

# **The Effect on International Competitiveness of Differing Labour Standards in the Fertiliser Industry of the NIS and the EU**

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## **Abstract**

The project which generated this paper arose from continuing concern in the European Union about the persistence of high unemployment and the likely effects of economic reforms in the New Independent States. The study brought together researchers from four countries: Finland and the United Kingdom in the EU and Belarus and Russia in the NIS. The purpose was to examine the impact that differing labour standards in the two NIS countries and the two EU countries have and are likely to have on the ability of companies in each country to compete internationally. The core research activity comprised a small number of in-depth case studies of firms in the fertiliser sector, enabling comparisons to be made between the industries in each of the four countries.

The lack of structure of labour markets in the NIS and their comparatively low labour costs posed a potential threat to the competitive position of the EU and this study set out to understand the relevant issues more fully from a number of different perspectives. These included comparing labour costs and productivity, social costs such as health and safety, pensions and other benefits and exploring the impact of investment on productivity. Ultimately the study focused on how a levelling up of labour standards in the NIS would impact on the EU Member States.

This paper sets out the findings of the case studies within the fertiliser industries of the respective countries. These specific findings are presented within the general context of a comparison of labour market conditions.

The fertiliser industry has been through a period of change in all four countries. Factors which emerge strongly from the research are the differences in health and safety standards and costs and environmental standards and costs between the NIS producers and the EU producers. Productivity also presents a very varied picture, with the NIS producers being disadvantaged by out-dated technology.

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This research project was undertaken in four countries, Belarus, Finland, Russia and the United Kingdom, during 1995-97.

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## The Effect on International Competitiveness of Differing Labour Standards in the Fertiliser Industry of the NIS and the EU

### Introduction

#### Background

This paper presents partial findings of a study funded by the Tacis - ACE<sup>1</sup> programme on 'differing labour standards and their effects on international competitiveness'. The study arose from continuing concern in the European Union (EU) about the persistence of high unemployment and the likely effects of economic reforms in the former countries of the New Independent States (NIS). The basic premise was that in these transitional countries, the lack of structure in labour markets and the comparatively low costs of employment posed a threat to the competitive position of the EU. Concerns over product dumping and the diversion of investment from the EU to the NIS were at the forefront of the issues addressed by the research.

More specifically the research focused on the following key issues:

- comparisons of labour costs and productivity
- comparisons of social costs such as health and safety at work provisions, pensions, unemployment benefits, maternity/paternity rights, redundancy and dismissal provisions
- the impact of investment on productivity and the extent to which foreign investors are seeking to exploit the lower costs in the NIS
- an assessment of the quality control issues and the extent to which changes in quality in the NIS will impact upon industries in the EU
- a consideration of changes in, and the levelling up, of labour standards and the potential impact on international trade

The study brought together researchers from four countries: in the EU, Finland and the United Kingdom, and in the NIS, Belarus and the Russian Federation (hereafter simply referred to as Russia).

## **Objectives**

The overall objective of the study was to understand more fully the issues surrounding the effects of differing labour standards on international competitiveness. However within this broader objective there were a number of specific goals, summarised as follows:

- to develop a set of appropriate policy recommendations to inform EU policy and decision-making in the sphere of economic reform and the integration of the transitional economies
- to develop and improve the understanding of the international trade implications of the transition process in the countries of the NIS
- to generate and improve understanding of international comparisons of labour standards and their implications
- to develop intra-industry comparisons of total labour costs (direct and indirect) between the partner countries
- to establish the extent to which the textile industries in the NIS countries will be able to compete directly with similar industries in the EU and to test their ability to attract inward investment away from the EU

In order to meet these objectives, the study gathered a mixture of quantitative and qualitative information from the textile, steel and fertiliser industries. This paper focuses on the fertiliser sector. The fertiliser sector was chosen as representative of those industries likely to be significantly affected by more open international competition and because of its common interest to all four countries involved with the study.

## **Methodology**

The method of approach involved a number of distinct, though inter-related activities, the key ones of which are described below:

- inaugural workshop bringing all partners together to exchange basic information and agree the study parameters, basic approach and timetable (this was held in Moscow in December 1995);
- preparation of contextual information on the national labour markets, including basic indicators of economy and employment and basic legislative provisions in the area of labour standards;
- case studies of firms in the textile sector.

The employer case studies represent the core research activity. The approach was to isolate those sub-sectors (ISIC Classes) of most relevance to the study and its objectives and to each partner country (ISIC classes 1711, 1712). A schedule of target case studies, stratified by sub-sector and size, was agreed between the partners, and this formed the basis of the case study selection.

Each partner country began the case study work by selecting and completing a study of one pilot firm. For the pilots a draft *information request* and *discussion guide* were developed to ensure a consistency of approach in the interviews. However, it was necessary to modify the structure of the questions to fit with national conventions and this adaptation process was the responsibility of the researchers in each partner country. Firms in each country displayed varying levels of familiarity with responding to such enquiries and these characteristics have been taken into account. In the UK, for example, there is a tradition of qualitative interviews with employers, where discussions tend to be semi-structured and can range across a number of issues. By contrast, in Belarus there is a preference for inquiries that ask for precise information and so with less room in interviews for exploring the topics in a more qualitative way.

The UK research team drew up a common sampling frame for the case studies to be used by each research team, and a common discussion guide for the case study interviews. Each research team then identified and contacted appropriate companies in their country in conformity with the agreed sampling frame.

Although the sampling frame used was common in terms of ISIC codes, numbers of companies in each industry and in each employment size category, some variation was allowed to ensure that case studies conducted in each country were fully reflective of the industry in that particular country. For example, firms in the NIS countries are on the whole very large, whereas companies in Finland tend to be relatively small. It was deemed preferable to conduct a small number of in-depth case studies, rather than a large number of less detailed studies, as this would enable more meaningful conclusions to be drawn. Case studies were completed in all four countries by the end of 1996, and exchanged between the participating research teams. Subsequently a workshop involving all participating researchers was held in Minsk in May 1997, with the final report being written by the UK research team.

This project has involved researchers from four countries, with differing backgrounds, cultures and methodological traditions. For example, whereas in the UK and Finland, the practice of semi-structured qualitative interviewing is well established, in the NIS countries this is not the tradition. Hence, although each research team used a common format, there were initially some difficulties in ensuring a comparable product. There have also been communications difficulties, in particular with Belarus, due to a shortage of telephone lines, uncertain postal communications, and a lack of email facilities.

It proved difficult to obtain quantitative data which is fully comparable across all four countries. In part this is due to the vagaries of national systems, but also due to factors such as the fixed exchange rate of Belarus. For example, figures on

productivity and wages in Belarus, which while available, are highly misleading due to the official exchange rate in which they are quoted. Such problems render meaningful comparisons extremely difficult and so quantitative comparisons across all four countries have not been attempted, but instead the analysis has concentrated on qualitative comparisons with country specific figures quoted where appropriate and meaningful.

Even within the EU, comparisons between the UK and Finland are not as straightforward as may appear, and the added dimension of Belarus and Russia makes for a difficult situation. The use of labour market statistics in this context is problematic, especially given the acknowledged unreliability of information from the transitional states. Nevertheless, the available statistics have been used where possible alongside more qualitative information.

## **Labour Market Context**

### Key Issues

This section sets out the broad labour market contexts within which the four study countries operate, drawing comparisons as appropriate, with the primary aim of aiding understanding of the subsequent fertiliser industry section. In doing so the discussion focuses on the following key areas:

- demographic indicators
- employment
- unemployment
- social partners
- wage determination
- labour legislation
- economic performance

### Demographic Trends

Basic demographic indicators are presented in Figure 3.1. They show the relative size of the four countries in term of population, with Russia and to a lesser extent the UK contrasting sharply with the much smaller populations of Belarus and Finland. The size of the working population will be influenced by the age structure of the overall population and here all four countries are facing ageing populations which will impact both on the available population for the labour market and the number of dependants outside the labour market.

Activity rates for both men and women have traditionally been higher in the transitional states than in the EU countries, and this is still the case, despite the disproportionate job losses among women, (which in Russia are expected to worsen as labour market legislation protecting female employment is removed or breached). In 1995 the activity rate for women in Russia fell to 56.3% from a figure of 61.6% only two years earlier. Over the same period the male activity rate has also fallen sharply. This contrasts with the experience in the EU countries, where increased numbers of women are entering the labour market, and with Belarus, where job losses have not been permitted.

**Table 3.1: Demographic Indicators**

<b>Indicator</b>	<b>Belarus (1995)</b>	<b>Finland (1995)</b>	<b>Russia (1995)</b>	<b>UK (1995)</b>
Population (million)	10.3	5.1	147.9	58.4
Working population (million)	5.9	3.4	74.0	38.1
Employment (million)	4.4	1.9	72.0	25.1
Activity rate (%)	74.6	69.9	63.1	72.8
Female activity rate (%)	-	67.2	56.3	64.6

*Source: National Statistics*

### Employment

In comparison with the two EU countries, Belarus and Russia have a much larger proportion of total employment in agriculture with 19.1% and 15.1% respectively. However, even between the two EU countries there is a marked difference, with the UK having a comparatively small proportion of employment in agriculture at 2.1% compared with 8.6% in Finland. Figures for employment in industry are, however, more consistent between the four countries ranging from 27.8% in the UK, which is only marginally higher than the smallest proportion - in Finland (26.3%). Comparisons of service sector employment across the four countries are not possible due to the deficiencies of the Belarusan figures, although between the three remaining countries the two EU Member States have much higher service sector employment than Russia, with the highest in the UK.

**Table 3.2: Employment by Broad Sector**  
(1995, Percentage of Total Employment)

<b>Sector</b>	<b>Belarus</b>	<b>Finland</b>	<b>Russia</b>	<b>UK</b>
Agriculture	19.1	8.6	15.1	2.1
Industry	27.6	26.3	27.1	27.8
Services	*29.3	65.1	57.8	70.1

\* in 'non-material sphere', excludes public sector (for example civil service, government, etc.)

*Source: National Statistics*

It is difficult to be precise about the reliability of the Russian employment figures since the estimated large informal sector (accounting for anything between 20-40% of overall economic activity) will distort the information shown. Employment in the informal sector is not concentrated in any particular industry but widely distributed in the economy. However, services may be a higher proportion of the informal than the formal economy. In Belarus estimates of the size of the informal economy are equally precarious, although 36-46% has been estimated on the basis of changing cash shares. Other more cautiously based estimates put it at between 5.5% and 13.5% of GDP. In the two EU Member States there is undoubtedly some informal economic activity, but it is generally reckoned to be comparatively small and does not represent the same potential threat to economic policy as is the case in the transitional states. In the UK, for example, the informal sector is thought to be relatively small and concentrated in certain occupational areas such as construction and personal services.

### Employment Status

It would be expected that these variations in the sectoral distribution of employment would be reflected in the types of employment status found in each country, but this is only partly confirmed by the information in Table 3.3. For example, in EU Member States with high levels of employment in agriculture there is an associated high proportion of self employment (representing the farm owners). This is not the case in either Belarus or Russia where, despite high levels of agricultural employment, self employment is comparatively small at 7.2% and 9.4% respectively. Finland, with a higher proportion of agricultural employment than the UK, has a correspondingly higher level of self employment. A similar argument applies to the number of family workers, and here the expected relationship with high agricultural employment obtains in Belarus, figures not being available for Russia.

**Table 3.3: Employment Status**  
(1995, Percentage of total employment)

<b>Employment Status</b>	<b>Belarus</b>	<b>Finland</b>	<b>Russia</b>	<b>UK</b>
Employees	80.4	84.2	90.6	86.5
Self employed	7.2	14.3	9.4	12.9
Family workers	12.0	1.5	NA	0.6
Temporary workers	NA	12.9	NA	6.3
Part-time workers	0.9	8.4	4.0*	3.8

\* Includes only those voluntarily working part-time.

Source: National Statistics

In the two EU Member States the number of those with fixed term contracts is significant, but the use of such contracts is well established. In Finland there are over twice as many temporary workers as there are in the UK. By contrast, part-time working is far higher in the UK than in Finland or Russia, with over one quarter of all those in employment working part-time (mostly because they want to). In the UK and

Finland the majority of part-time workers are women. The Russian figures on part-time working provide only a partial picture since they do not take into account the increasingly common factor of those working less than full-time because they have had their normal hours cut by the firm. Further, in the informal economy there may be much moonlighting by (officially) full-time workers who are in practice under-employed. Voluntary part-time working in Belarus is not common practice, hence the low figure of less than 1% working part-time.

### Unemployment

Of all the labour market statistics presented here, those on unemployment present the greatest challenge in comparisons between the four countries. Within the EU the problem is less severe in that the measure used in Table 3.4 for Finland and the UK is derived from *Labour Force Survey* sources which are carried out in each Member State along reasonably comparable lines. For these two countries the statistics for 1995 show that Finland has a comparatively high rate of unemployment, well over twice that of the UK.

**Table 3.4: Unemployment**  
(1995, Percentages)

<b>Country</b>	<b>Unemployment Rate</b>
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Belarus	2.4
Finland	18.4
Russia	7.9
UK	8.3

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*Source: National Statistics*

The unemployment rates of 2.4% for Belarus and 7.9% for Russia are wholly misleading. In the case of Belarus there is substantial hidden unemployment and underemployment with firms compelled to hold on to labour they do not really need, as evidenced in the high level of unpaid layoffs. Unemployment is not yet allowed to become visible. This is also still the case to some extent in Russia with, for example, the statutory costs of redundancy a definite disincentive for firms to release labour they do not need. There is also a high level of hidden unemployment estimated at over 9% of all employment and over 28% of employment in light industry. Underemployment is also prevalent with an estimated 8.8% working below their capabilities across all industries. 'Forced vacations' without pay (in effect unpaid temporary layoffs) have increased and are a common feature of larger firms.

## Social Partners

Between Finland and the UK there are substantial differences in the social partner framework and their involvement in such activities as collective bargaining, tripartite consultations, and the like. However, these differences have to be seen in the context of free, independent trade unions and employer bodies with a long tradition in both countries. In Belarus and Russia the prevalence of similarly based organisations is less clear and in order to illustrate this the basic parameters of the social partners in all four countries are summarised:

- **Finland:** Trade union membership is high at almost 100%, mostly because the unions are involved with the payment of unemployment benefits. There are some 81 individual trade unions grouped into three main confederations. For employers there are seven employers' associations. These do not represent all firms, but firms which are not members must also follow the collective bargaining agreements reached.
- **United Kingdom:** Membership has been steadily declining since 1989. In 1995 there were around 7.2 million trade union members indicating a membership density of under one third.. There are in excess of 200 individual trade unions with a mix of general, industrial and craft based, although amalgamations have brought the overall figure down. The sole confederation is the Trades Union Congress (TUC) which has the majority of individual unions as members. There is a dominant employers' association, the Confederation of British Industry (CBI). It can claim only a small proportion of total firms as members but most of the largest are represented. Other federations exist and tend to be organised along sectoral lines.
- **Belarus:** There is one dominant government-backed trade union federation, the FPB or Federation of Trade Unions of the Republic of Belarus, which has over 31,000 organisations at branch, region and plant levels and claims over 4 million members, amounting to almost all those in employment. Union membership is seen as a normal requirement of employment, and although there are some additional small independent unions emerging, they are at present insignificant. For employers there are six employers' associations of a general nature.
- **Russia:** There are more than 100 separate trade unions with a combined membership of over 50 million, or around 75% of those in employment. Many of these unions were operational before the reform process started and have been slow to change their approach. The majority form the main confederation, the FNPR (Federation of Independent Trade Unions of Russia) but there are some additional smaller federations emerging which are particularly attractive to the new trade unions. Employers' associations have emerged since the reforms, with three growing national bodies and many regional associations.

The degree of involvement of the social partners in fundamental issues such as collective bargaining varies a great deal and is at its most intense in Finland where both sides are involved in forming sectoral agreements. In addition, if problems occur and the parties cannot make an agreement, the partners work with the government under a tripartite framework that sets a general agreement on incomes policy for the whole economy on an annual basis. This differs substantially from the UK where there currently is no tripartite framework that consults with the social partners. In addition, the main employer and trade union confederations do not get involved in collective bargaining, being seen more as pressure groups.

In Belarus the closeness of the trade unions to the state indicates that they will reflect government policy on wage increases and such matters, suggesting that the degree of 'bargaining' may be limited. This was also the case in Russia, although more recently the unions have themselves been reformed and are involved with collective bargaining and protecting the interests of their members. The law on collective agreements allows them to be conducted at federal and regional levels and for specific professions at a local level, although the most common types of agreement reached are those at federal and regional levels for all industries and federal ones for specific sectors and occupations.

#### Wage Determination

The collective bargaining arrangements outlined above suggest a highly formalised process in Finland and Belarus, with national economic policy providing a backdrop against which sectoral or enterprise level wages are set. In the Finnish case tripartite discussions are held only if employers' and employees' central organisations cannot agree on wage increases, otherwise agreements typically establish a general level of pay increases and possibly other terms and conditions of employment. The agreement currently in force, for example, provides for minimum increases each year to the end of the agreement period (January 1998) as well as provisions for low paid workers and the prevention of a widening income differentials. However, outside this broad agreement, individual firms have the right to negotiate and award other changes to remuneration but this is normally done through the consultative machinery in place.

In principle, in Belarus enterprises are free to determine the wages of their employees (subject to the provisions of the minimum wage). In practice virtually all follow the public sector pay scales; a grid of 28 wage groups, all based on percentage mark-ups over the first budgetary wage scale (which is slightly above the minimum wage). Thus there is a great deal of uniformity in wages between industries, although variations do exist. Clearly the national minimum wage is a fundamental part of the process and, it is seen as an instrument of economic policy and benchmark for the setting of social benefits such as pensions and child allowances. Over the past few years the real level of the minimum wage has steadily declined under the pressure of inflation.

This system differs from the current situation in the UK where government has only a minimal involvement in wage setting. There is currently no national minimum wage and basic rates are set only in the agricultural sector. Collective bargaining (normally between the employer and trade union) is still important in setting base rates of pay

and establishing minimum terms and conditions in the manufacturing, transport and financial services sectors and in the public sector (health, education, etc.). Yet the trend even in these sectors is towards fragmentation with local and individually negotiated remuneration packages, with performance related pay increasingly used as an incentive.

In Russia the Russian Tripartite Commission has an intermediary role in collective bargaining, although industry based agreements and (increasingly) plant-based agreements are establishing themselves as the norm. There is a minimum wage which is set by government and updated according to cost of living measures. The level of the minimum wage has been set well below what can be deemed a 'survival wage' and so few workers actually receive the minimum. Prior to 1995 the minimum wage was used as a benchmark to determine whether firms would pay an 'excess wage tax' which was set at a level six times the minimum wage, after which tax rates would increase progressively. However, firms manoeuvred around this by keeping low paid workers on the payroll so that other employees could be paid more than the threshold but without attracting the tax.

Many workers in Belarus and Russia currently suffer from late payment of wages, with 2-3 months being typical in Russia. This arises from cash flow problems caused by customer firms, and from a lack of funds to the firms through the taxation system (since most are still dependent on the public sector). This is not a situation likely to arise in the EU Member States where legislation protects workers' rights to receive their income, even in the event of bankruptcies.

### Labour Legislation

All four countries have a degree of legislation geared towards employment matters, although there are substantial differences in the intensity of the measures and their enforcement. It is not the purpose of this report to provide a comprehensive account of all such legislation, but more it is to provide a view on the effects of the overall package on international competitiveness. The judgement of employers on this matter is covered in the three subsequent case studies and here it is appropriate to make some broader statements on the possible effects.

When assessing the effects of labour legislation it may be too simplistic to concentrate on the provisions of the law in such matters. While all employers are expected to comply with the statutory provisions, it could also be argued that those provisions of a non-statutory nature, but which have, by virtue of custom and practice, become normal provisions should also be included. In many cases, employers who choose to ignore these established, but non-statutory, provisions will tend to lose out when it comes to the recruitment and retention of employees. The issue is particularly important for EU Member States where there tends to be a higher level of occupational mobility than in the transitional states. Also, tighter labour markets (as proxied by a low level of unemployment) will also experience greater movement of labour between jobs as employers bid up wages in order to achieve their labour needs. However, of the four countries studied, this scenario would tend to apply principally to the UK where unemployment is comparatively low, although in all countries

particular occupations and sectors will display their own supply and demand conditions.

Table 3.5 summarises the extent of statutory provisions in all four countries using the main headings emerging from this study. The information shows that all four countries have basic provisions covering such aspects of employment as pensions, unemployment insurance and holidays, etc., albeit set at different levels, thereby constituting different proportions of non-wage costs to employers. Also some of the statutory provisions may allow for rather partial coverage of the issue. For example, sick pay in the UK is governed by the terms of the Statutory Sick Pay Scheme but this only guarantees a minimum level of payment from the employer-contributed fund and for a maximum period of 28 weeks. However, it is common practice amongst the larger employers to have an additional privately funded sick pay scheme which allows employees to claim a much higher proportion of their earnings for a longer period of absence due to sickness.

It is problematic to go one stage further in this analysis by including actual levels of provision because of the different contexts within which they operate and the very real difficulties in finding comparable exchange rates, etc. However, it is evident that in Russia, for example, the statutory provisions are often inadequate and suffer from late payment.

**Table 3.5: Comparisons of Statutory Provisions**  
(Indicates whether statutory provisions exist (√) or not (X))

<b>Statutory Provision</b>	<b>Belarus</b>	<b>Finland</b>	<b>Russia</b>	<b>UK</b>
Social security	√	√	√	√
Pension (basic)	√	√	√	√
Pension (additional)	X	√	X	X
Unemployment insurance	X	√	√	√
Accident insurance	X	√	√	√
Sick pay	√	√	√	√
Maternity leave/pay	√	√	√	√
Paternity leave/pay	X	√	X	X
Accident pay	√	√	√	√
Holiday pay	√	√	√	√
Layoff pay	X	√	X	√
Redundancy notice/pay	X	√	√	√
Minimum wage	√	√	√	X
Working time	X	√	X	X
Equal opportunity	X	√	√	√
Employment of disabled	√	√	√	√
Health and safety at work	√	√	√	√

Source: National information.

Table 3.6 provides a similar analysis for those non-statutory provisions by employers which have become established practice amongst at least the larger employers. The EU Member States, for example, frequently provide a contributory pension scheme that is additional to the state pension covered by general taxation. Employer-based pensions are normally made up from contributions from employer and employee and in the UK represent one of the largest elements of non-wage costs for employers, often adding upwards of 10% to the wage bill. Insofar as they are voluntary they could, theoretically, be withdrawn by employers at any time. In reality, however, they have become an intrinsic part of the employee's remuneration package and in some cases have been enshrined in collective agreements which, of course, provides a legal limit on what the employer can do with such benefits.

**Table 3.6: Comparisons of Non-Statutory Provisions**  
(Indicates whether provisions exist (√) or not (X))

<b>Non-Statutory Provision</b>	<b>Belarus</b>	<b>Finland</b>	<b>Russia</b>	<b>UK</b>
Pensions	X	√	X	√
Workplace catering	√	√	√	√
Employee housing	√	X	√	X
Holiday accommodation	√	√	√	X
Medical/health service	√	√	√	√
Additional leave	X	√	X	√
Protective clothing	√	√	√	√

Source: National information

The UK is, by common consent, the least regulated labour market in the EU. It relies on a 'voluntarist' approach which basically means that the state will remain outside the employment relationship allowing employers and employees (or their representative bodies) to strike whatever contractual relationships that are appropriate for them, subject to a minimum of statutory provisions. This situation has endured despite the UK's membership of the EU. Some reliance is placed on 'codes of practice' in areas such as good industrial relations or disciplinary practices which employers are encouraged to follow<sup>3</sup>. In taking this approach the UK amongst the four countries studied here therefore represents the polar case in terms of labour market regulation. It also indicates that in the UK the non-wage costs are generally lower than those with more highly regulated labour markets (such as Finland), although the custom and practice of non-statutory elements should be brought into the debate. However, by their very nature these will vary in scale, thus making any meaningful comparisons impossible.

#### Economic Indicators

Comparisons of key economic indicators between the four countries is severely hampered by a lack of comparable data. It is accepted that the economic activity of the two EU Member States, as measured by GDP per capita for example, will far exceed those of Belarus and Russia. However, the extent of this difference cannot be judged from the official statistics available in the NIS, where reliance on the traditional methods of measurement is problematic.

For Belarus and Russia it is possible to identify those key features of economic life that they have had to grapple with since the reform process started, as listed below:

- falling output
- high levels of inflation
- low savings ratio
- falling government tax revenues
- high interest rates
- reducing value of the currency

In the case of Russia, there are signs of improvement in some of the economic indicators as policy achieves a degree of stability. Inflation, for example, peaked in 1992 at around 2,600% per annum and has since fallen back to a comparatively moderate 27% in 1996. However, the tight monetary policy behind such improvements has also had a negative effect on the economy, encouraging the non-payment of debts which causes problems for businesses and their workers alike.

Belarus displays many of the characteristics of economic change that Russia is experiencing (particularly high inflation, falling output and currency values) but here the changes are taking place against a somewhat different policy backdrop. In Belarus the pace of privatisation has been much slower. Official figures quoted by the IMF suggest that the overall share of employment in so-called public enterprises had fallen from 81% in 1985 to 68% in 1993. This suggests a much stronger direct involvement of government in the management of the economy. However, the fact that the country is still experiencing the same economic effects as others which have liberalised further, indicates that economic and labour market problems are not being overcome but simply stored up for the future.

#### Overview

All four countries are facing similar kinds of demographic pressure, such as an ageing population, but activity rates are falling rapidly in Russia, especially for women. This is against the general trend observed in the EU Member States where female activity rates are tending to increase. Much of this increase is in part-time working which is yet to establish itself in Belarus and is relatively small in Russia. The UK has one of the highest proportions of part-time workers in the EU with almost one in four workers, and one in two women in employment being part-time.

Other indicative statistics of a changing labour market would be the proportion of those in employment on fixed term contracts (temporary workers). Here there is only information available for the EU Member States which shows Finland with twice the proportion of temporary workers as the UK. Self employment has been growing in all four countries, although Belarus and Russia are some way behind the proportions in Finland or the UK. Unfortunately the statistics are much less reliable on unemployment and meaningful comparisons between the four countries cannot be

made. It is evident that there is considerable hidden unemployment in Belarus and Russia, with underemployment a significant problem bolstered by government policy towards the release of employees in enterprises.

The role of the social partners is still emerging in the NIS. Trade unions are developing their own separate identity and employers' associations are in their infancy. Comparisons with the EU Member States are also complicated by differences within the EU, and this is clearly illustrated by the two examples of Finland and the UK. The UK, with its falling trade union membership and influence and absence of any tripartite framework, represents the polar case within the EU. By contrast Finland follows more closely the European 'Social Model' of fairly formalised structures and procedures in such areas as collective agreements and incomes policy. The situation illustrates above all that there is no single approach to the regulation of the labour market within the EU and suggests that the transitional states would be advised to adopt policies and procedures that suit their local conditions best.

## **The Fertiliser Industry**

### **Background**

The case study firms in the fertiliser industry produce a variety of products across the spectrum from potash at the low/medium end of the technology scale, through to highly sophisticated and targeted products produced in high technology plants (for example NPK (Nitrogen, phosphorous, potassium) and ammonium nitrate). The industry experienced a period of change and uncertainty in the early to mid 1990s, with increased world supply leading to a collapse of prices. The increased export orientation of some NIS firms in the early phase of transition contributed to this. However, a variety of measures including anti-dumping action by the EU has now stabilised prices.

The Finnish and UK firms in the study primarily produce the more highly sophisticated products which require large scale capital investment in high technology plants enabling the production of a quality product which gives even spread and yield. The quality difference between, for example, UK produced ammonium nitrate, and that imported from Russia, accounts for some of the price differential between the producers. The NIS producers are primarily engaged in the low/ medium technology less sophisticated product range (for example potash), although whilst their equipment may be outdated by EU standards, it is not as deficient as in some other NIS industries.

### **Belarus**

The fertiliser industry is very important to the Belarusian economy, being a major exporter and hence a vital source of much needed hard currency. The case study firms produce potash, nitrogen and phosphorous fertilisers, with complex and concentrated fertilisers accounting for 14 percent of total production. The largest producer is the

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second largest potash producer in Europe, exporting 93 percent of its output. The exports of this company make a significant contribution to total Belarusian exports. Two other case study firms are very much less export oriented, with one exporting only 0.4 percent of its output, entirely to Germany, and the other exporting only negligible quantities. In 1995, 71.8 percent of Belarusian fertiliser production was exported, representing 9.6 percent of the country's total exports. Potash alone accounted for 7.2 percent of total exports. Fertilisers represent 1.6 percent (by volume) of external trade with the NIS countries, and 22.9 percent of trade with other countries. Potash exports bring in 40 percent of all of the hard currency revenues in Belarus, underlining the vital importance to the economy.

The main export destinations are given in Table 4.1. They show that exports are concentrated on a fairly small number of countries.

**Table 4.1: Destination Countries of Belarusian Fertiliser Exports 1995**

Product	Country	% of Total Exports (Vol.)
Potash	China	24.3
	Poland	14.6
	Brazil	11.7
	USA	6.8
	Russia	6.5
	India	5.2
	Lithuania	3.9
	Croatia	3.7
Nitrogen	Germany	100.0
Phosphorous	Ukraine	100.0

Source: National Statistics

Table 4.2 shows the percentage of Belarusian GDP generated by fertiliser production, the ratio of domestic to export prices, and the fraction of fertiliser production which is exported.

**Table 4.2: Belarus Fertiliser Production 1995**

	%GDP	Ave. Level Prices Domestic/ Exports (\$)	Exports as % Total Production
Fertilisers	5.7	-	77.8
Potash	3.2	55/76	93.2
Nitrogen	2.3	72/75	0.4
Phosphorous	0.2	113/111	0.1

Source: National Statistics

The case study firms all experienced significant falls in output in the mid-1990s, although the largest has subsequently recovered, whilst the output of the second largest has stabilised now. The third firm, however, remains in a very vulnerable situation, with little output recovery since 1994. All three are very large scale production units, with the largest employing 16,800 workers (producing 61 percent of Belarusian fertiliser output), the second 5,600 workers (producing 32 percent of total fertiliser output), and the third employing 2,200 workers (producing four percent of total fertiliser output).

At the beginning of the transition process, when the previously centralised export system of the USSR ceased, the Belarusian and Russian potash producers increased exports, contributing to a collapse of the world price. The EU initiated antidumping measures against potash exports from Belarus and Russia and measures were taken to stabilise the world price. The Belarusian formed an association with two of the main Russian producers, which proved beneficial in stabilising their situation and in facilitating exports. In the mid-90s, world production capacity was almost twice demand for the product. Another factor in this equation is the very sharp drop in demand for fertiliser from Eastern Europe and the NIS post-transition, due to the low purchasing ability of farmers, but demand has also been falling in Western Europe and North America. The production costs of the Belarusian firm are now on a par with those of the Canadian producers, and higher than those of the Israeli and Jordanian producers. Another post-transition problem has been access to port facilities in Ukraine and Latvia. More than 55 percent of NIS potash exports go through the port of Ventspils in Latvia.

#### Russia

The Russian fertiliser industry produces a wide variety of organic and non-organic products. It encompasses 40 very large plants, with a total production capacity of 18.9 million tons. Total production in 1994 was 8.3 million tons, of which 4 million tons was nitrophosphates, 2.5 million tons potash, and 1.7 million tons phosphate. Capacity utilisation has increased since 1994, but the industry is still producing at well under capacity. The industry employs 140,000 people, and has a gross profit margin of around 21 percent. The decline in output 1990-94 during the initial transition period was around 50 percent. This has now improved somewhat, due primarily to increasing exports. The case study firms each employ between 1243-7028 workers. Whereas in 1990 the industry was primarily oriented to the domestic market (75 percent), it is now much more export oriented, with approximately 75 percent of output being destined for the export market. For Russia, mineral fertilisers are major exports to non-NIS countries. Table 4.3 shows a general breakdown of costs in Russian fertiliser firms.

**Table 4.3: Industry Cost Structure**

Raw materials	45-56%
Energy	12-22%
Labour	11-12%

## The Effect on International Competitiveness of Differing Labour Standards in the Fertiliser Industry of the NIS and the EU

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Source: *Russian Fertiliser Manufacturers' Association*

A breakdown of labour costs from one of the case study firms is given in Figure 4.4. This shows the relatively high percentage of labour costs which are due to basic wages, bonuses and payments to the four Government Funds discussed elsewhere.

**Figure 4.4: Labour Costs in a Russian Fertiliser Company**

<b>Total labour cost</b>	<b>100%</b>
Wages	71.76
Time related wages	40.51
Working conditions supplements	4.39
Bonuses	16.57
Incentive payments	2.39
Social payments	3.39
Statutory	0.20
Voluntary	3.19
Government funds	28.24

Source: *Russian case study*

The case study companies produce a variety of products including ammonia, saltpetre, nitrophosphates and carbamide. Production of ammonia and saltpetre has been increasing sharply over the last 3 years. Firms are increasingly export oriented, with the main export destinations for ammonia being Switzerland, USA, Bulgaria, Turkey and Germany, Finland and Latvia. The products of the Russian industry are relatively unsophisticated, concentrating primarily on less complex fertilisers. The production technology in use, whilst in some cases being relatively modern in Russian industrial terms, is still sufficiently out of date to make the production of fertilisers of a high and consistent quality problematic.

### Finland

The Finnish fertiliser industry consists in practice of one firm, a member of a large group. In addition, a small number of smaller companies produce biodynamic fertilisers. The case study firm specialises in NPK production. Output is approximately 900,000 tons per annum, of which about half is exported. The main export destinations are: South East Asia and the Far East (with China being a major customer), Africa, Europe, Japan, USA and South America. Raw materials are obtained from Russia (ammonia and potassium) and from Finland (phosphorous).

The case study firm's advantages lie in its versatile product range, with over 50 different types of NPK being produced, and in the technologically sophisticated nature of its products. During the early 1990s, the firm faced very low cost competition from the FSU countries, a situation which eased from 1994 onwards. Sales to EU markets have also been adversely affected by the set-aside scheme of the CAP.

## United Kingdom

The fertiliser industry in the UK consists of a small number of large producers producing either very complex products in high technology plants, or simple products in medium technology plants. In addition to the large producers, there are a number of much smaller producers, who produce NPK or liquid fertilisers. The industry has been facing strong pressure during the 1990s, from low cost imports. Anti-dumping measures have stabilised the prices, but the firms still feel themselves to be under threat. Employment levels in the industry are down from the beginning of the 1980s. This is partly due to productivity improvements from increased capital investment, and partly due to reduction of past overmanning. In addition to import pressure, firms have also been affected during the 1990s by the set-aside scheme of the CAP, and by the BSE crisis in the UK, which has affected farmers' liquidity and future expectations.

The three case study firms are all large players in the industry, and represent two different sub-branches of the fertiliser industry. However, the problems identified are broadly similar. In all cases strong import pressure, moderated by anti-dumping measures, has resulted in price becoming crucial. All three of the case study firms are wholly owned subsidiaries of foreign owned groups.

Exports for two of the firms are minimal with small potential for growth, due to farmers' preferences for fertiliser type. For the other firm, whilst it exports 50 percent of its product, approximately the same amount is imported into the UK. This firm complained that one of its major foreign competitors in the EU is heavily state subsidised.

## **Labour Costs and Productivity Issues**

### Productivity

The official figures from Belarus on labour productivity showing sharp improvements in labour productivity are misleading, principally due to the distortions caused by the exchange rate measures referred to elsewhere. Nevertheless it is reasonable to conclude that labour productivity is significantly lower in the NIS companies than in the EU companies, and it is clear that this has not recently improved. Both of the NIS governments have measures in place designed to prevent labour shedding, as discussed elsewhere. As a result even in those firms where output has dropped sharply (in one Belarusian fertiliser firm, by 50 percent) appropriate labour reduction measures have not been instigated. The age of the equipment and technology contributes to low productivity, especially in Belarus. In the case of the largest Belarusian firm, productivity has actually halved during the 1990s. Russian firms are in a slightly less disadvantaged technological position. In contrast, there have been significant labour productivity improvements in the EU firms in recent years, due to attention to overmanning and to technological improvements and large scale capital investment.

## Wages

Wages in the NIS firms are low by EU standards. Belarus presents a varied picture, with firms paying differing wage rates dependent on the health of the firm. As a result, the firm which has seen output fall by 50 percent has the lowest wages, which are low even by Belarusian standards. For the EU firms, although labour costs are a fairly small component of total costs, they are nevertheless important due to the price sensitive nature of the industry's product.

## Social Costs of Labour

In the NIS social costs of labour follow a similar pattern to that discussed in other sectoral chapters. For example, in Russia statutory and voluntary labour payments make up a relatively high percentage of the total wage bill. However, one firm did report the Federal Government's failure to collect the statutory payments. The Finnish firm budgets 57 percent on top of the wage bill for labour costs. Statutory payments amount to 28 percent of the wage bill, and non-statutory costs 29 percent. These include such items as contributions to the sickness fund, seniority pay and company pension costs. The firm has however now discontinued the company pension scheme. In the UK, all three case study firms incur significant voluntary labour costs, including company pensions schemes, holiday pay, fully staffed medical centres on site in all three firms, and sickness benefits schemes. One of the firms felt that although these costs were normal for the UK, other countries may not have such good facilities and hence would incur lower costs. However, this firm felt that good facilities pay for themselves, increasing productivity, lower amounts of lost time etc.

## Employment Dynamics

The EU firms have all experienced redundancies during the 1990s, resulting from the elimination of overmanning and from the installation of improved technology (and in the case of the Finnish firm, a change to bulk shipments). One UK firm has seen employment fall from 2,000 in the early 1980s to 458 now, and another has halved its workforce during the same period. By contrast, the NIS firms have failed to shed their surplus labour, and in some cases have actually taken on more labour despite sharp falls in output. For example, all of the Russian case study firms report increased employment levels, in spite of in one case only 60 percent capacity utilisation. This firm reports that the ageing of its equipment necessitates more maintenance workers. Another Russian firm has increased its workforce by 5.1 percent during 1995-6 as a result of its increasing export orientation. One of the Belarusian firms also indicated that its increased workforce (in spite of 50 percent fall in output over the 1990s) is due to the need for increased maintenance of ageing equipment. Another of the other Belarusian firms estimates hidden unemployment in the firm to be 50 percent.

### Automation and Technology

In terms of equipment and technology, there is an important difference between the EU and NIS firms, with the latter having outdated equipment and technology compared to that of the EU firms. The advanced technology of the EU producers has enabled them to achieve increased productivity in recent years, although several firms indicated that the current uncertain prospects and the low rate of return on capital investment precluded further installation of even more up to date capital equipment. One of the UK producers is constrained by an environmentally sensitive site.

### Working Practices

None of the NIS firms have introduced multiskilling or flexibility with the exception of some Russian firms who have introduced multiskilling for repair workers. By contrast, two of the UK firms use multiskilling, with one in particular actively seeking to further develop this. However, one firm complained of having to pay “artificially inflated “ wages to newly multiskilled electricians to prevent their being poached by other local companies. In Finland, the case study firm operates the flexible working time pattern discussed elsewhere.

### Wage Determination

With regard to trade union representation and free collective bargaining, the NIS firms present a similar picture as discussed elsewhere, in that in every case there is a very high union membership rate, but little or no evidence of free collective bargaining. The exception to this is a firm in Belarus which produces potash. Here there is a free trade union in addition to the official one, and there was a strike in 1992. By contrast, free collective bargaining exists in all of the EU firms, with much lower levels of union membership in the UK and virtually 100 percent membership in Finland. In the UK, collective bargaining takes place locally at plant level. In Finland, there is the usual national bargaining, with additional local bargaining system. One UK firm reported that the bargaining round consists of one meeting between management and union representatives, while another UK firm has three major unions represented, as well as a number of smaller craft unions. The high union density in the Finnish firm was not in this case attributed to the Finnish unemployment benefit system, but to company tradition. This firm has four recognised unions, with the main one representing 65 percent of the workforce, although its attitudes were said to impede further development of subcontracting.

No performance related pay and other measures to improve productivity were observed in the Belarusan firms as yet. This is not yet a priority given the productivity problems discussed above. The Russian firms make fairly limited use of performance related pay schemes. The UK presents a varied picture, with all firms using some sort of PRP scheme, of varying complexity and impact on wages. The scheme in use in Finland appears to be the most complex and represents the highest percentage of pay (20 percent).

### Legislative Pressures

In both of the EU countries, case study firms face stringent health and safety and environmental standards. In no case do they regard these as problematic. Indeed, firms are anxious to meet and even to exceed the standards set. However, in this potentially hazardous industry, both these sets of standards do impose high costs on firms. High standards are not required of the NIS companies, and the lower standards which do exist are not rigorously enforced.

The activities of the Belarusian firms generates significant pollution of their local environment. A similar picture exists in Russia, where the low environmental standards are frequently not being met by the firms. For example, the largest Belarusian case study firm generates large deposits of waste from production that pollutes the local water supplies and salts up the streams, affecting thousands of hectares of formerly worked agricultural land. This situation is reported as getting worse, but little attention has yet been given to its amelioration, either by the firm or the local authority. Another Belarusian firm reports that “it has no problems with the environment, because for 80 percent of the time, the wind blows away from the town”. The third Belarusian firm is located in an area which still has a high level of radioactivity as a result of Chernobyl. With one exception, the Russian firms claim to be unable to afford even the fines for exceeding the basic standards set by the Government. One firm admitted that the local authority allows them to pay only a fraction of their pollution fines, as they are the major employer in the area. Jobs are regarded as the priority, not the environment.

By contrast, the environmental standards required of and met by the Finnish firm are very high. The firm is located in an area of outstanding natural beauty. One of the criteria for receipt of bonuses is the minimisation of pollution generated, and potential increased production is evaluated against the pollution which it may generate. The firm aims to exceed the standards set for it by Finnish legislation, aiming for 50 percent of its permitted pollution levels. However, the firm is concerned in case Finnish environmental standards become more stringent than the EU standards, and in particular about possible new nitrogen emission controls, and the expense of the proposal for compulsory biological denitrification. On the positive side, the use of bulk blended nutrients is forbidden under Finnish law, and this is advantageous to the firm, with its more complex products. The firm is involved in working with local farmers to ensure more efficient and environmentally aware use of fertilisers.

In the UK, all three firms incur significant costs as a result of EU / UK environmental legislation. None saw this as a problem, and two aimed to exceed legislative requirements. One firm, whilst fully endorsing environmental standards and aiming to exceed them, nevertheless felt that foreign producers selling into EU markets should be subject to the same standards. The third firm has the additional problem of being located in a protected area, and hence having additional problems in needing to meet local planning requirements.

The perspective on health and safety is not dissimilar. The EU firms all have very thorough health and safety standards and concomitant costs, whereas the NIS producers have much lower standards to meet, so low that they do not regard them as problematic. In the UK, all three of the firms place heavy emphasis on health and safety issues, and in all cases aim to exceed the statutory requirements. This is a potentially hazardous industry, hence firms incur very significant costs in protecting not only their workforce, but also their local communities. One firm mentioned that it has cost £10,000 for installation of an emergency roll-call system alone. All firms have fully equipped and staffed on-site medical centres, employing doctors and nurses, with quotas of staff also fully qualified in first aid.

### Future Expectations

Future expectations for the case study firms differ markedly by country. The UK firms are concerned for the future, fearing that removal of protection may cause further price collapse, and render them vulnerable to competition. The Finnish firm, on the other hand, is confident of its future, anticipating a more stable price level and further levelling off of competition from the FSU. The NIS producers present a much more varied set of views. On the whole the Russian firms are confident. The current situation and future prospects of the case study firms in Belarus varies. The largest firm has been facing strong competition in the developing export markets. In Belarus, 50 percent of the cost of fertilisers for farmers is paid for from the state budget, and this helps the financial position of the firms. However, many farmers are unable to afford even the remaining 50 percent of the cost of fertiliser. The government is experiencing difficulties in resourcing these subsidies to agriculture. It is therefore likely that the volume of production will fall. The second largest case study firm is planning to issue shares, and Russian investors are showing some interest. It is the intention that some of the shares will go to Russia in part payment of Belarusian debts for energy supplies. This is causing some dissatisfaction amongst workers, who fear deterioration of their working conditions.

In Russia, all three case study firms appear to be doing well compared to many Russian firms, and all are looking positively to the future. There is currently a problem in expanding the domestic market, in that not only do Russian customer firms have difficulty in meeting their bills, but also Russian farmers are currently unable to obtain loans at reasonable rates to buy fertilisers. However, this problem may be addressed in the future, leading to the potential for increased domestic sales. One firm is looking to find new markets to increase its capacity utilisation. Another firm is looking to further develop its exports, which have been facilitated by a joint venture with a Panamanian company, and it anticipates taking on more labour. To that end, they plan a major restructuring programme in 1997-8, designed to cut pollution by 15 percent and to increase capacity utilisation to 87 percent. They anticipate increasing ammonia production for the domestic market by 50 percent. Another firm intends to replace some of its equipment to increase energy saving, reduce pollution, and increase durability of equipment. They are also intending to restructure the workforce and to increase multiskilling.

In Finland, the firm is optimistic about the future. It is concerned about the likelihood of more stringent environmental standards, which will impose significant additional costs on them. The domestic use of plant nutrients is continuing to decrease, but they plan to develop their export markets, with particular emphasis on China, South East Asia (Thailand and Malaysia) and India. The demand for fertilisers would also be positively affected by further reductions in the set-aside acreage in the EU. They anticipate a more stable price level in the future, with the levelling off of imports from the FSU.

In the United Kingdom, all three firms view the prognosis for the future as being dependent on what happens to the price of their products under significant import pressure. They have all faced strong competition from imports. One firm felt that the future was uncertain, and that whilst EU anti-dumping measures currently in place help to stabilise the price, removal of these and subsequent price collapse would render the firm very vulnerable. The other two firms also made strong representations on these lines. One firm said that they were now at core level with their workforce, and could not really reduce any further. In all three cases, further investment is currently not envisaged, due to insufficient current profitability.

#### Overview

The fertiliser industry in these four countries, as evidenced by the case studies, presents a picture of an industry which has been through a period of change. A varied picture emerges from the NIS countries, where some firms have been doing comparatively well in the post-transition period, whilst others are in a vulnerable situation. The EU producers have faced a period of intense import pressure during the early 1990s leading to the collapse of prices and profitability. The introduction of anti-dumping measures has stabilised prices, but there remains strong pressure on the price of standardised products, hence keeping bottom line costs down is important.

Factors which emerge strongly from the case studies are the difference in health and safety standards and costs, and environmental standards and costs between the NIS producers and the EU producers. These considerations have, understandably, not yet made it onto the agenda of the NIS producers, although there is some evidence that at least one Russian firm is moving in this direction. Local authorities are currently more concerned for jobs than for the environment or health and safety. In contrast, all of the EU producers place very strong emphasis on meeting and indeed exceeding health and safety and environmental standards, and see this not so much as a cost imposed but as something which they would wish to do irrespective of national and EU requirements. There is some concern however that imports from countries with lower standards are permitted access to EU markets.

Productivity also presents a very varied picture across NIS and EU boundaries. The NIS producers are disadvantaged by out-dated technology. By contrast, the EU producers have advanced technology which has delivered productivity improvements over the last decade. Uncertainty for the future and low returns on capital have however precluded installation of state of the art technology in at least two of the EU case study firms.

The NIS case study firms are all carrying surplus labour, which they are precluded from shedding. The EU firms have all experienced significant downsizing during the last decade, which has contributed to their productivity improvements. The much higher productivity of the EU producers to some extent counteracts the much lower wage and social costs of labour, health and safety costs of the NIS producers. The quality differential on some products contributes to the ability to maintain competitiveness.

With regard to collective bargaining and trade union rights, all of the NIS producers have very high union density and comprehensive collective agreements in place. However, the extent of actual collective bargaining which takes place is limited. Either the government (in the case of Belarus) or management (in the case of Russia) determine wages and conditions. However, it is noteworthy that one of the Belarusian firms did experience a strike in 1992, and does have a free trade union which appears active. The EU firms present a somewhat varied picture, with Finland having almost 100 percent union density and strong unions with real influence. Although the UK firms have much lower union density, the trade unions are actively involved with local managements in free collective bargaining. It therefore would appear that in this industry the UK has a much stronger real union involvement than do the NIS firms despite much higher membership in the latter.

### **Policy Issues**

There is a range of influences that affect the competitive position of firms in the EU alongside NIS producers. Labour market structures can inhibit firms in doing what they wish to do to maximise productivity and this is the case in Finland as well as in Belarus and Russia, but less so in the UK where legislation is less comprehensive and the social dialogue less prescribed. However, the provision of an adequate legislative framework in such areas as health and safety at work may impose significant costs on firms, but could also have beneficial effects on productivity. The extent of non-wage costs in the four countries studied here vary from high in Finland to the lowest in the UK. The tradition of supporting employees is breaking down in the NIS and this will have the effect of reducing non-wage costs for firms, but at the same time wage costs are set to increase.

Convergence towards an EU approach to these matters is therefore observable in the NIS countries, but the process is extremely slow in Belarus and seriously inhibited in Russia. Issues likely to occupy firms in all four countries in the future include the cost of meeting environmental measures, where many firms in Finland in particular felt that they had much higher costs to contend with.

The study isolates a number of key issues that could provide a focus for attention by the EU in its dealing with industry within and outside the Union. These are as follows: Statistics, Social dialogue, Products and marketing, Import restrictions and Labour standards generally.

### Key Issues for International Competitiveness

The demographic and labour market backdrop strongly influences international competitiveness from a number of perspectives. Firstly the general availability of labour will be reflected in its cost (wage) to an employer so that in the generally tighter labour markets of the EU Member States, the cost of labour will be higher than in the countries of the NIS. This, of course, is a simplistic interpretation of a more complex issue. There is unlikely to be a *national* labour market for most occupational groups and there will tend to be strong *sectoral* tendencies. This is illustrated by the evidence in this report from the three sectors studied.

The availability of appropriate labour and its price will be a key determinant of the decision of industry to invest in capital equipment. However, speed of output may not be the dominant measure of productivity in the transitional states (as it tends to be in the EU producers), when labour can be used cheaply but not just because of low levels of wage, but also due to a lack of attention to such matters as health and safety which have the effect of increasing production costs, if adhered to.

However, it is clear from the case study firms that wages in Belarus and to a lesser extent Russia are artificially depressed at the moment. There are signs that in some sectors bonus systems have developed which aim to reward effort, but they tend to be poorly targeted and in some cases set at too high a proportion of income (50 per cent or more) that they act as a disincentive to the majority of the workforce that do not meet the demanding targets set. In the EU Member States, while there has been a significant spread of pay systems based on individual or team performance, they are normally at a proportion of income that enables firms to maintain the balance between incentive and disincentive.

There is an issue of the extent of unemployment and under-employment in the countries studied. The differences in measuring unemployment between the EU Member States and the NIS countries effectively rules out meaningful statistical comparisons, though it is evident that the official figures on unemployment in Belarus and Russia significantly understate the true extent of the problem. High levels of hidden unemployment and underemployment in firms in the NIS countries, coupled with growing levels of unpaid layoffs (euphemistically called 'forced vacations') means that national labour resources are not being used effectively. From a competitive perspective it means that firms in Belarus and Russia are at a disadvantage when it comes to adjusting their workforce in the most productive manner. In Belarus, for example, firms have been encouraged to take on labour whilst output has been falling. In Russia the situation is only slightly better in that firms are dissuaded from shedding surplus labour because of the punitive costs of redundancy.

Of course the price to pay for this freedom among firms to adjust their labour requirements is visible unemployment and the associated social and economic costs that come with it. Many firms in the UK have been through this adjustment process and have found it painful but ultimately beneficial (although the displaced workers might disagree). Productivity levels are generally comparatively high in the UK firms,

while wage and non-wage employment costs are comparatively low (among the EU Member States). Unemployment is also comparatively low which is not the case in Finland, yet here too the firms studied had in the majority of cases gone through labour adjustment. However, wages are noticeably higher in Finland and the associated employment costs substantial when compared to the UK.

It is possible to identify some of the key competitive issues that emerged from the analysis:

- Vulnerable sector to competition from the NIS producers;
- Capital intensive, large plants dominate production in Finland and the UK (where they are all foreign-owned) whereas domestic producers with labour-intensive operations are the norm in Belarus and Russia;
- Health and safety and environmental issues are a high priority in Finnish and UK firms and impose significant costs which is not the case in Belarus and Russia.
- The system of firms providing social benefits to employees is breaking down in Russia especially and to a lesser extent in Belarus.

Another issue relates to standards on health and safety at work where the divergence between the EU firms and the NIS firms is quite marked. It is often assumed by employers that a greater degree of attention to these issues poses a financial burden on the firm with consequent extra costs that will ultimately contribute to a worsening competitive position. However, the argument is advanced that instigating appropriate health and safety practices, while imposing extra costs, will eventually contribute to increased productivity through such factors as reduced absence from work.

### The Future

There are signs that labour markets and employer practices are moving towards the EU 'model', though the process is extremely slow in Belarus and seriously inhibited in Russia. However, it is difficult to conceive a clear idea of this EU model when there is still so much difference in approach between Member States, as amply illustrated by the labour markets in Finland and the UK. It is too misleading to consider that EU labour markets are converging, although it is reasonable to consider that certain aspects of their operation show increasing similarity. This emerges in the case studies, with the development of outsourcing and performance related pay elements as clear indications of employers in Finland and the UK adopting similar approaches. On this basis, labour markets in Belarus and Russia are also moving in the general direction of the EU, although it is obvious that there are still too many impediments to expect them to achieve even partial convergence within the next five or more years.

One particular area of legislation that is likely to figure prominently in the medium to longer term is that relating to the environment. Firms in Finland and the UK raised this as an important factor in their cost structure and one that was becoming increasingly demanding of resources. Firms in the fertiliser sector are in a sensitive environmental position and there was clearly some frustration amongst EU producers at the cost advantages enjoyed by NIS firms in the lack of comparable legislation and enforcement.

Greater attention to environmental matters will demand more capital investment from firms and this was recognised by case studies in all four countries. However, the EU firms in all three sectors had clearly a head start in terms of the quality and relevance of their equipment including that needed for environmental controls. Furthermore, the EU firms were generally committed to maintaining an investment programme that would ensure a head start over their NIS counterparts would remain.

## **Issues for the European Union**

From this study of labour standards and international competitiveness it is possible to isolate a number of key issues that could provide a focus for future policy in the EU. The issues discussed below are in no particular order and offer no solutions. Rather they are intended to stimulate debate about the future competitiveness of EU industry arising from its relations with the NIS.

### **Statistics**

The serious problems with the comparability of economic, social and labour market statistics represents a serious threat to understanding the scale of any potential threat to the EU from the NIS. Some efforts have been made to bring statistics in the transitional states in line with international recommendations and practices, but the rate and scale of the improvements has not been encouraging;

### **Social Dialogue**

Effective social dialogue is in its infancy in the NIS with independent trade unions and employers' associations only emerging slowly. Social partner involvement in the development of industry must be considered a prerequisite for firms and employees alike and the considerable, though varied experience of the EU Member States provides a good basis for advice;

### **Products and Marketing**

The degree to which firms in the transitional states represent serious competition for EU firms will vary between sectors. The nature of the product is important here (its bulk and ease of transportation, for example) and the proximity of NIS producers to EU markets. This makes Member States sharing borders with NIS countries (and CEE countries) particularly vulnerable and demanding special attention;

### **Import Restrictions**

In some sectors the prevalence of EU import restrictions is considered highly protective and their removal threatens the existence of some EU producers;

### **Labour Standards**

The threat posed by the relatively high labour standards and their contribution to labour costs in the EU is, for the most part, illusory. High standards in such areas as health and safety bring associated benefits which are not currently enjoyed by most NIS firms. Greater flexibility in pay and conditions allows EU firms to adjust production as required and encourage increased productivity.

The above issues provide a focus for assistance projects such as Tacis and PHARE, as well as indicating the kinds of support EU firms might need in the longer term as markets are inevitably opened up and competition intensifies.

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**FOOTNOTES**

- <sup>1</sup> The Tacis Programme is an EU initiative in the NIS and Mongolia which fosters the development of harmonious and prosperous economic and political links between the EU and these partner countries. Its aim is to support the partner countries' initiatives to develop societies based on political freedoms and economic prosperity. ACE represents a focused strand of the programme covering Action for Co-operation in the Field of Economics.
  
- <sup>2</sup> Trade union membership density is the ratio of total membership to potential membership, the latter including only those groups eligible to become union members (which normally excludes those unemployed, for example).
  
- <sup>3</sup> These codes of practice are not legally enforceable but can be used in evidence in the law (such as during an industrial tribunal).

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