

- *Enhancing labor market programs helps to mitigate the adverse social impacts of economic restructuring.*
- *Income support mechanisms need to be reinforced to avoid poverty increase and reward job-search efforts.*
- *Active labor market programs should be directed to job search and training assistance and alignment of workforce skills with the needs of employers.*

### **Why Reform the Social Protection System?**

**Belarus's labor market and its social protection system are dependent on an increasingly unsustainable growth model that has the state as the main employer.** About two-thirds of wage earners in Belarus work at state-owned enterprises (SOEs). Firm-level econometric evidence<sup>1</sup> suggests that Belarus SOEs have about 10 percent more employees than they need, and a deteriorating macroeconomic situation is raising the costs of preserving unproductive jobs. However, if all excess workers are laid off, the unemployment rate could shoot up by 4.2 percentage points. Deteriorating macroeconomic situation increases the costs of preserving unproductive jobs. In early 2015, some SOEs have resorted to administrative leaves and delayed wage payments neither of which helps to increase labor productivity—to achieve that will require large-scale economic restructuring.

**Current labor market support programs in Belarus do not meet the demands of a dynamic labor market.** Unemployment benefits are extremely low and reach few of the unemployed. In February 2015, the average monthly unemployment benefit paid out in Belarus was 10.4 percent of the official subsistence level, 7.1 percent of the minimum wage, and just 2.4 percent of the average wage. Current active labor market programs (ALMPs) encompass such standard instruments as job-search support, training, employment incentives, public works, and entrepreneurship programs, but the main focus is on public works. Belarus spends considerably less on these programs than either Organization for Economic Co-operation and Development (OECD) and post-socialist countries: in 2013, Belarus spent 0.036 percent of GDP on ALMPs, in comparison to 0.6 percent for OECD and 0.34 percent for post-socialist countries. Current ALMPs in Belarus are not geared to serving active job seekers and need to be re-oriented to respond to the needs of a dynamic labor market.

**Inadequate income support for the unemployed complicates economic restructuring.** The main labor challenge confronting Belarus is how to enhance its income support program to provide adequate protection for all unemployed who need it without distorting work incentives and within current fiscal constraints. This means that the system should be able to cater to rising levels of unemployment but that, unlike the current system of subsidies to enterprises, it should also save on costs and not add to the tax burden on workers. In the short run, higher costs can be met by optimizing budget expenditures, particularly state aid and interest rate subsidization.

### **Better Income Support for the Unemployed**

**The social protection system can be reformed gradually.** In the initial phase, given the heavy fiscal pressures likely to emerge during initial restructuring, two concurrent programs are proposed: (1) unemployment assistance that provides a flat but not means-tested benefit for a limited period for those who have been laid off, financed by the government budget (benefits might be earnings-related, as is currently the case in Belarus); and (2) social assistance that provides a flat but means-tested benefit, with no time limits, also financed by the government budget. The reason for reliance on budget financing is the already exceedingly high tax burden on labor, which limits the space for contribution-based unemployment insurance, at least in the short to medium run. For the long term, two other concurrent programs are proposed: (1) unemployment insurance, a contribution-based, limited-duration program designed to smooth consumption; and (2) social assistance, a means-tested program of unlimited duration with a goal of reducing poverty (this is a general program but would also cover the unemployed who have exhausted unemployment insurance benefits and those unemployed who are not eligible for unemployment insurance). Both

<sup>1</sup> World Bank (2012), Belarus Country Economic Memorandum, Report No. 66614.

types of income support is found in the vast majority of OECD and post-socialist countries, where it has proved that it can provide adequate support in a fiscally sustainable manner.

**Solid and effective income support requires that the benefits have both a long-enough duration to facilitate job transition and reasonable, yet affordable, benefit levels.** In the current unemployment insurance program, the replacement rates range formally from 50 to 70 percent, falling over time. At the same time, the legislation permits the application of caps based on 'base value', which results in a very low benefit. In principle, the formal replacement rates are appropriate but may not be affordable. In the short run, unemployment benefits can be increased to at least the minimum subsistence level, with a prospect of gradual increases to at least the minimum wage level. The unemployment assistance program should have the same benefit levels as social assistance. The duration of both unemployment assistance and unemployment insurance could range from 6 to 12 months, perhaps becoming longer for those close to retirement age. The duration of social assistance benefits should be unlimited. To promote access to benefits, eligibility conditions could be relatively relaxed. To prevent misuse of the system, participants could be filtered via self-selection, just as participants currently respond to conditionality related to referrals to public works and training.

**There are a number of ways to counter the reduction of work incentives.** To avoid the undesirable consequences of paying unemployment benefits, the government should: (1) Design program parameters carefully, such as setting replacement rates consistent with work incentives and avoiding unemployment or poverty traps due to the loss of the unemployment or social assistance benefit, such as by reducing personal income tax rates for certain groups. (2) Condition receipt of unemployment benefits on job-search, temporary work assignment, and training requirements, building on the principle of mutual obligation. (3) Monitor and apply sanctions for beneficiaries who fail to follow rules (a practice that has elsewhere proven effective in motivating benefit recipients to look for a job). One important lesson from the experience of post-socialist countries is to make sure that benefit levels upon transfer from one program to another act as incentives for job search. For instance, the social assistance package should not exceed unemployment benefits or unemployment insurance payouts.

### **Active Programs Can Promote Labor Market Adjustment**

**The experience of OECD and post-socialist countries can provide valuable guidance.** While training programs are only modestly effective in the short run, they have the potential for major impact in the long run. Wage subsidies typically show positive effects, but they work best with specific target groups in well-defined contexts (one sector, one region) and may not always be good candidates for large-scale public policies. However, job search assistance has been found to be effective, and usually also cost-effective. Youth groups have been particularly difficult to assist effectively, but they do benefit from programs that help them combine job-search assistance, counseling, and training and placement services. However, early intervention in training is better than late; skills formed early have a longer payoff period. It is important to build integrated structures for skills formation, especially by forming an institutional relationship between vocational training programs and the formal education system.

**ALMPs for Belarus should be of several types.** The emphasis should be on job search assistance—both for short-term impact and to avoid information failures in a changing market environment; and on training programs—for long-term effects and for reskilling the labor force. These can be complemented by targeted wage subsidy schemes, perhaps in hybrid versions such as temporary working arrangements, in essence keeping people in jobs by reducing working hours and subsidizing earnings or replacing foregone earnings. The public employment service should be closely involved in the planning and conduct of restructuring programs at the firm level so that it can offer tailored job search assistance and services to those likely to be unemployed. Enterprises, particularly private firms, can be invited to consult on desirable skills profiles. For some jobseekers, paid public works may be an option to provide a safety net or to preserve human capital. Clearly, the specifics of each program, its administration, and how it interacts with the unemployment insurance system need to be thought through carefully. Evaluation from the very beginning will help to promptly assess the effects of each new policy.

*This Note is prepared on the basis of the World Bank Report "Getting Ready for a Dynamic Jobs Market: Enhancing Labor Market Policies to Support Structural Reforms in Belarus", March 13, 2014, Report No. 86017-BY.*

Contact info: Sebastian Eckardt

Johannes Koettl

Kiryl Haiduk

Maryna Sidarenka

SEckardt@worldbank.org

JKoettl@worldbank.org

KHaiduk@worldbank.org

MSidarenka@worldbank.org

(+375 17) 359-19-50 • [www.worldbank.org/belarus](http://www.worldbank.org/belarus)