ECONOMIC DEVELOPMENT AND THE LEVEL OF UNEMPLOYMENT IN THE CONDITIONS OF ECONOMIC RECESSION

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Abstract

This study looks into the analysis of macroeconomic correlation between economic growth and unemployment rate. Moreover it demonstrates this correlation within the present economic development of manufacturing companies, especially in the conditions of economic recession caused by world financial crisis. The analysis itself above all explores economic growth expressed by GDP indicators, and in addition it defines its correlation with unemployment rate in present conditions. In doing so, the correlation dependence between GDP and unemployment rate during present so called “post-crisis” status quo is compared with the growth of GDP and unemployment rate drop in the pre-crisis period. At the same time the economic development of manufacturing companies is analyzed and its correlation dependence on the number of employees participating in production is defined. Study furthermore looks into the way, how this discovered trend in economic production growth and the employment within manufacturing companies matches macroeconomic indicators of GDP growth and unemployment rate presented by state statistics.

Keywords: economic growth, level of economic production, recession, financial crisis, level of employment, unemployment.

JEL Classification: M21, J23

Introduction

The goal of this study is to find the character of relation between the trends of economic production and employment on the level of production companies in the period of today’s economic growth, following after the phase of economic recession caused by world financial crisis.

Economic recession caused by today’s world crisis essentially influenced economic development and the situation of labor market. Theoretical discussion about the course of the world financial crisis, questions about its phases and especially the period of its ending are still opened and unanswered. In the analysis of the reasons and impacts of the world financial crisis upon the economic development we can go out from the fact that the level of economic production predominantly in the advanced countries had fallen to red indexes. As a consequence of this the level of employment was falling – production companies were forced to lay off employees. In the common repute but also within the professional community the belief stays valid that in finishing the economic recession and in growth of the level of economic production will also the level of employment rise – for the achievement for most of the pre-crisis level of production, the companies will return to pre-crisis status of employment.

At the same time it is known that the economic production was stabilized already by the end of 2009 and in 2010 its slow rise was noticed in most of the countries hit by the crisis as it was due to newly imposed anti-crisis measurements from the position of governments and position of production companies. The development of Slovakia is not transcended form this trend. Macroeconomic indices of the level of economic production was testifying to its rise, what is in line with trends in macroeconomic indices of level of employment respectively the unemployment.

Research methods used in given study:

- analysis of the macroeconomic statistical indices in economic development and level of employment in the period since the occurrence of economic recession till today,
- correlation analysis of trends of economic production and level of employment in the phase of economic recession and in the phase of smooth economic growth,
- realization of empirical research by the methods of structured interview with the purpose of finding the level of economic production and employment at the level of production companies in the phase of economic recession and in the phase of tame economic growth,
- correlation analysis of indices of the economic production and employment at the level of production companies in the phase of economic recession and in the phase of slack economic growth.

Scientific originality of the article is:
• defining the relations of indices of economic growth and level of employment in various phases of economic development – recession and growth,
• finding of the relation among the indices of economic production and employment at the level of production companies in the phase of slow economic growth,
• reasoning the absence and reasons of direct macroeconomic relation in indices of economic growth and indices of growth of employment in conditions of present economic revival.

Practical significance of the article is:
• scientific results of research of given study have a merit of creation and realization of concrete measures of economic policy,
• results of research are starting point for planning and realization of effective measures of state policies of employment and solving of problems of unemployment and elimination of its negative impacts and economic and social development.

Macroeconomic reflections on economic development and employment

Macroeconomic patterns relating to production factors within the economic theory have been formed mainly in the conditions of so called dominantly extensive development of industrial production. Under these conditions a direct correlation between the indicators of economic growth and the amount of used production factors has been recognized. The connection between economic growth and the unemployment rate was no exception. Even during present expert discussions it is reasoned, that there is direct arithmetic connection between the height of GDP and the pace of the unemployment rate growth. For instance, it is believed that economic growth expressed through the growth or fall of GDP is the major macroeconomic indicator of increasing or decreasing of economic activities on the commodity and services market. Above mentioned economic activities adequately raise or lower unemployment rate. These changes have substantial influence on the situation on the labor market and determine the development of the unemployment rate (Kárász, 2009). This relation is even being justified on the level of proportional statistic indicators of the GDP and unemployment rate growth or fall. For example, it is emphasized that decrease of the real GPD by 1 % causes the drop in the demand for new workers in the height of 20 % (Budúcnosť, 2009).

It is known that the structure of economic production changes in the process of technological development and labor productivity growth mainly in the industrial production, where it causes lazing off unnecessary workers. This redundant labor power in the conditions of extensive development of industrial and agricultural production was absorbed by the growing need within developing tertiary sector. However, in the second half of 20th century the industry shifted into the phase of intensive production (followed by agriculture and services at the end of century), in which the added value growth is seen as a result of higher labor productivity and reduction of input factors including labor power (Mcconnell, 1999). The advancement of knowledge economy, which is based on human intellectual capital and does not require vast amount of financial resources, raw material and man-power, has changed the situation.

In these conditions the direct linear correlation between the economic growth results and the input production factors can no longer by applied. Especially these dependences have been complicated by the economic recession caused by the world financial crisis. Nevertheless the crisis itself did not influenced nor caused the non-linear correlation. It has merely revealed the problems caused by previous period of economic growth. That is why the world financial crisis followed by economic recession has become some sort of milestone not only in the economic development but in the economics as well.

Even before the crisis some economists expressed doubts about the ability of modern economic order to ensure the stability of economic system and to solve the existing problems with its development (Stiglitz, 2003). This author emphasizes that the belief in the power of neoliberalism was not consistent enough. While there was strong rhetorical enthusiasm about free market, the government’s support (particularly subsidies for agriculture in developed countries) often resulted in negative effects on economic development.

In their responses to the world financial crisis most economists not only in its beginning (Gianella, 2008; Jung, 2008; Paletta, 2008; Skidelsky, 2008; Stiglitz, 2009) but afterwards as well (Sedláček, 2009; Staněk, 2009; Stiglitz, 2010; Time, 2010) voiced their opinions on the incapability of economic neoliberalism to solve existing economic problems. As stressed out by Joseph E. Stiglitz, the Great depression undermined the belief in macroeconomy – the ability to retain full employment, stable prices and sustainable growth. Present financial crisis stroke a blow to the belief in microeconomy – the ability of markets and companies to effectively distribute labor force and capital. This was a result of “so many
catastrophic cases of incorrect distribution of financial resources and inability to adjust to the risk factors that private sector was forced to ask for help from government in order to prevent the collapse of the entire system” (Stiglitz, 2008).

Unlike theoretical reflections of above mentioned authors, most of Slovak economists, entrepreneurs and politicians follow traditional macroeconomic relations between results of economic growth and input production factors when evaluating the course of economic recession and relations in economic growth tendencies, employment and unemployment rate. Even though quite realistic and even skeptic perspective on the course of economic recession and its impact on social and economic development prevails, the solution of the unemployment problem is expected to be in agreement with the proportional growth of GDP.

Similar expectations are based for instance on trends of economic development in Slovakia during period prior to crisis. Significant economic drop in Slovakia, which lasted from 1997 until 2000, and its impact on the employment resembled the one which can be observed nowadays. The fall of economic production, which followed the crisis with approximately one year delay, lessened the employment rate and caused growth of unemployment. This negative tendency reached its peak, when the unemployment rate hit the level of 20 %, which was a historic maximum. The ensuing economic development in the years from 2001 until 2007 was associated predominantly with the inflow of foreign investments, solving of negative credit portfolio of commercial banks and debts of manufacturing concerns. Changes on the labor market included improvement of its institutional aspects and labor legislative, creating of flexible mechanisms, which are able to react to economic changes, application of flexible forms of employing etc.

The tight direct correlation between GDP growth and the employment and at the same time quite tight indirect correlation between GDP growth and unemployment rate were typical for the whole period of this economic growth. During this period of time (2001 – 2007) an average rate, by which grew the number of employed persons in economy, reached 1.7 %. Unemployment rate sank by 8.8 % a year according to methodology of selected finding of labor force and by 13.1 % according to methodology of filed unemployment (Trh práce. ŠÚ, 2010). This movement in employment or unemployment development set in the period of 2001 - 2004, when the economic development expressed by GDP growth shifted from 3.4 % to 5.2 % and the unemployment rate fell from 19.8 % to 14.6 % (Tempo, 2010). Prior to this phase in spite of growth of economic efficiency the employment rate was falling and the unemployment rate was rising. However within above mentioned period the development of the employment rate was quite the opposite.

Exactly these positive trends in economic and employment development invoke optimistic expectations and influence the evaluation of present economic processes caused by world financial crisis and ensuing economic recession. Primarily is expected the end of economic downfall and the beginning of the following period of growth. Then, after expiry of certain amount of time a period of employment growth will come – just as it happened during characterized period. Therefore “in terms of further development it is necessary to point out that this relation will apply in the following years as well. It means that growth (fall) of economic efficiency will be connected with growth (fall) of employment rate and with the fall (growth) of unemployment rate “(Kárász, 2009, s.14).

With a certain amount of optimism we can say that it was year 2010 which presented a milestone in the economic development of develop countries including Slovakia and which was characterized by mild economic growth. That is why we will look into the way the economy is developing in these times of moderate economic growth not only on the macroeconomic level but on the level of individual manufacturing companies.

**Pre-crisis level of production and post-crisis state of employment**

In order to understand the nature of present economic processes it is necessary to briefly describe the course and origin of economic recession in Slovakia, which originated after and under the influence of world financial crisis. It is known that as a result of dependence of Slovak economy on exporting to other countries the economic downfall during the period of world crisis was influenced by fall of demand on the product market, which was observed in Europe and the rest of the world. The height of GDP dipped to 4.2 % in 2008. This drop was followed by another one during the next year – this time GDP fell by 12 percentage points (as seen in Tab. 1). The indirect correlation of filed employment rise was only 0.2 percentage point in 2008 and almost 5 in 2009. Year 2010 was marked by GDP growth by 7.5 percentage points – from minus 6.4 % in 2009 to 1.1 % in 2010. In spite of this tendency the unemployment rate decreased only by 0.4 percentage point. That means that slightly over 5 thousand applicants for work were employed in 2010, whereas more than 140 thousand employees lost their job during economic recession in the past two years.

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The question, whether this economic growth is sustainable or it is only certain oscillation within economic recession will be answered by time. Same as the question, whether or not in case of sustainable GDP growth the unemployment rate will fall, as it is expected. However, these macroeconomic relations do not provide relevant readings about specific causes and factors of decrease or rise of unemployment. Generally as a rule, the laying off of employees matches the economic soundness of unemployment increase. Companies usually lay off their employees in the times of economic difficulties and drop in demand for their products. Nevertheless this drop at the level of macroeconomic indicators may be influenced by some other factors, especially in short-term. These factors can be: elevated demand on new gained market segments, investment interventions, labor force migration, legislative measures, retiring of relevant part of unemployed etc.

The development during economic recession was very much alike. The fall of demand for products and goods forced the companies to reduce their costs. Laying off employees is one of the most frequent consequences and fairly effective way to do so in short time. This happens every time, when the company has to face economic difficulties. With the arrival of another economic phase – growth or the smallest possible oscillation connected with economic revival and the need for production enhancement – the companies do not employ workers automatically. Uncertainty caused by previous fall forces the management of these companies to be very careful when employing new workers. More often the companies begin to look for ways to rationalize within the organization of labor, management structure, motivation, standards and regulations, information flows, organization of overtime labor while absenting flexible forms of employing etc.

This tendency in behavior of companies is confirmed by the study we realized within the framework of solving the scientific assignment by grant agency MS SR VEGA in October and November 2010. The directors (or representatives or production managers) of 57 manufacturing companies mostly active in automobile, engineering or electrotechnic industry were addressed through the structured interview. In addition to the questions about the flexibility of labor relations we looked into the trends in production in the conditions of economic recession and into precautions taken to eliminate its negative impact.

All approached companies were compelled to reduce production mainly during the period 2008 to 2009. The production was cut by 16 % to 45 % in most of them. The dominant and practically the only measure, which came into consideration under these circumstances, was employee dismissal. Nearly half of these companies (47 %) reduced their staff by 3 %, one fifth by 5 %, one tenth by 6 to 10 % and 3 % of the companies dismissed more than 10 % of their employees. 14 % of the companies did under the threat of further reduction of production lay off even more employees than the up-to-date production situation demanded, what was consequently considered to be a useful step. Only 19 % of them tried to take different approach to the problem of costs reduction. In most cases they were applying organizational measures, work rationalization etc. However, these arrangements alone proved to be less efficient than expected and therefore also these companies had to make more radical decisions – employee dismissal.

Simultaneously with staff reduction was also often implemented work rationalization. And exactly this precaution was according to 95 % of respondents considered decisive in cost reduction and creation of certain reserve for production enhancement. Organizational changes aiming to reduce production costs were executed by 65 % of the companies, production standards and directions were revised by 89 %, information flows and processing were improved by 75 %, the system of motivation and rewarding was made more effective by 58 %, 14 % invested into new technologies, 12 % made use of their own innovations and 56 % used overtime work.
These actions were rewarded in the case of 3% of companies already by the end of 2009, when they obtained commissions which led to extended production. The biggest part of interviewed companies (87%) started to raise their production in 2010 but 7% of them have not managed to solve their problems. 84% from the overall number of companies, which succeeded in implementing of necessary precautions and managed to increase the production, reaches the pre-crisis level of production in 2010 (78% of all respondents).

Still, in most cases, this enhancement was not accompanied by recruiting new employees. Only 29% of companies hired new employees in 2010 and their number by no means matched or exceeded the number of workers dismissed at the beginning of economic crisis and this status is not expected to change in the near future. Merely one fifth of approached companies would be willing to recruit higher number of employees under the condition of obtaining the bigger amount of commissions, despite the fact that these dispose of necessary technological potential. Two thirds would employ more workers and invest into new technologies in case of obtaining stable orders and return on investment and state subventions would convince only one quarter. Under other than these conditions they see no need to recruit new staff, since they “learned” to produce more with fewer employees.

Representatives of production sphere in Slovakia call this situation “Pre-crisis level of production and post-crisis state of employment”.

This state of development of economic production and employing corresponds with state statistic data and some other macroeconomic indicators. As it was already mentioned (Tab. 1), GDP growth in 2010 reached 7.5 percentage points while showing moderate indirect correlation with unemployment rate decrease (0.4 percentage point). Also the indicators of GDP growth confirm that the industry in 2010 exceeded the expectations and the industrial production swiftly resumed its pre-crisis state. Slovak industry benefited particularly from quick recovery of German economy, which is the most important business partner (Slovenský, 2011).

Nevertheless, when it comes to the recruiting new workers, the prognosis of Slovak Ministry of Finance matches the attitude of industrial companies and therefore does not expect positive changed in employing (Tab. 2).

<table>
<thead>
<tr>
<th>Indicator</th>
<th>Reality</th>
<th>Prognosis</th>
</tr>
</thead>
<tbody>
<tr>
<td>GDP, real growth</td>
<td>-4,8</td>
<td>4,1</td>
</tr>
<tr>
<td>Employment (VZPS*), growth</td>
<td>-2,8</td>
<td>-2,1</td>
</tr>
<tr>
<td>Unemployment rate (VZPS)</td>
<td>12,0</td>
<td>14,4</td>
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<td></td>
<td></td>
<td>13,9</td>
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<td></td>
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<td>13,3</td>
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<td></td>
<td></td>
<td>12,5</td>
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<td></td>
<td></td>
<td>11,8</td>
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</tbody>
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Source: http://spravy.pravda.sk/slovensko-ma-pred-sebou-dobre

These data indicate that the labor market will remain to be influenced by the crisis. It is predicted that including Slovak citizens employed abroad the general employment should rise by 0.7%, what represents 16 thousand workplaces. But this is only roughly 11% from the total number of employees who lost their job due to the crisis.

**Conclusion**

One of many impacts of economic crisis as statistic data and results of our research of production companies suggest is the absence of expected tight indirect correlation between GDP height and unemployment rate. While during pre-crisis period the GDP growth was accompanied by proportional unemployment rate decrease, in the conditions of present GDP growth there is no tight correlation between GDP growth, employment growth and unemployment rate fall. In case this trend continues to prevail henceforward and is confirmed by further findings, it will require clarification and explanation of some economic theory soundnesses – generally accepted macroeconomic relations between GDP and employment. Simultaneously it will require a change of rules and approaches to the creation of specific measures taken by government. In the conditions when GDP growth does not solve the unemployment problem, the change of state policy principles is necessary in order to take such precautions, which would be effective when solving
unemployment problems and which would eliminate its negative impact on economic and social development.

References