of time in filling vacancies, especially at higher skills level.

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<sup>86</sup>Kochetov A.N., “Professional education and the labour market” Russian Education and Society, vol. 54, no. 3, March 2012

### 4.3. Labour market policies and institutions

The main features of the employment policy of the Russian Federation till 2020 are set forth in the draft *National Programme on Employment Promotion*.<sup>87</sup> The Programme comprises three areas of action: employment promotion, migration of skilled foreign workers and development of labour market institutions. The National Programme aims at addressing a number of labour market challenges, namely widespread differences in regional labour market performance; skills shortages and skills mismatches; low mobility of workers; poor enforcement of labour law; and limited quality of labour and employment services.

The overall investment required to achieve these objectives is estimated at RUB 597.7 billion (equal to 1.1 per cent of GDP at 2011 prices), mostly provided by the federal budget (89 per cent). Most of the funds (0.68 per cent of GDP) are to be invested in active labour market programmes, unemployment benefits, labour mobility and improvement of the labour market information system. Approximately 0.24 per cent of GDP would go to the promotion of labour migration of skilled foreign workers and the return of skilled Russian living abroad, while the remaining amount (equivalent to 0.04 per cent of GDP) is to be invested in the development of labour market institutions (qualification system, wage increases for officials providing municipal employment services, strengthening of labour inspection and promotion of occupational health and safety).

The *National Programme* appears to rely exclusively on supply-side interventions, with no measures envisaged to address labour demand constraints. These latter may possibly be dealt with by other national programmes – currently under preparation – but such a framework poses serious problems of policy coherence and coordination.

***The National Programme on Employment Promotion contains no specific objective on youth employment, relying on the expansion of overall employment as a means to improve youth labour market outcomes. However, the labour market trends analyzed in previous chapters show that most of the employment gains recorded since the early 2000s were reaped by workers aged 25 and over. The only action planned in the Programme to promote youth employment is an expansion of the internship programme for graduates aged 18 to 20 years.***

<sup>87</sup>Prepared by the Employment Department of the Ministry of Labour and Social Policy, the National Programme on Employment Promotion has not been officially approved yet.

The National Programme as it stands today fails to recognize three important issues. The first is the relative large share of low productivity enterprises able to survive only by containing labour costs and exploiting available fixed assets. Many of these enterprises rely on atypical forms of work, low wages and informal arrangements to contain production costs. As young people are more willing to accept these forms of work to gain a foothold in the labour market, failure to act will affect young people more than other group of workers.

Secondly, the Programme fails to systematically address the specific barriers that young people face in getting employment, namely the quality of skills acquired in the education system (and the ability to use the knowledge acquired in a work setting) and the lack of work experience – highly valued by employers. Whereas the development of occupational standards will, eventually, have an impact on the relevance of education for the labour market, this is a longer-term endeavour that does not address the skill gaps faced by today's young unemployed and workers.

Finally, the National Programme is silent on the measures to be deployed to reach the target to create/modernize 25 million jobs, envisaged by the *Long-Term Economic Policy*. The increase of labour productivity by 1.5 times, on the other hand, is expected to be achieved by increasing human capital (through training and re-training of registered unemployed), promoting health and safety in the workplace and increasing labour mobility.<sup>88</sup> These actions alone, however, are unlikely to achieve the target labour productivity growth (see Box 4.7).

#### **Box 4.7. Determinants of labour productivity**

Research on the determinants of labour productivity in a number of developed and emerging countries confirms the positive and significant role of education and training (human capital), Research and Development (R&D) investment, financial sector development, Foreign Direct Investments (FDIs) and sectoral distribution of employment for labour productivity growth. These factors alone explain the productivity gaps found among countries at different income levels. In the presence of accelerating technological change, job-related training becomes particularly important for workers to update their skills. A research

<sup>88</sup>Labour productivity measured in terms of GDP per hour worked increased rapidly from 2003 to 2008. From 2008 to 2010, labour productivity fell (it amounted only to 43 per cent of the labour productivity of high-income OECD countries). World Bank, Russian Economic Report, April 2012, op.cit.

### Box 4.7. Determinants of labour productivity (continued)

conducted on the role of vocational training in increasing labour productivity in European countries finds that one extra hour of vocational training per employee contributes to accelerate the growth rate of labour productivity by 0.55 percentage points. When the percentage of highly educated workers is increased by 1 percentage points, productivity raises by 0.70 percentage points. The joint effect of the factors related to the quality of labour (1.25 percentage points) is similar in magnitude to the increase in productivity caused by one percentage point growth of R&D expenditures (1.19 percentage points).

These findings call for a reappraisal of the policies related to education, active labour market policies, and R&D programmes. The main lesson learned is that they cannot be designed in isolation. Conditional on sectoral specificities, job training and R&D activities should be seen as part of the same set.

Source: Choudhr, M.T. Determinants of labor productivity: An empirical investigation of productivity divergence, University of Groningen, 2009; Sala H., Silva J. I., Labor productivity and vocational training: Evidence from Europe, IZA Working Paper 6171, 2011

The decline of the working age population in the next decade is expected to be addressed through a combination of policy options in three areas, namely incentives for workers to remain longer in the labour market (flexible working time and preferential pensions; promotion of labour mobility see Box 4.8); and migration to bridge skills shortages.<sup>89</sup>

<sup>89</sup>A recent research shows that 45 per cent of expanding Russian firms (and 60 per cent of SMEs) face skills shortages. However, skilled international migration currently does not appear to be filling gaps in innovative sectors, but rather fill generic managerial and professional posts. Commander S., Denisova I., Are skills a constraint on firms? New evidence from Russia, IZA Discussion Paper DP No. 7041, 2012

#### Box 4.8. Policies to promote youth labour mobility across regions

The promotion of geographic mobility is a key enabler for a more efficient labour market, but also for youth employment, as it has the potential to enhance youth employability, wages and career prospects. In addition, since the propensity to move falls with age, mobility policies may have a larger impact on young people compared to other age groups. In the Russian Federation, the key factors that constraint internal labour mobility mainly relate to poverty traps and the costs of migration. Many young individuals who would migrate cannot afford to do so, even though migration would improve their employment and earning opportunities. Internal migration costs are affected by geographical distance and the high housing prices in richer regions. Since young people are more likely to be unemployed or to earn lower wages compared to adults, have typically little savings and lower access to finance, they are less able to afford migration costs. The range of policy options that may be considered for improving geographical mobility span from labour market (passive and active), education, social integration and housing policies. Their interaction ensures that the impact of each is maximized.

Research has found that income differentials – net of migration costs – have a stronger effect on the probability to migrate of young people compared to adults (since the returns from migration are higher and the opportunity costs lower for youth). This implies that youth mobility flows are largely determined by the differential in labour market outcomes (in terms of wages and employment opportunities) in origin and destination regions. **Local economic development** policies, focused on growth and job creation, would reduce the incentives to migrate to other, more developed regions in the short term, and attract skilled workforce from other parts of the country, in the long run.

Several studies indicate that relatively generous **income replacement** during unemployment tend to increase, rather than decrease, labour mobility. This is because the costs of job search are higher at the national level than at the local level. Higher income-replacement benefits relax liquidity constraints and increase the propensity to search for a job outside the local community. To avoid the risks that a generous benefit system entails, countries apply limitations to duration and replacement levels and link benefit receipts to active job search and the taking up of jobs also in other parts of the country. Therefore, policies that ensure that young people have access to well-designed income replacement schemes, linked to active labour market policies, would increase labour mobility in the country.

There are two main ways in which **active labour market policies** can promote labour mobility. First, by providing labour market information (job vacancies, conditions of work, skills requirements and so on) and job search assistance, employment services reduce the costs associated with job search in other regions. They can also assist in acquiring the skills required by employers in the region of destination. Second, by providing relocation assistance (information on the region of destination, skills training, travel grants, tax deductions on earnings and so on) these policies substantially reduce migration costs.

**Education** is a strong driver of youth geographical mobility. First, the relationship between higher levels of education and mobility presents two key

#### **Box 4.8. Policies to promote youth labour mobility across regions (continued)**

features, namely: i) individuals with higher levels of education are those most likely to move (as the costs of migration are likely to decrease as skills levels increase), and ii) self-selection of migrants across destination regions. Regions with high skills rewards (where educated workers earn relatively more) attract a disproportionate share of higher educated youth. Second, migration for education purposes (especially at tertiary level) is a key determinant of youth migration flows, both domestically and internationally. Education policies can act on these drivers by making higher education affordable through scholarships and grants to a larger pool of young people, by promoting students' exchange programmes, by ensuring affordable housing and making education credentials transferable.

The effect of the above mentioned policies on geographical mobility is greater when they are accompanied by other social policies aimed at improving the social integration of young migrants in destination regions. The most important are housing policies (that reduce the cost of relocation) and anti-discrimination policies (to ensure that migrants and their families have access to public services and employment opportunities on an equal basis).

Source: ILO, How can national policies address internal labour mobility? A compilation of practices, Geneva, Mimeo 2013

The final set of policies aimed at addressing the aging of the working age population is to increase activity rates by bringing into the labour market inactive individuals who are willing to work, such as individuals with family responsibilities (see Box 4.9).

#### **Box 4.9. Policies to tackle the labour market consequences of demographic changes**

One of the key mechanisms to address the labour market effects of demographic changes is to increase the labour force participation rate generally, and especially among young women who are more likely than their male peers and adult women to be inactive due to family responsibilities.

Measures targeting young women who are inactive, but willing to work, typically fall within three main categories of policies: i) welfare policies, ii) active labour market policies and iii) policies which promote anti-discriminatory and family-friendly workplaces. These policies are mutually reinforcing and should be deployed in concert to increase the number of young women who join the labour force and ensure that those who are in the labour market remain there throughout their working lives. For instance, a neutral tax treatment of second earners would have little impact in the absence of affordable child care or opportunities for part-time work. Promoting alternative career pathways for young women would have little effect if they not accompanied by well designed and enforced anti-

### Box 4.9. Policies to tackle the labour market consequences of demographic changes (continued)

discrimination policies and measures to reconcile work and family life.

**Welfare policies** that create incentives for women to join the labour force and achieve work-life balance are key determinants of raising women's labour force participation rates. Three policies are particularly relevant in this area: i) tax policies that use individual taxation systems where the second earner is taxed less heavily than the primary earner for the same level of additional earnings; ii) childcare subsidies, which affect both financial incentives to work and work-life balance reconciliation; and iii) paid parental leave, which provide incentives for sharing leave between the two parents and grant the possibility for women to re-enter the labour market after giving birth.

All types of **active labour market programmes** generally have a more positive effects on women compared to men, especially in countries where female labour force participation rates are relatively low. Career guidance and employment counselling may help in steering young women's careers towards sectors where they are underrepresented and where there is high demand for labour. Skills-training programmes may affect women's participation in the labour market both directly (by increasing their employability) and indirectly (by affecting women's level of wages, training programmes may raise the incentives for women to enter and remain in the labour market). Wage subsidies, when well targeted, can create employment and compensate for initial lack of skills or experience. Finally, entrepreneurship development programmes may address the higher skills, capital and network barriers that young people and young women, specifically, face in setting up their own business.

Finally, policies that promote **anti-discriminatory and family-friendly workplaces** ensure fair recruitment practices, so that women stand an equal chance of entering the labour market, and flexible working hours that allow both men and women to reconcile work with family responsibilities. Increasing the availability of part-time work also tends to raise women's participation. However, when part-time work entails a wage penalty, low social security coverage, job insecurity, and little training, it risks marginalizing women rather than integrating them. In such instances, policy should aim at fostering better access to full-time jobs, or reduce the negative future career consequences of a period spent in part-time work.

Ministry of Labour and Social Protection, National Programme on Employment Promotion, August 2012

Finally, the National Programme envisages a number of policy actions specifically aimed at improving the quality of work.<sup>90</sup>

- *Better enforcement of labour laws and increased efficiency of the inspection system:* The targets envisage decreases in the rate of work-related fatalities (which was 1,824 in 2011 down from 2,004 in 2010), occupational diseases, and the share of workers in jobs not in compliance with health and safety regulations, as well as increases in the number of labour law violations redressed (shifting of workers from informal to formal employment). Within this area of action, the Programme also includes incentives to employers to improve working conditions and to formalize labour relations.
- *Improvement of the qualification, training and re-training systems.* The target is to develop 800 occupational standards in line with labour market requirements by 2014 and to increase the share of registered unemployed referred to training and re-training programmes (from the current 8.5 per cent to 20 per cent). The development of occupational standards is expected to improve the quality of vocational education.
- *Development of labour market institutions.* The targets relate to the share of jobseekers placed in a job by the employment services (from 63 to 70 per cent); the share of registered long-term unemployment (from 13 to 5 per cent); the number of jobs equipped for workers with disabilities (14,200 by 2015); the share of unemployed relocating for work purposes with the assistance of the employment service (from 0.3 to 3 per cent of registered unemployed); and the ratio of the unemployment benefit to the minimum income (from the current 40 per cent to 100 per cent by 2020). The Government also expects to develop a labour market forecasting system to inform career guidance and employment counselling services.

### 4.3.1 Wage policy

The most characterizing feature of the Russian wage-setting mechanism is the importance of the variable part of workers' wages, which represents 40-50 per cent of the total wage and depends on the performance of the enterprise. In larger enterprises the setting of the variable part of

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<sup>90</sup>Ministry of Labour and Social Protection, National Programme on Employment Promotion, August 2012

the wage is relatively formalized, while it is not uncommon for newly-established and smaller enterprises to pay a low base salary – on which taxes and social contribution are paid – and provide additional cash payments to workers (envelope wage).<sup>91</sup>

The federal minimum wage is set by law after discussion in the tripartite commission. The minimum wage level more than doubled in the last four years (from RUB 2,300 at the beginning of 2009 to RUB 5,205 in 2012). Despite these increases, however, the ratio of the minimum wage to the average wage is just over 19 per cent, with the minimum wage remaining below the minimum subsistence level (set at RUB 6,259 in 2012) by 20 per cent.

After the decentralization reform of 2007, regions have the right to set a minimum wage that is higher than the minimum established at federal level. In regions with medium or high average wages, the share of workers earning the minimum wage is negligible, while in poorer regions their share is substantially higher (especially for workers engaged in municipal services).

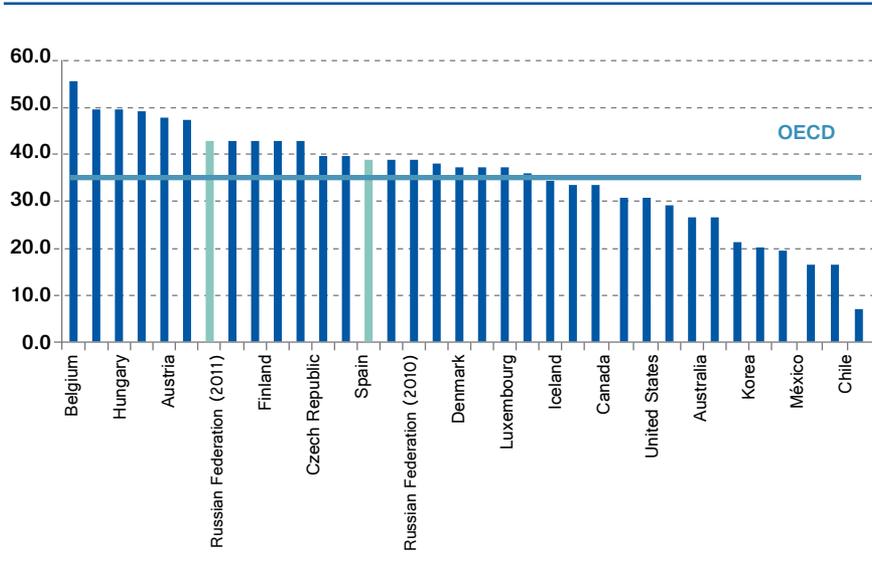
*The minimum wage as a labour market institution is hardly effective due to its low level and, foremost, to poor enforcement. In the absence of enforcement policies any increase of the minimum wage is likely to have the perverse effect of raising incentives for under-reporting, especially in those economic sectors where the minimum wage represents a substantial share of the average wage – such as agriculture (where the minimum wage comprises 42 per cent of the average wage for the sector), hotels and restaurants (34 per cent) and education (32 per cent) – sectors where youth employment is relatively high (see Figure 2.4 in Chapter 2). In light of the above, the minimum wage does not appear to be a limiting factor in employment growth, although – like employment protection legislation – it may have an impact on its distribution.* Low wages and poor working conditions allow least productive enterprises to remain in the market, but decrease job attachment. This is evidenced by high job turnover, with about 30 per cent of workers leaving their job each year.<sup>92</sup>

<sup>91</sup>The share of workers receiving envelop wages is estimated at 19 per cent of total employment. See Lehmann, H., Zaiceva A., Informal employment in Russia: Definitions, incidence, determinants and labour market segmentation, OECD Economics Department Working Papers, No. 1098, 2013

<sup>92</sup>OECD, Economic Surveys: Russian Federation 2013, Paris, 2014.

*Payroll taxes and social security contributions probably play a more significant role in determining labour market outcomes and informality in the Russian Federation and especially among youth.* The tax wedge, after the 2011 increase in social security contribution rates, increased from 39 per cent (for a single worker with no children earning the average wage) to 43 per cent, well above the average tax wedge reported in OECD countries in 2011 (35.3 per cent).<sup>93</sup>

**Figure 4.7. Tax wedge, Russian Federation and OECD countries, 2011**



Source: Calculation based on Ministry of Labour and Social Protection figures (2010 and 2011); OECD, Taxation database, 2011 downloadable at <http://www.oecd.org/ctp/tax-policy/>

Until 2010, the Russian Federation had a regressive social contribution system. In that year a 26 per cent flat-rate social security contribution system was introduced, with the only exceptions being for agriculture and new or innovative industries. In 2011 the social security contribution rate increased to 34 per cent and then decreased in 2012 to 30 per cent for earnings up to twice the level of the average wage. Today, the only element of progressivity of the tax wedge is that a very limited number of workers have rates at the lower rate of 20 per cent, applicable to earnings below

<sup>93</sup>The social security contribution rate, paid totally by employers, was set at 30 per cent for workers earning up to RUB 512,000 per year and to 34 per cent for those earning over this threshold. This makes the social contribution system regressive, especially for workers earning the minimum or average wage.

the RUB 512,000 annual threshold. This means that the many low-paid workers still face the relatively heavy burden of 30 per cent. Such situation will most likely push firms – especially those for which labour represents a large share of production costs – towards the informal economy.

In countries where non-wage labour costs are too high, their reduction has increasingly been considered as a tool for reducing unemployment and informality, especially among youth. An analysis of labour costs in the countries of Central and Eastern Europe found that youth unemployment tends to be higher in countries where payroll taxes are higher.<sup>94</sup> This is confirmed by a research on social security-driven tax wedges in Russia and Ukraine, which estimates that a 10 per cent reduction of the tax wedge for low-skilled workers would result in 6 per cent employment growth and reduce informality, more widespread among young workers compared to adults.<sup>95</sup> Reducing non-wage labour costs may, therefore, result in youth employment gains, especially for low-paid young workers.

### 4.3.2. Employment protection legislation

Employment protection legislation (EPL) consists of labour law provisions governing the recruitment and dismissal of workers, and particularly regulations on temporary and regular contracts and collective dismissals. The impact of employment protection legislation on youth employment is a matter of diverging interpretations. On the one hand, it is argued that stricter EPL increases dismissal costs and reduces the flexibility of enterprises to adjust to the economic cycle. This would negatively affect employment in general, and youth employment in particular, by favouring those who are already employed to the detriment of those seeking work (the “insider-outsider” effect). On the other hand, EPL is thought to ensure basic security, increase incentives for employers to invest in human capital and encourage cooperative labour relations, which should all lead to improvements in productivity, competitiveness and overall efficiency.<sup>96</sup>

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<sup>94</sup>Cazes, S., Nesporova, A. (eds), *Flexicurity: A relevant approach in Central and Eastern Europe*. Geneva, 2007

<sup>95</sup>M. Gora et al, *Social security driven tax wedge and its effects on employment and shadow employment*, DIW, Berlin, 2008.

<sup>96</sup>ILO, *Improving prospects for young women and men in the world of work: A guide to youth employment*, 2004.

### Box 4.10. Employment Protection Legislation (EPL) indexes in the Russian Federation, 2012

Employment protection legislation is described along 21 basic items, grouped in three main areas: (i) employment protection for workers against individual dismissal; (ii) specific requirements for collective dismissals; and (iii) regulation of temporary forms of employment. Each of the 21 basic items is scored on a scale from 0 to 6, with higher scores representing stricter regulation. These scores are then transformed into weighted averages to build the four sets of summary measures. The EPL scores for the Russian Federation in all the sub-indexes are shown below.

Level 3 Scale 0-6	Level 2 Scale 0-6	Level 1 Scale 0-6	Sub-index	Index	
Regular contracts	Procedural inconvenience	1. Notification procedures	4.00	2.05	
		2. Delay to start notice	2.00		
	Notice and severance pay for no-fault dismissal	3. Notice period after	9 months		3.00
			4 years		2.00
		4. Severance pay after	20 years		1.00
			9 months		3.00
	Difficulty of dismissal	5. Definition of unfair dismissal	4 years		3.00
			20 years		1.00
		6. Trial period	5.00		5.00
7. Compensation			4.00		
8. Reinstatement			1.00		
9. Maximum time for claim	6.00	1.00			
Temporary contracts	Fixed term contracts	10. Valid cases for the use of FT contracts	2.00	0.75	
		11. Maximum number of successive contracts	1.00		
		12. Maximum cumulated duration	1.00		
	Temporary work agency employment	13. Types of work for which it is legal	14. Restriction on number of renewals	0.00	0.50
			15. Maximum cumulated duration	3.00	
			16. TWA authorization and reporting	0.00	
Collective dismissal		17. Equal treatment	0.00	0.43	
		18. Definition of collective dismissal	3.00		
		19. Additional notification requirements	0.00		
		20. Additional delays	3.00		
		21. Other special costs to employers	0.00		

Source: OECD, Employment Protection Legislation database, <http://www.oecd.org/employment/emp/oecdindicatorsofemploymentprotection.htm/>

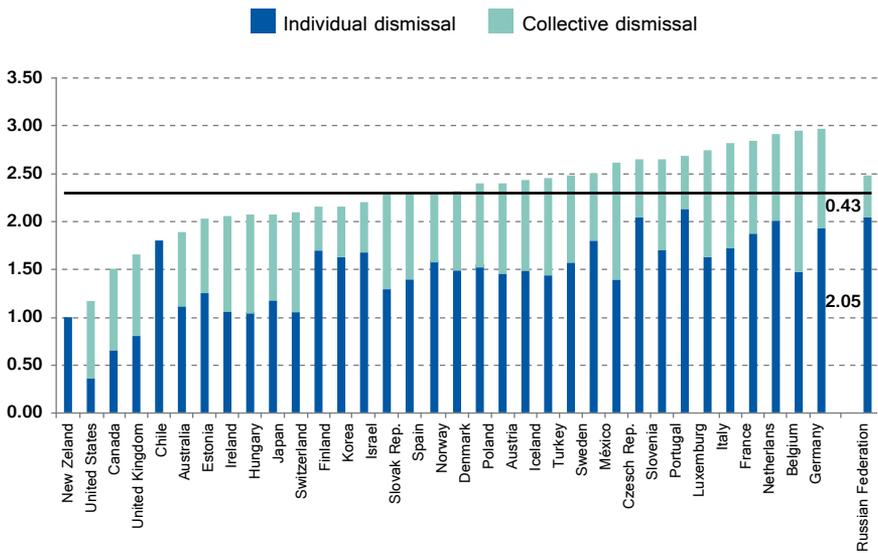
Overall employment protection legislation (EPL) in the Russian Federation is less restrictive than in OECD countries (Figures 4.8 and 4.9).<sup>97</sup> The index on individual and collective dismissal is slightly higher than the OECD average (2.48 and 2.29, respectively) due to the more restrictive rules governing individual dismissals. *The strictness of EPL for temporary contracts is much lower than the OECD average (1.25 and*

<sup>97</sup>The EPL index ranges from 0 (very liberal) to 6 (very restrictive).

2.08 respectively) due to the less restrictive rules governing both temporary contracts and temporary work agency (TWA) employment in the Russian Federation (Box 4.10).<sup>98</sup>

The index on individual dismissal is slightly higher than the average found in OECD countries, as notice period and severance allowance rules do not depend on tenure (two months notice and two months average wage for severance payment). This makes the dismissal of workers with short tenure rather costly. The index on collective dismissal, conversely, is less restrictive than the OECD average, since there are neither additional notification procedures nor additional costs for employers to dismiss workers collectively.

**Figure 4.8. Employment protection against individual and collective dismissal in OECD countries and the Russian Federation, 2013\***

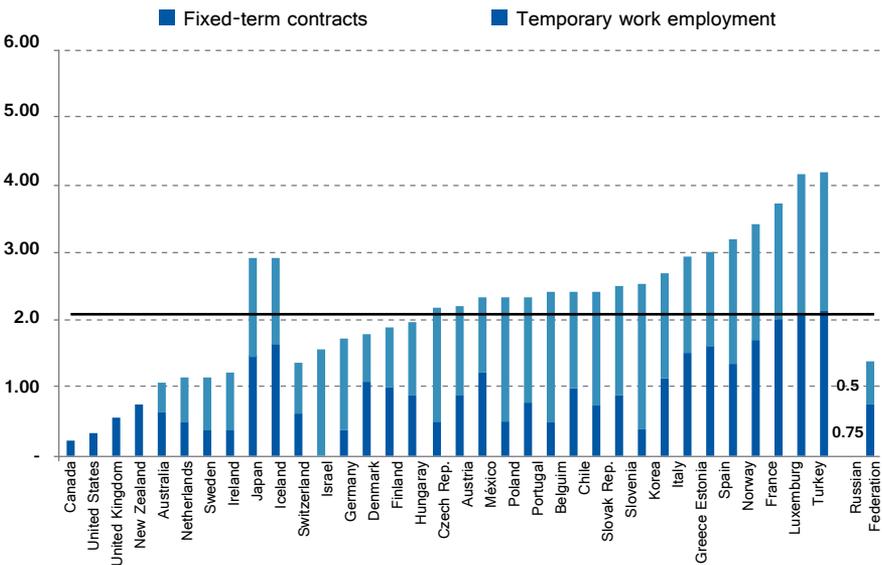


(\*) Data for the Russian Federation are for 2012, while for OECD countries for 2013. Source: OECD, Employment Protection Legislation database, <http://www.oecd.org/employment/emp/oecdindicatorsofemploymentprotection.htm/>

<sup>98</sup>The methodology to measure the strictness of EPL was recently revised, to include a more accurate assessment of national legislation, collective bargaining agreements and case law. Rather than being summarized in one unique measure, the strictness of EPL is now summarized into two measures, one for individual and collective dismissal and one for temporary contracts. See OECD, Employment Outlook 2013, Paris, 2013.

The indexes for fixed term contracts and temporary work agency contracts are among the less restrictive among all OECD countries (see Figure 4.9 below). A fixed term employment contract can be issued for a maximum of five years and for reasons and workers detailed in the Labour Code.<sup>99</sup> The rules governing fixed term contracts were amended in 2002 and in 2006, extending their use to a wider range of workers and situations. At present, small business (up to 20-35 employees) can hire fixed-term workers with no limitations, provided that the maximum duration does not exceed 3-5 years. Similarly, pensioners and students can be recruited under a fixed term contract without conditions. The rules governing temporary work agency employment are particularly flexible with the regard the type of work for which this type of employment is legal, the maximum duration of assignments and on authorization and reporting requirements.

**Figure 4.9. Employment protection on fixed term contracts and temporary work agency employment in OECD countries and the Russian Federation, 2013\***



(\*) Data for the Russian Federation are for 2012, while for OECD countries for 2013. Source: OECD, Employment Protection Legislation database, <http://www.oecd.org/employment/emp/oecdindicatorsofemploymentprotection.htm/>

<sup>99</sup>Article 59 of the labour Code specifies that temporary work contracts can be issued to substitute an absent worker, for seasonal work, or work beyond the normal course of business and limited in time, or internship and for temporary work and community services organized by the Public Employment Service. Workers that can be employed under a fixed term contract include: persons near retirement, persons whose health permits only work for a limited period, workers in the Far North, when such work entail a relocation, elected officials, performing artists, individuals enrolled in full time education and part-time workers.

The above mentioned indexes, however, do not capture the variation of EPL enforcement across Russian regions and the impact that this may have on regional labour market performance. A research conducted in 2009 reveals that: i) there are significant variations in enforcement across regions; and ii) violations of employment legislation were most frequent in the North and Far East and less frequent in more diversified economies with dynamic labour markets. This suggests lower demand for enforcement in these regions, since enforcement capacities are stronger.<sup>100</sup>

***The combined analysis of data on informal employment, labour turnover and shifts among labour market status points to a duality in the labour market (formal vs. informal workers).<sup>101</sup> Since young workers are more likely to be employed informally compared to adults (see Figure 2.5 in Chapter 2), they are more exposed to the detrimental effects a segmented labour market (wage gaps, lower access to training and social security, poorer working conditions or tenure, limited transitions to better jobs).<sup>102</sup>***

The monitoring of labour legislation and occupational safety is carried out by the Federal Labour and Employment Service, under the jurisdiction of the Ministry of Labour and Social Policy. Labour inspectors are located in regional offices. These offices are divided into health and safety, and labour legislation branches. At the end of 2011, there were 3,169 labour inspectors (e.g. one labour inspector for every 22,000 workers) – a decrease of nearly 6 per cent compared to 2010.<sup>103</sup> The number of inspectors is expected to decrease further in 2012 and 2013 (by 17 per cent, approximately), pursuant to the decision to decrease the overall number of employees of the Federal Labour and Employment Service at regional level. In 2010, the government limited the number of inspections in each particular business to maximum one every three years.

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<sup>100</sup>Gimpelson V., Kapeliushnikov R., Lukiyanova A., Employment Protection Legislation in Russia: Regional enforcement and labour market outcomes, IZA Discussion paper No. 4484, 2009. Such a research, however, was carried out on 2007 data, when the EPL index for the Russian Federation was 3.6.

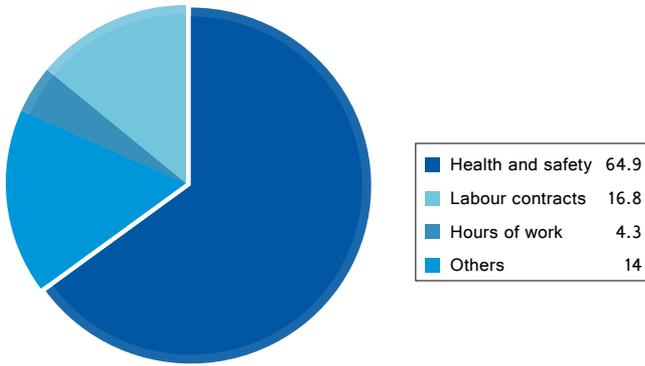
<sup>101</sup>Nearly one third of workers quitting an informal job found a new job in the informal economy, compared to 83 per cent of formal workers quitting and finding a job in the formal economy. Lehmann, H., Zaiceva A., Informal employment in Russia: Definitions, incidence, determinants and labour market segmentation, OECD Economics Department Working Papers N. 1098, 2013.

<sup>102</sup>Labour market segmentation also has macroeconomic implications, such as lower productivity and higher employment volatility. See Deakin, S., Addressing labour market segmentation: the role of labour law, ILO, Geneva, 2013.

<sup>103</sup>The ILO benchmark for transition countries is 1 inspector for every 20,000 workers, while the ratio for developed countries is 1:10,000. In terms of labour inspectors, the Russian Federation scores below a number of Central European countries, like Hungary, the Slovak Republic, Poland and the Czech Republic. OECD, Employment Outlook, 2008.

In 2011, labour inspectors carried out more than 156,000 inspections (48 per cent of which were in small enterprises), detecting over 846,000 violations (Figure 4.10). Inspections mainly targeted wholesale and retail trade (17.3 per cent of all inspections), manufacturing (13.9 per cent), construction (12.4 per cent), and other services (8.1 per cent).

**Figure 4.10. Violation of labour legislation, 2011**



*Source: Federal Service for Labour and Employment, Annual Report, 2011 (in Russian only)*

Similarly to the prior year, the main violations detected in 2011 regarded health and safety in the workplace (including failure to train workers on health and safety and to provide personal protective equipment); violation of the prescription of labour law regarding employment contracts; wage arrears; as well as violation of collective agreements, hours of work and rest period regulations. Whereas violations of occupational health and safety decreased compared to 2010, those regarding hours of work, rest periods and labour contracts, increased.

Given the limited resources available, most inspections occur as a result of complaints or follow up of previous cases. The sanction system currently in force plays a limited role in preventing labour law violations. Sanctions are in the range of RUB 30,000-50,000 (approximately US\$ 1,000-1,700) and the suspension of activity up to 90 days. To make the system more effective, the government is considering raising sanctions up to a maximum of RUB 500,000 (US\$ 13,000).<sup>104</sup>

<sup>104</sup>One additional measure currently being considered is to devolve the responsibility of labour inspection to the regions. The extent of such decentralization measure is still unclear. However, article 4 of ILO Convention No 181, (Labour Inspection Convention, 1947) ratified by the Russian Federation in 1998, prescribes that in the case of federal States labour inspection is to be placed under the supervision and control of a central authority.

### 4.3.3. Passive labour market policies

The social protection system of the Russian Federation consists of several cash transfer schemes (See Annex 1). Social protection spending is the item that increased most in the last few years, to reach approximately 12.5 per cent of GDP in 2012 (advanced countries spend on average 14 per cent of GDP on social protection).<sup>105</sup> The largest share of social protection expenditures finances social insurance programmes (pensions, sickness, unemployment and maternity benefits), while non-contributory social assistance programmes account for approximately 20 per cent of total social protection expenditures. All social protection benefits in the last few years have increased in real terms (except child allowances). Pension expenditures increased the most (by 40 per cent in real terms) and now account for approximately 80 per cent of the total social protection expenditures.<sup>106</sup> Although the resources invested in social (non-contributory) programmes account for approximately 2.4 per cent of GDP, only a small fraction targets the poor. In addition, the few income-tested programmes designed to address the needs of vulnerable population groups have inefficient targeting and large leakages. The majority of these programmes are administrated by regional governments, with the federal budget covering only 10 per cent of all non-contributory expenditures.<sup>107</sup>

In Russia, there are two types of unemployment benefits, with a large pool of eligible recipients (41.5 per cent of registered unemployed in 2010, down from 48.2 per cent in 2009). The first is a contributory unemployment benefit available to individuals who worked at least six months in the prior twelve months. The benefit is 75 per cent of the previous wage in the first 3 months, 60 per cent for the following 4 months and 45 per cent thereafter. The monthly benefit is subject to a minimum and maximum threshold (RUB 850 and RUB 4,900 in 2011). The second is a flat unemployment assistance benefit (equal to the minimum unemployment benefit plus a regional coefficient) for twelve months. Unemployment assistance is available to individuals who do not qualify for the earnings-related unemployment benefit or have already exhausted it. Despite a five-fold increase since 2004, the amount of the unemployment benefit and the replacement rate are extremely low. In 2011, the minimum monthly benefit represented 3.5 per cent of the average wage and the maximum 20.6 per cent, an amount that is lower than the minimum subsistence income.<sup>108</sup> In

<sup>105</sup> IMF, Russian Federation, 2013 Article IV Consultation, IMF Country Report, 2013 op.cit.

<sup>106</sup> The nominal base pension increased by 30 per cent in 2009 and by 46 per cent in 2010.

<sup>107</sup> World Bank, Public Expenditures Review, 2011, op.cit.

<sup>108</sup> The minimum and maximum amount payable for the unemployment benefit is established by law annually.

some instances, unemployed individuals have access to additional benefits (such as housing, utility and medical care allowances), which increase the replacement rate. Few individuals, however, seem to take up these additional allowances.

*Neither the level nor the coverage of the unemployment benefit can be considered a constraint to active job search. Rather, the low level of the benefit may force individuals who cannot afford not to work to accept poor job offers, thus contributing to mismatch problems and low productivity. It also reduces the incentive to register with the Public Employment Service.* This is one of the reasons for the large gap between the number of individuals registered as unemployed with the Public Employment Service (1.1 million at the end of 2012) and that of unemployed persons detected by the Labour Force Survey (7.5 million).

In 2011, total spending on the unemployment benefit amounted to RUB 404 million (0.07 per cent of GDP), down from the peak recorded in 2009 (0.08 per cent of GDP). Public spending on unemployment benefits is forecasted to remain stable in the next few years, as the increase of the benefit level to the minimum subsistence level – which is planned by the National Programme on Employment Promotion – will be accompanied by a decrease in the number of registered unemployed. *Increasing the level of the unemployment benefit, however, needs to be accompanied by increase spending in active labour market policies to reinforce job search requirements and improve the assistance provided by the public employment services. An increase in the level of the unemployment benefit may also contribute to the reduction of informal employment, especially among low-skilled individuals.*<sup>109</sup>

#### 4.3.4 Active labour market policies

Employment promotion and unemployment protection programmes are the responsibility of the Federal Employment Service (FES), a department of the Federal Labour and Employment Service (ROSTRUD) under the supervision of the Ministry of Labour and Social Policy. Since 2007, as part of the decentralization reform, the regional public employment services have been subordinated to regional authorities and have gradually assumed the responsibility for administering and financing active

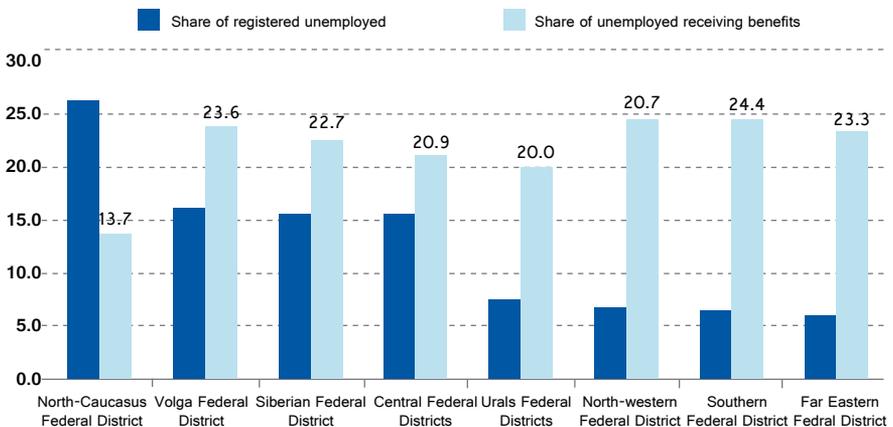
<sup>109</sup>OECD, Economic Surveys: Russian Federation, Paris, 2014, op.cit.

labour market programmes under the overall supervision of the FES. The only function managed by the federal level is the unemployment benefit system.

At the end of 2011, there were 4,430 labour and employment departments in the regions of the Russian Federation and approximately 2,150 employment centres. According to the information provided by the Federal Labour and Employment Service, 80 per cent of the employment service staff deals directly with clients.

The figures on registered unemployment reflect closely regional development and poverty gaps. At the end of 2012, North Caucasus accounted for the largest share of registered unemployed (26.2 per cent of the total), but had the lower share of registered unemployed receiving benefits (see Figure 4.11 below that shows the share of registered unemployed by district and the share of benefit-recipients on the total unemployed registered in each district). This is due to the long-term nature of unemployment in this District, where the majority of registered unemployed has already exhausted available benefits. The regions showing higher shares of benefit recipients over total registered unemployed were the Southern Federal District (24.4 per cent) and the North-Western District (23.7 per cent). The share of registered unemployed in this latter district, however, is among the lowest in all the Russian Federation (6.9 per cent of total registered unemployment).

**Figure 4.11. Registered unemployment and benefit recipients by Federal District, 2012**

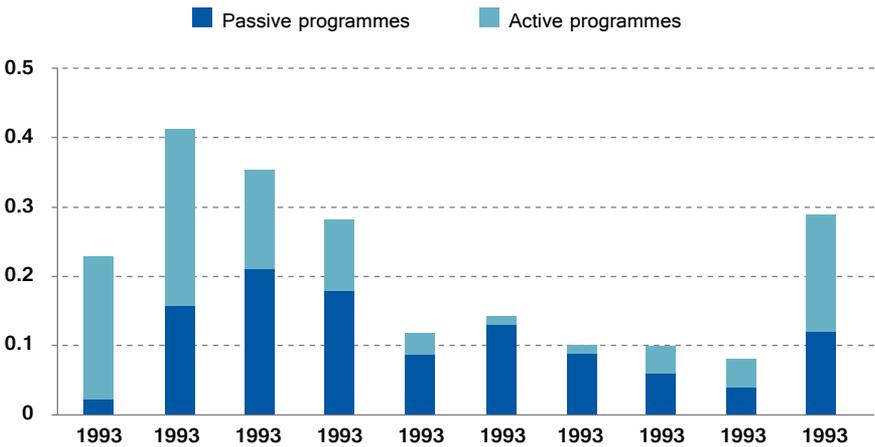


Source: Calculation based on ROSTRUD figures at <http://www.rostrud.ru/documents/25/>

The financing system of labour market programmes in the Russian Federation changed considerably in the last two decades. Before 2001, labour market programmes depended on the resources of the Employment Fund, which was financed by a contribution of employers (2 per cent until 1995 and 1.5 per cent thereafter) collected by regional governments. Until 1995 most of the resources of the Employment Fund were invested in active labour market policies (ALMPs).

From 1995, increases in the unemployment claim and declining resources caused a reduction in the funding of ALMPs in favour of passive programmes (Figure 4.12). The introduction in 2001 of the Unified Social Tax abolished the Employment Fund. Since then, active labour market policies have been funded by the federal budget through transfers to the regions.

**Figure 4.12. Labour market expenditures, percentage of GDP**



Source: OECD, *Review of labour market and social policies: Russian Federation, 2011, op.cit*

The annual allocation to regions is made on the estimates of registered unemployment, the priorities set by the Ministry of Labour and Social Policy and the overall labour market conditions of each region (with regions facing labour market unbalances receiving more funding).<sup>110</sup> *Des-*

<sup>110</sup>The Russian Federation classifies regions with “labour market tension” those regions whose labour market index (which computes the registered and official unemployment rate) is 1.5 times the national average. At the end of 2012, only the North-Caucasus region complied with this rule, with an index of 11.3 compared to the national average of 0.9.

*pite the doubling of resources in 2009 to mitigate the effect of the economic crisis (from less than 0.1 per cent to 0.3 per cent of GDP), spending is well below the average recorded in OECD countries (1.69 per cent of GDP in 2010, of which 0.66 per cent invested in active programmes).*

In 2011, expenditures for employment services and programmes totalled 0.12 per cent of GDP and benefitted 12.9 million individuals (Table 4.5). The figures show the gradual reduction of programmes that were scaled up during the crisis (namely public works and employment subsidies), but also a decrease in vocational training, self-employment and internship programmes for school leavers. This trend – due to the decrease of individuals seeking employment assistance – continued also in the first half of 2012, when the number of registered unemployed was 17 per cent lower than at the end of 2011.

**Table 4.5. ALMPs beneficiaries and expenditures in the Russian Federation, 2010-2011**

Type of service and programme <sup>111</sup>	2010		2011	
	% of total expenditures	% of total participants	% of total expenditures	% of total participants
Labour market information (employers and jobseekers)	4.1	51.6	4.4	52.8
Vocational guidance	2.5	28.7	2.4	28.9
Job fairs, job search training	1.9	0.2	2.5	0.2
Temporary employment (14-18 years old)	12.4	6.9	12.2	6.6
Temporary employment (vulnerable jobseekers)	3.9	0.6	4.2	0.7
Vocational training	52.7	3.4	54.5	3.0
Internship (18-20 years old)	1.4	0.2	0.9	0.1
Public works	15.7	4.4	14.6	3.7
Self employment	3.7	2.0	3.0	1.7
Social adaptation (job clubs and fresh start)	1.7	2.0	1.4	2.3

Source: ROSTRUD, *Annual report of activities in the field of labour and employment, Moscow 2010-2011*

The paragraphs that follow outline the main features of the current job search services and employment promotion programmes.

<sup>111</sup>The total number of recipients of public services is six times the number of registered unemployed at the end of the period because i) the same individual may have access to more than one of the services available, and ii) access to basic services does not require the registration as unemployed.

**Employment services**, including labour market information, vocational guidance, job search training and matching of jobseekers and vacancies – although representing only 9.2 per cent of the total budget for ALMPs (see Table 4.5 above) – comprises over 80 per cent of all participants to employment promotion measures. *The human resources allocated to the PES, however, appear inadequate to meet basic service requirements. The current ratio of staff-to-registered unemployed is 1:230 and it increases further when only the staff actually assigned to deliver the services to clients (approximately 80 per cent of total staff) is considered.*<sup>112</sup> This ratio compare unfavourably with the average international benchmark of 1:100 that is used as reference to assess quality of employment service delivery. On the basis of this ratio, the current number of PES staff should be doubled.

**Vocational training and re-training**, increased, since the late 1990s, both in terms of beneficiaries and resources invested, with targeting shifting from long-term and low skilled unemployed to younger jobseekers and women. Despite the high share of the budget allocated (over 50 per cent of total spending in 2011), only 3.4 per cent of all participants are referred to training programmes. *Administrative data suggest that placement rates of the training programmes for young school leavers have increased over time (to reach 80 per cent), also thanks to the fact that in some regions trainees are guaranteed a job before joining the programme. In regions where a job guarantee is not a prerequisite for attending a training programme, placement rates are in the range of 40 per cent.* The evidence available on the impact of training programmes in the Russian Federation is rather limited and the results are rather mixed. One study – measuring the impact of re-training programmes in the Central and Ural Federal Districts – found no significant effect of re-training programmes in terms of employment probabilities, wage levels and duration of unemployment spell. In terms of groups targeted, training programmes improved the current employment status and wage prospects of older participants (45 years old), but it worsen the likelihood of being employed and receiving a higher salary for youth below 30 years of age.<sup>113</sup> Another research carried out on training and retraining programmes in the city of Rostov-on-Don (Southern Russia), found a positive effect on employment probabilities and the level of wages, especially so for adult men and for blue collar workers. The effect, however, tended to disappear after one

<sup>112</sup>OECD, Economic Surveys: Russian Federation 2013, OECD, Paris, 2014.

<sup>113</sup>Benus, J. et al. “Re-training Programs in Russia and Romania: Impact Evaluation Study”, CEFIR Policy Papers, 2005

year.<sup>114</sup> These results are in line with the evaluation findings of similar programmes in several countries around the world, i.e. that general vocational training programmes yield lower employment returns among young people compared to measures that combine training with job placement and/or a work experience (Box 4.11).

**Box 4.11. Youth employment programmes: Lessons from evaluation**

Several evaluation studies of youth employment programmes have shown that some programmes are successful while others fail to improve young participants’ chances of gaining a job. Some of the advantages and disadvantages of these programmes are summarized below.

Type of programme	Advantages	Disadvantages
Labour market training	Works better with broader vocational and employability skills that are in demand and when it includes work experience and employment services	May produce temporary, rather than sustainable solutions and, if not well targeted, may benefit those who are already “better off”; training alone may not be sufficient to increase youth employment prospects
Employment services (job search, career guidance and labour market information)	Can help youth make realistic choices and match their aspirations with employment and training opportunities; improve information on job prospects and on the efficiency, effectiveness and relevance of initiatives	May create unrealistic expectations if not linked to labour market needs, and they often only cover urban areas and the formal economy
Employment intensive public works and community services	Help young people gain labour market attachment and, at the same time, improve physical and social infrastructure and the environment, especially when combined with development and sectoral strategies, and can enhance employability if combined with training	Low capacity for labour market integration; young workers may become trapped in a carousel of public works programmes; often gender biased; displacement of private sector companies
Employment subsidies	Can create employment if targeted at specific needs (e.g. to compensate for initial lower productivity and training) and at groups of disadvantaged young people	High deadweight losses and substitution effects (if not targeted); employment may last only as long as the subsidy
Entrepreneurship promotion	Can have high employment potential and may meet young people’s aspirations (e.g. for flexibility, independence); more effective when combined with financial and other services, including mentoring	May create displacement effects and have a high failure rate, which limits its capacity to create sustainable employment; is often difficult for disadvantaged youth due to their lack of networks, experience, know-how and collateral

Source: ILO, Policy options to support young workers during recovery, ILO Policy brief, Geneva, 2011

<sup>114</sup>Nivorozhkin A., Evaluation of active labor market policies in Russia, 2003

**Internship schemes:** this is the only programme that specifically targets youth (beside the temporary work scheme for teen-agers). The programme targets school leavers (18-20) entering the labour market for the first time. In 2011, beneficiaries represented 0.1 per cent of all ALMP beneficiaries, with an investment of 0.9 per cent of the budget. These schemes, when they are well targeted, involve the social partners in their design and implementation and have a balanced mix of theoretical training and work-related experience, may indeed yield high labour market returns among young participants (see Box 4.12).

#### Box 4.12. Traineeship in the European Union

Traineeship schemes, delivered as part of active labour market policies were introduced across most EU countries with the objective to ease the transition of young people to the world of work. These programmes are usually targeted at: (i) youth who lose their job to the impact of the economic crisis; (ii) early school leavers and low skilled or unqualified young people who have difficulties in entering the labour market; (iii) young people at risk of social exclusion (e.g. young people from migrant and/or ethnic minority backgrounds, those from socially and economically disadvantaged backgrounds, young people living in deprived and/or remote areas, young people with physical and/or learning disabilities, etc.); and (iv) young graduates, who have also been hit particularly hard by the economic crisis.

Most forms of traineeships share a number of common characteristics, including: (i) the learning objective; (ii) the practical element of learning; and (iii) the temporary character of the placement. Traineeships have a number of key features. First, they can be part of an education or training programme, or involve work-based training organised by education and training institutions and/or public employment services. Second, the practical work-related training aims at completing theoretical education, enhance employability and/or allow participants to acquire a first work experience. Third, duration is variable, but much shorter than standard training programmes. Fourth, in most countries, the traineeship agreement is not an employment contract. The trainee is considered a pupil, student or a person who is working on a temporary basis to acquire on-the-job experience relevant to his/her studies and/or need to acquire a first work experience. In addition, trainees are not always remunerated, and – where they are – the level of remuneration varies widely. Finally, traineeship programmes often do not lead to a formal qualification and the involvement of the social partners is often scant, even though there is evidence that the most effective traineeship programmes are characterised by strong social partner involvement in design, implementation and quality assurance.

Employment outcomes of traineeship programmes that are part of ALMPs range from 13 per cent (Greece) to 90 per cent (Cyprus) with schemes aimed at university graduates securing the best employment outcomes (for example in Belgium, Ireland, Portugal, Romania and Spain). In part, these results are associated with

#### Box 4.12. Traineeship in the European Union (continued)

the employer incentives (employment subsidy) granted during and after the completion of the scheme if the trainee is retained. There are a number of factors which most often contribute to the success of traineeship schemes:

- A strong institutional and regulatory framework and the engagement of social partners.
- Close alignment to labour market needs, with a balanced mix of theoretical learning and practical, work-related experience;
- Flexible and individualized delivery to meet the needs of different groups of young people;
- High quality guidance, support and mentoring;
- Good matching of beneficiary with partner organization(s);
- Existence of traineeship agreement and certification procedures.

Source: European Commission, 2013. Apprenticeship and traineeship schemes in EU27: Key success factors. A guidebook for policy planners and practitioners.

***Employment subsidies (temporary employment):*** These measures provide temporary employment opportunities for teen-agers (14-18), vulnerable unemployed, but also workers at risk of losing their jobs. Spending figures show that, although declining compared to the late 1990s, the resources invested in job creation/preservation programmes (i.e. temporary employment) remain well above the average of OECD countries and accounted for over 17 per cent of the overall ALMP expenditures in 2011. Wage subsidies and other financial incentives (e.g. tax or social security exemptions for a limited period of time) for employers who recruit young people can help improve the school-to-work transition. Indeed, these financial incentives can offset the cost of the initial training that young workers require, or compensate for their limited work experience and initial lower productivity (see Box 4.13).

#### Box 4.13. Duration and targeting make wage subsidies work better for youth

There is a wide array of measures for sharing initial hiring costs between employers and government. The main features include: duration, amount of subsidy or employer's compensation, and type of contractual arrangement. In some countries, employers receive the equivalent of the national minimum wage per person hired or apprenticed. In others, subsidies are paid for the hiring of young people, on the grounds that these contracts can serve as stepping stones onto the labour market. For instance, in France and Italy, financial incentives

### Box 4.13. Duration and targeting make wage subsidies work better for youth (continued)

are granted to employers who recruit and provide on-the-job training to young jobseekers.

Wage subsidies can be particularly effective in improving the employment rates of young workers facing labour market disadvantages (e.g. low-educated and low-skilled youth, young disadvantaged women, young people exposed to discrimination in employment and occupation) provided they are specifically targeted. An efficient monitoring system is also essential to avoid abuses and achieve the policy objective of improving employability and employment outcomes of young workers, rather than turning them into cheap labour.

Overall, wage subsidies have had positive effects on improving the employment outcomes of youth. Existing evaluations show that generalized subsidies that target young people mainly on the basis of their age are unlikely to have a long-term impact on employment and earnings. If not targeted, these subsidies often result in labour market distortions in terms of deadweight and substitution effects, with employment lasting only as long as the subsidy. Evaluation results also stress the benefit of combining subsidies with on-the-job training and other measures in the form of comprehensive service packages offered to young workers.

Source: ILO and OECD, Giving youth a better start. A policy note for the G20 meeting of labour and employment Ministries, Paris, 2011.

**Public works:** the objective of public works is to help long-term unemployed maintain an attachment to the labour market and avoid poverty traps. After a sharp increase in 2009, the number of beneficiaries and level of spending decreased in 2010. In 2011, approximately 3.7 per cent of ALMP beneficiaries participated to public works with expenditures totalling 14.5 per cent of ALMP resources. The only impact evaluation available is a research limited to the Voronezh province and the city of Chelyabinsk (1996-2000), which measures the impact of public works, vocational information and guidance, job clubs and psychological support on decreasing the length of unemployment spells. This evaluation found a negative impact on the duration of unemployment among participants in Voronezh compared to the control group, while in Chelyabinsk most programmes had no overall effect on reducing the duration of unemployment.<sup>115</sup>

<sup>115</sup> Akhmedov A, Denisova I., Kartseva M., Active labor market policies in Russia: Regional interpretation determines effectiveness?, Centre for Economic and Financial Research, New Economic School, Moscow, 2003

***Self-employment programmes:*** The number of beneficiaries of this programme has been increasing steadily over the years. It now comprises 1.7 per cent of all ALMPs beneficiaries, with spending equal to 3 per cent of the total budget for ALMPs. Self-employment programmes in many instances can address the higher constraints that young people face in opening their own business compared to adults (e.g. less capital, in the form of skills, knowledge and experience; lower savings and access to credit; and scarce business networks). However, a wide range of services are required to ensure that youth business ventures are successful (see Box 4.14).

#### **Box 4.14. Promoting entrepreneurship among young people**

The review of successful youth entrepreneurship programmes reveals that the effectiveness of initiatives can be attributed to a number of key features.

- Clarity of objectives and commercial orientation: successful programmes have few and well-designed objectives and do not attempt to combine social and economic purposes. Programmes often fail due to the multiplicity of aims that result in the dispersion of resources. A commercial orientation allows providers to develop the technical competence that is critical for the provision of quality services.

- Range of services provided and adequate funding: programmes that have significant outcomes for young people combine advisory, training and grant/credit services, thus recognizing that young people embarking into self-employment have multiple needs. Successful programmes also rely on financial resources coming from various sources (private, public, governmental, non-governmental) to avoid the risk of resources drying up during implementation.

- Well-trained support staff: the technical and business competence of the support staff of an entrepreneurship development programme is of the essence to guarantee good results. The lack of impact in many countries can often be attributed to poor quality assistance and advice. A corollary of this is flexibility and adaptability of service delivery matched to the needs of young people.

- Reliance on locally-based delivery mechanisms: reliance on local delivery mechanisms (for instance local authorities, schools, universities, regional funding schemes) diversifies service provision and makes it more client- and market-oriented. In addition, leveraging on the knowledge and expertise of the local business community increases the probability of success and enable young participants to develop support networks.

- Initiative-base: thriving programmes do not impose enterprise choices on young people. Setting up young people as independent micro-enterprise owners in a line of business in which they have no prior experience or insufficient vocational skills may end up in failure.

- Customer-centred loans: although group lending is a common feature of many micro-credit schemes, an individualized approach to lending allows the programme to treat young people as clients and to avoid the delivery of pre-packaged services that may be ill-adapted to needs.

#### Box 4.14. Promoting entrepreneurship among young people (continued)

- Proper targeting and selection: young people are not a homogenous group and programmes should make an effort to identify differences amongst young women and men in skills, experience, status, aspirations and capacity to obtain resources – all of which influence their ability to establish and run a small business successfully.
- Mentoring: Successful programmes have strong and highly effective mentoring systems that are designed to provide young people with advice and guidance in the start-up period and beyond. This helps young entrepreneurs to overcome the constraints of limited business experience, contacts and skills.

Source: ILO, Youth Employment Programme note, Mimeo

*The current design, targeting and funding mechanisms of ALMPs do not appear to cater to the needs of the most vulnerable categories of unemployed. Funding allocations based simply on forecasted regional unemployment levels fail to take into account the specific risk factors faced by unemployed individuals at local level. Local employment offices are, therefore, unable to adjust the relative intensity of employment services based on the specific barriers various categories of unemployed face in the local labour markets. The types of programmes currently available, as well as their coverage, appear to be ill-suited to the current situation in the labour market. It is quite surprising, in fact, that given a youth unemployment that is three times that of adults, youth-specific programmes command only 13 per cent of the total ALMP allocation.*

The approach followed by ROSTRUD in providing services to employers seems to be rather passive, i.e. meeting the request of employers who post vacancies. The fact that over one third of the vacancies collected by the employment services are for jobs paying below the minimum subsistence income points to a lack of proactive approach in canvassing more attractive vacancies.

The provision of employment services and programmes is complicated by the multiplicity of labour and employment institutions and the lack of uniformity of administrative structure at local level. This often results in widespread differences in the quality of services provided to

clients and in the administration of employment programmes.

Overall, both targeting and performance monitoring of ALMPs are weak and rigorous impact evaluation analyses are rarely conducted. The importance of measuring the absolute and relative impact that the measures implemented by the employment service have on different categories of unemployed (men vs. women, adult vs. youth) cannot be overlooked. Evaluation is also important to measure the cost-effectiveness, relevance and impact of the interventions, as well as draw lessons for the design of new programmes and services to be fed into the decision making process.



# 5

## CONCLUSIONS AND POLICY IMPLICATIONS

### 5.1 Conclusions

In the decade leading up to the economic crisis of 2008, the Russian Federation witnessed strong economic growth, increasing productivity and real wages, and declining unemployment and poverty rates.

Since 1998 absolute poverty has fallen significantly while relative poverty has decreased only marginally, leaving behind a relatively large share of working poor (over 13 per cent in 2011) and low-paid workers (nearly 29 per cent of total employment in the same year).

***Strong economic growth in the period 2001-2008 led to significant improvements in the Russian labour market.*** The labour force participation and employment rate of the working age population increased, while unemployment decreased. Such positive employment developments also spilled over to the youth (15-24) labour market. Young people experience raising labour force participation (from 40.8 per cent to 43.1 per cent) and employment rates (from 33.7 to 37 per cent) and declining unemployment rates (from 18 to 14.1 per cent). In relative terms, however, youth labour market gains in the period were much lower than those recorded among adult workers (25-64 years old), with the youth-to-adult unemployment rate ratio actually worsening (from 2.3 in 2001 to 2.7 in 2008) and youth employment growing twice as slow compared to the employment growth recorded among adults (3.5 and 6.3 percentage points, respectively). Even more importantly, working conditions among young workers did not improve, with young Russian workers more exposed to low-paid work, atypical forms of employment, underemployment and persistent high levels of informal employment.

The 2008 crisis affected the Russian economy mainly through the trade channel and declining oil and commodity prices. In 2009, output growth declined by nearly 8 per cent of GDP, driven by contracting domestic demand. The large stimulus package deployed by the Russian Government (amounting to 6.7 per cent of GDP) managed to mitigate the negative impact of the economic crisis on the labour market. Employment losses and unemployment surges were relatively contained –at least for adult workers–, as the labour market adjusted mostly through cuts in working hours by 5.5 per cent and real wages by 4 per cent).

The distribution of young workers in economic sectors and occupations most affected by the downturn and the segmentation of the Russian labour market explain the larger job losses experience by youth compared to adults during the crisis. Between 2008 and 2009 youth employment levels decreased by 10 per cent (compared to 1.2 per cent for adults), while the unemployment rate increased by 4.5 percentage points (1.8 percentage points for adults). This was caused by the drops in employment in the manufacturing, construction and other service sectors that have large shares of young employment. The sectoral and occupational distribution of youth employment also explain the higher employment losses of young men compared to young women and of urban workers compared to rural ones. The wider incidence of flexible contractual arrangements (service and fixed term contracts) and of informal employment among young workers also played a role in their higher exposure to a labour demand decline. Data on informal employment, labour turnover and shift among labour market statuses points to a duality between formal (first-tier) and informal employment (second-tier) and a higher exposure of young people to the negative effects of labour market segmentation (wage gaps, lower access to training and social security, poor working conditions and tenure and limited opportunities to transition to better jobs).

Young people are more exposed than adults to working poverty, low-paid work and informal employment. Although data disaggregated by age-group are not available, the concentration of youth employment in economic sectors that are more affected by working poverty and low-paid work (agriculture, trade, manufacturing and construction) makes a suspect that many young workers fall under these two categories. In 2012, the share of young people (15-24) employed in informal enterprises was 24.4 per cent (17.1 per cent among workers aged 15-64). Adding to the informality count include young individuals working under informal arrangement in formal

enterprises and those receiving part of the salary as envelope wages would increase the youth informality rate to approximately 50 per cent of total youth employment.

Education and training pays a premium in the labour market and has a positive impact on the school to work transition, but does not protect against and over-qualification. Educational achievement is positively related to labour market outcomes, as young people with lower educational attainment are more likely to be unemployed compared to youth with vocational and higher education. Young university graduates, however, have roughly the same probability of being unemployed as young people with initial and secondary vocational education. In part, this situation reflects a misalignment of higher educational outcomes with the requirements of an economic system still characterized by a relatively large share of non-competitive firms able to survive in the market thanks to low wages, poor working conditions and outdated production assets. Having a tertiary educational attainment pays a wage premium (37 per cent compared to young workers with basic education only) and eases the transition to a stable and satisfactory job. Such returns, however, are undermined by high rates of over-qualification among young university-educated workers (38.8 per cent) and the prevalence of employment in economic sectors exposed to high job turnover, atypical forms of employment and lower wages.

The economic recovery – despite averaging lower growth rates compared to the pre-crisis period – increased employment and brought unemployment to its lowest level in two decades. The effect of recovery on youth employment, however, has been marginal **youth** employment decreased (from 34.2 in 2007 to 33.7 per cent in 2012) and the youth unemployment rate in 2012 was still slightly higher than in the pre-crisis period (14.8 per cent compared to 14.4 per cent in 2007). This may point to the fact that a part of youth unemployment has become structural.

Despite the progress made across a number of economic and social indicators– which place Russia within the range of OECD countries –there are still a number of challenges to be addressed.

The private sector is still underdeveloped, as evidenced by the low share of employment (27 per cent) and output (23 per cent) generated by small and medium size enterprises (SMEs); the still high proportion of employment in state-owned companies (28.8 per cent); the low rate of enterprise entry/exit in the market; the concentration of exports in

commodities; and the lower level of FDIs compared to other fast-growing countries. The main weaknesses that the Russian Federation will have to address in the near future include the inefficient institutional framework (especially the enforcement of property rights, the burden of government regulation, and the existence of an efficient judicial system); the quality of educational outcomes and their alignment to an innovation-driven economic model; the intensity of competition (barriers to trade and investment, exploitation of dominant position, excessive state intervention), access to finance, weak corporate governance and poor infrastructure development. Even more importantly, it will be necessary to address the issue of non-competitive enterprises, owing their market survival mainly to low wages, poor working conditions and the use of outdated production assets.

Russia is endowed with a largely educated workforce. By 2012, over 55 per cent of adults (25 to 64 years old) had attained a higher education degree. The level of workforce education is likely to remain high over the next years, as the participation in education at all levels remains high by international comparison. In the last few years, however, there are indications that the quality of education outcomes has been deteriorating compared to other fast-growing countries. Such deterioration is attributable to a number of factors. First, there are still wide regional disparities in education spending (expenditures per student is twice as low in poor regions as the national average), which affects educational outcomes. Second, the introduction of the Unified State Examination may have caused teachers to focus more on textbooks and curriculum requirements (e.g. encyclopaedic knowledge), rather than problem solving and other core employability skills. This is probably the cause of lower scores for Russian students in the PISA assessment over the years compared to the OECD average. Third, the vocational education and training system is plagued by excess supply of some streams (economists and lawyers) and shortages of others; insufficient funding for the modernization of education institutions; and narrow specializations that do not respond to labour market requirements. Finally, the country spends twice more per student at the tertiary level than at lower levels. Higher spending, however, does not result in skills that are relevant for the labour market. The specialized nature of Russia's tertiary institutions leaves graduates with skills that have limited transferability across industries, occupations and regions. The data suggests that nearly 39 per cent of young workers with higher education are over-qualified for the job they do and, at the same time, highly qualified workers continue to migrate abroad.

Neither the level of the minimum wage nor Employment Protection Legislation (EPL) in the Russian Federation appears to be a barrier to youth employment. The minimum wage amounts to less than 20 per cent the average wage and its level 20 per cent lower than the minimum subsistence level (which is the poverty threshold). The index of employment protection legislation in the Russian Federation is less restrictive than in the OECD countries, especially with regards to the rules governing temporary contracts (1.25 and 2.08, respectively). In addition, the role of EPL in protecting workers is undermined by limited enforcement, an ineffective sanction system and the existence of labour market segmentation. Payroll taxes and social security contributions probably play a more significant role in determining youth labour market outcomes. The recent increase in social security contribution rates (entirely paid by the employer), goes against the findings of research that shows that a reduction of the tax wedge for young and low-skilled workers could have a significant effect on their employment levels, as well as on the reduction of informality.

To mitigate the impact of the economic crisis, spending on labour market policies increased from 0.1 per cent of GDP in 2008 to 0.3 per cent in 2009. Measures included a rise in the maximum level of the unemployment benefit and additional funding for active labour market programmes. Coverage of the unemployment benefit system is relatively high (41.5 per cent of registered unemployed in 2011), but its maximum level— despite the recent hikes — is still below the minimum subsistence income. In 2011, expenditures on active labour market programmes totalled 0.12 per cent of GDP. The main active labour market measures currently encompass wage subsidies, public works and training provided to workers at risk of being dismissed and to long-term unemployed. Whereas these measures may have preserved some jobs and cushioned income shocks during the crisis, a re-orientation is now required towards cost-effective programmes that are targeted to the most disadvantaged groups among the unemployed, ease the transition from unemployment to work and shorten unemployment spells. Programmes targeting young unemployed currently command only 13 per cent of total expenditures on active labour market programmes, despite the fact that youth unemployment is three times that of adults.

The draft National Programme on Employment Promotion is addressing, to an extent, the labour market challenges highlighted above, namely widespread differences in regional labour market performance; skills shortages and skills mismatches; low mobility of workers; poor enforcement of labour law; and limited quality of labour and employment services. The

overall investment envisaged by the Programme equals 1.1 per cent of GDP (at 2011 prices). The Programme contains no specific objective on youth employment, relying on the expansion of overall employment as a means to improve youth labour market outcomes. The increase of overall employment since the end of the economic crisis, however, left young people behind, with decreasing employment-to-population ratio and unemployment rates still above the pre-crisis level.

In addition, the Programme focuses exclusively on supply-side interventions, with no measures deployed to address labour demand constraints and the youth employment content of growth. In the past, such type of strategy has proven to be largely ineffective in raising the quantity – and most importantly the quality – of jobs for youth. The National Programme, hence, fails to recognize the specific barriers that young people face in getting decent jobs, especially in regions lagging behind. Finally, increasing human capital (through training and re-training of registered unemployed), promoting health and safety in the workplace and increasing labour mobility are unlikely to double labour productivity by 2020 –as envisaged by the Long-Term Economic Policy – without substantial improvements in the structure of labour demand and the competitiveness of enterprises.

## 5.2. Policy implications

*The youth employment crisis in the Russian Federation calls for the development of a national action plan for youth employment that addresses both its cyclical and structural nature.* The economic crisis drew attention to the fragility of Russia's economic growth path, based mainly on the exploitation of natural resources rather than entrepreneurial activities. The preconditions for enhancing competitiveness, achieving sustainable growth and creating jobs for all categories of the population and especially for young people, are to stimulate demand and place employment at the centre of economic and social policies. The employment challenges facing the Russian Federation require integrated and coherent strategies that address employment as a priority objective of economic and social policy, and which include explicit targets and policy outcomes for youth employment. A national action plan on youth employment – linked to the National Programmes developed under the long-term economic policy of the

new administration – could provide the means to ensure coherence between the youth employment interventions contained in the various economic and social policies and identify clear and measurable outcomes to be achieved in a specific timeframe. Such integrated framework would promote action to: (i) increase the youth employment content of macroeconomic policies; (ii) support private sector development and especially small and medium size enterprises that have the potential to increase the demand of youth labour; (iii) enhance the relevance of education and training to labour market requirements, particularly through broader specializations and the inclusion of work-experience components; (iv) address labour market segmentation and improve workers' protection, and (v) improve the range and scope of employment services and active labour market programmes, so that they address the specific barriers that young people face in entering the labour market. Such action plan would play the important role of fostering inter-institutional coordination by bringing together the various actors with a stake on youth employment, including representatives of employers' and workers' organizations.

*The employment-content of economic and fiscal policies could be increased without undermining macroeconomic stability....*

Economic growth is a pre-requisite for employment growth, but it is not, in itself, sufficient. While the jobs gap stemming from the crisis has been largely closed in the Russian Federation, a decline in youth unemployment will require actual growth to exceed potential, with the composition of output growth and the management of macroeconomic and fiscal policies playing a central role.

The fiscal stance that the Russian Federation appears to be embarking upon is one of moderate, back-loaded fiscal tightening. A delay in fiscal adjustment may indeed support aggregate demand in the presence of a still weak world recovery. But for such a policy to succeed, it is necessary that credible structural reforms (on the investment climate, competition, trade liberalization, human capital and infrastructure development) become an integral part of the adjustment package. To maintain the fiscal deficit within the projected range, a re-distribution across revenue and expenditure items is needed, with a strong focus on improving the efficiency of the respective systems on the one hand, and balancing revenue and spending measures, on the other. The level of investment has a substantial effect on the capacity of the economy to generate jobs. In turn, investment is dependent on access to credit and its cost. When financial institutions are reluctant to lend, or

only lend at high interest rates, enterprises face serious barriers to doing business and recruiting young workers. The debate on measures to increase competitiveness has mostly focused on the diversification of the economy, with limited attention paid to the competitiveness of enterprises and, foremost capacity to innovate and absorb skilled human resources.

*...by expanding the tax base and reducing tax “regressivity”, especially for lower income groups....*

On the revenue side, an expansion of the tax base and a more progressive tax regime would improve equity as well as the operation of the tax system as an automatic stabilizer. The general financing strategy in the country has been to rely on indirect taxes and relatively high rates of social security contributions. A better ratio of direct to indirect taxation would reduce the regressivity of the tax system that places a higher burden on lower income groups. In addition, high taxes on salaries contribute, not only to higher unemployment and especially among youth, but also to lower participation in the labour market, while the size and quality of the labour supply are key determinants of the competitiveness of the economy. This is of particular relevance for the Russian Federation, in light of the projected decreases of the working age population.

*...as well as improving the efficiency of social spending*

On the expenditure side, the full phasing out of enterprise subsidies, which distort competition and carry heavy deadweight, combined with measures to improve the efficiency of social spending could open some space to increase investment for the modernization of infrastructure. The effectiveness of the social protection system could be improved by streamlining and simplifying the existing social protection programmes and enhancing targeting. This would improve the efficiency and quality of social assistance programmes, have a significant impact on poverty and reduce social spending outlays in the longer-run. The existence of a flat unemployment assistance benefit offers the opportunity to introduce an activation system for young jobseekers, whereby eligibility to unemployment assistance is conditional to active job search and participation to active labour market programmes.

*The acceleration of reforms to foster private sector development would boost the demand for labour as well as improve the quality of jobs....*

A further improvement of the business environment – including the strengthening of competition rules, the simplification of administrative procedures and the improvement of the judicial system – would boost potential returns in the private sector, shift the composition of investment towards sectors with high value added and ease the reallocation of resources from unproductive to productive enterprises. This would provide fertile ground for the creation of more and better jobs.

Strategies to increase the level of employment among young people are not likely to work unless enterprises invest in young people. It is by improving competitiveness and supporting investment in dynamic sectors that enterprises can maximize their capacity to create decent jobs. Policies that offer fiscal incentives, support the development of infrastructure, invest in research and development and provide enabling regulations to enterprises operating in competitive sectors with high youth employment elasticity can generate significant demand for labour in the medium to long run. Similarly, incentives to productive enterprises to provide training and work experience to young people can have a significant impact on easing the transition from school to work.

Maintaining the country's competitive edge requires that the quality and relevance of the education and training system be improved ....

In the transition to a market economy, the Russian workforce underwent an extensive reallocation across industries and occupations. Mismatches in the labour market became widespread, with shortages of some types of skilled workers coexisting with excess supplies of others. The reforms carried out to date have attempted to address both the quality and relevance of the education and training system. However, some of the measures implemented had unexpected consequences. For instance, the current education financing mechanism reinforced – rather than level out – regional differences, with regions and schools better endowed receiving more funds compared to those lagging behind. Similarly, the Unified State Exam, while attempting to improve the monitoring of educational outcomes, has created perverse incentives for teachers to focus on curriculum requirements, rather than on the capacity of students to apply the knowledge and skills gained. It is expected that the new Education Law, approved at the end of 2012, will address these concerns.

Better cooperation with enterprises, the revision of specializations on the basis of updated standards and the introduction of work experience as part of the curriculum would improve the alignment of education outcomes to enterprise requirements and reduce skills mismatches. On the labour demand size, measures are needed to increase innovation, business

sophistication and the technological readiness of enterprises in general, so that the talent of highly-skilled youth can be maximized.

*.... and that skills development opportunities be expanded to ease the transition of young people to decent jobs*

The reforms of the education and training system – an important part of the State policy to increase competitiveness – will, however, have a positive effect on labour market developments only in the medium to long-term. In the short term, the expansion of subsidized skill development programmes, apprenticeship and internship programmes would improve employment prospects for young workers with inadequate skill levels, address the erosion of competencies resulting from long unemployment spells and ease the transition to jobs of first labour market entrants. Lifelong learning opportunities extend only to a small share of Russian adults. This is in clear contrast with the widespread changes of the economy in the past decade. Promoting lifelong learning and training opportunities would foster enterprise competitiveness and enhance labour productivity, as well as improve job quality. As enterprises invest mostly in training workers with already higher skills, incentives to increase the human capital of low-skilled workers are warranted.

*A better balance between labour market flexibility and workers' protection would address the duality of the Russian labour market ....*

During the last decade, employment protection legislation (EPL) has shown an easing of strictness, owing to reforms in labour legislation. The incidence of temporary contracts has been increasing, with certain groups of workers, especially young people, more exposed than others. The labour market data confirm the duality of the Russian labour market, i.e. one for “insiders” with stable formal employment and security of tenure and another for “outsiders” who tend to be trapped in short-term and informal jobs with precarious attachment to the labour market. This second-tier market is the one that took the brunt of the economic crisis. Such differences in the levels of protection occur when EPL reforms are carried out at the “margins”, i.e. by increasing labour market flexibility mainly through the liberalization of temporary contracts, and enforcement policies are weak. Such a situation calls for measures to review the current legislation in order to strengthen protection of workers in atypical forms of employment, encourage enterprises to formalize, as well as interventions to strengthen the labour inspection system and a reinforcement of sanctions for non-compliance with labour law provisions.

*...while well-targeted and resourced active labour market measures would facilitate young people's entry and re-entry into the labour market*

The GDP share invested in active labour market policies – and especially active ones – is extremely low. As a consequence, active labour market programmes remain rather limited in range. During the economic crisis, public works and employment subsidies significantly expanded. During a labour market contraction, these programmes help support job preservation and cushion income shocks, in particular for less competitive groups of workers. But once labour demand recovers, more effort needs to be deployed in implementing cost-effective measures aimed at decreasing unemployment spells, activating discouraged workers and easing the transition from unemployment to work. Whereas it is important to have large scale active labour market programmes, it is equally important to shift the emphasis towards programmes that are well targeted, respond to labour market requirements and involve the social partners in their design, monitoring and evaluation. As young people are a heterogeneous group and face different types of labour market disadvantages, an early identification of individual risk factors and of the determinants of labour market disadvantage is of crucial importance to provide appropriate and effective employment assistance. The fact that placement rates of training programmes for young school leavers have increased over time also due to the job guarantee attached to them, confirms the findings of impact evaluations carried out in a number of countries: multi-component interventions that combine training with work-experience programmes and job-search assistance, as well as incentives for employers to hire young workers, have demonstrated to be more cost-effective than single measures.

*Modernising the delivery of employment services could help prevent long-term unemployment, bridge the regional divide and promote the inclusion of youth most at risk*

The provision of employment services should be reviewed with the objective of offering a set of standard services to all young people and more intensive assistance to disadvantaged youth. Early interventions based on profiling techniques and outreach programmes should be developed at the local level to make the services more relevant to young people. Partnerships between employment offices and local actors (municipal authorities, social services and community-based organizations) are required to improve service provision to those young people who are neither in employment, education

and training (NEETs), but are available to work, and to motivate them to actively search and take up jobs.

In the next few years the employment services will be called to implement strategies aimed at managing the displacement of workers in sectors affected by increasing import competition resulting from Russia's accession to the WTO. This calls for an expansion of training and re-training of workers to gain higher skills, the provision of employment counselling and job search assistance to workers at risk of displacement, employment subsidies and relocation assistance. As relocation assistance is also one of the services to be deployed to increase labour mobility across regions, its design features would need to take account of the findings of international research, which shows that regional differentials in the ratio of house prices to earnings are the single most important determinant of regional migration flows, together with regional labour demand growth and unemployment rates.

The employment service approach to employers and canvassing vacancies need to be re-examined. A key challenge is to overcome the stereotype that the employment service deals only with low level jobs and to increase its penetration of the vacancy market. This will improve the functioning of the labour market and allow the employment service to capture better job vacancies for registered unemployed. In this regard, the use of information and communication technologies has emerged in many countries as key tool to improve service delivery to employers.

Monitoring and evaluation should be carried out regularly to assess the effectiveness and impact of active labour market programmes. A system to monitor both quantitative and qualitative indicators could help in assessing the performance of interventions targeted to young unemployed and in determining what works and for whom. The lessons learned from systematic impact evaluation would help to improve the cost-effectiveness of the measures taken and would provide policy-makers with information on how to optimize the use of the available funding.



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# ANNEX

## Annex 1 - Main social protection programmes in the Russian Federation

Programme	Eligibility	Benefit	Finance and administration
Pension (labour)	Women age 55+, Men age 60+, disabled and survivors	Monthly cash benefit	Contributory; three pillars (PAYG, funded, and voluntary); Administered by the Pension Fund
Pension (social)	Women age 60+, men age 65+, and people with disabilities ineligible for labour pension and with no other source of income	Monthly cash benefit	Non-contributory; general revenue; financing by the federal budget; administered by the Pension Fund
Unemployment benefit	Officially registered unemployed	Monthly cash benefit for 12 months; 75 per cent of the previous wage for the first three months of unemployment, 60 per cent for the next four months, and 45 per cent for the next five months; minimum and maximum thresholds	Non-contributory; general revenue financing; administered by the Employment Services
Unemployment assistance	Officially registered unemployed	Flat rate cash payment equal to the minimum unemployment benefit for 12 months, for unemployed who do not qualify for the unemployment benefit or have exhausted the 12-month earning-related benefit	Non-contributory; general revenue financing; administered by the Employment Services
Sick-leave compensation	Employed, temporarily unable to work	Monthly cash benefit for limited period	Contributory; funded by a tax paid to the Social Insurance Fund; administered by enterprises
Maternity leave	Employed mothers before delivery (70 days) and after (70 days; 110 days for more than one child)	Monthly cash payment	Contributory; financed by a tax paid to the Social Insurance Fund; administered by enterprises
Housing allowance	Income tested; based on share of family budget spent on Housing and Utility Services norms	Monthly housing subsidy	Non-contributory; funded and administered by local governments
Social assistance benefits	Income based	One-time or monthly benefit in cash or in kind	Non-contributory; funded and administered by local governments
Child allowance	Children from families with per capita income below regional subsistence minimum	Monthly cash benefit until the child reaches age 16 (age 18 if in school)	Non-contributory; funded and administered by local governments
Privileges and subsidies	Various categories of individuals and families; merit or needs based	Discounted or free goods and services (food, transportation, housing and utilities, recreation and rehabilitation, health services, preschool, training)	Non-contributory; funded by federal and regional budgets; administered by regional governments.
Social work and care services	Vulnerable children and youth and their families; adults and elderly	Counselling services, rehabilitation, day care, temporary shelters, psychosocial support	Non-contributory; funded by regional and local governments; administered by local governments
Residential care in institutions	Children deprived of parental care, poor children, children and adults with disabilities, and frail elderly	Long-term placement in residential care	Non-contributory; funded by regional and local governments; administered by local governments



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