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PUBLIC SECTOR PAY POLICY IN EAST EUROPEAN COUNTRIES

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Abstract *The public sector salaries in general, but especially in the civil administration has been and will be a topical issue, highly controversial, and with a permanent presence in the media. This article presents the developments that took place in wages of Eastern European public servants as a result of the international financial crisis.*

Keywords: Wages, public sector, private sector

JEL Codes: J31, J38

LITERATURE REVIEW

In the last decades a series of reforms have brought in public administration in almost every EU member state. Most reforms aimed the reducing of hierarchies, their leveling in organizations by introducing performance management systems and creating results-oriented mobility and flexibility.

Manuela Goretti in *Wage-Price Setting in New EU Member States* shows that the Romanian state employees have the most increases in salary package, and even exceed the total base salary. In nearly every category of state employees is applied a series of increases that does not alter their activity in any way the employee, the only role being to raise the salaries. Thus, the base salary in Romania is a disproportionately small part in the total remuneration; it fluctuated between 68% to 42% for teachers and public safety employees, excluding amounts paid by the employer social security contributions.

Costas Christou and **Juan J. Fernandez-Ansola** in *Romania: Wage Growth and Real Convergence* says that the sudden increase in public sector wages has put pressure on wages in the private sector, and statistical analysis shows that wage growth in the last 5-6 years in the Public sector has affected the private sector wage growth. In addition, it appears that total public sector employment grew at the expense of employment in private sector, on a labor market fairly tight. In

the jargon of economists, the employment in the administration had a crowding effect for employment in the private sector.

Indeed, public sector wage policy is the origin of certain anomalies in the structure of wages in Romania. Public administration wages were nearly twice the average wage at the end of 2006, due to their doubling in real terms since 2004. By comparison, the government salaries are close to the average wage in Germany and the Czech Republic are 10 percent lower than average wage in economy. While public sector productivity is difficult to measure, it would be difficult to claim that public sector efficiency in Romania, as measured by the quality of public services has increased significantly in recent years.

HOW MUCH EARN THE PUBLIC SERVANTS IN OTHER EUROPEAN COUNTRIES

At this moment, in Romania it is been more discussion about public sector wages, and to judge things in context, we want to see how we stand compared to other countries in the region and found themselves in financial crisis.

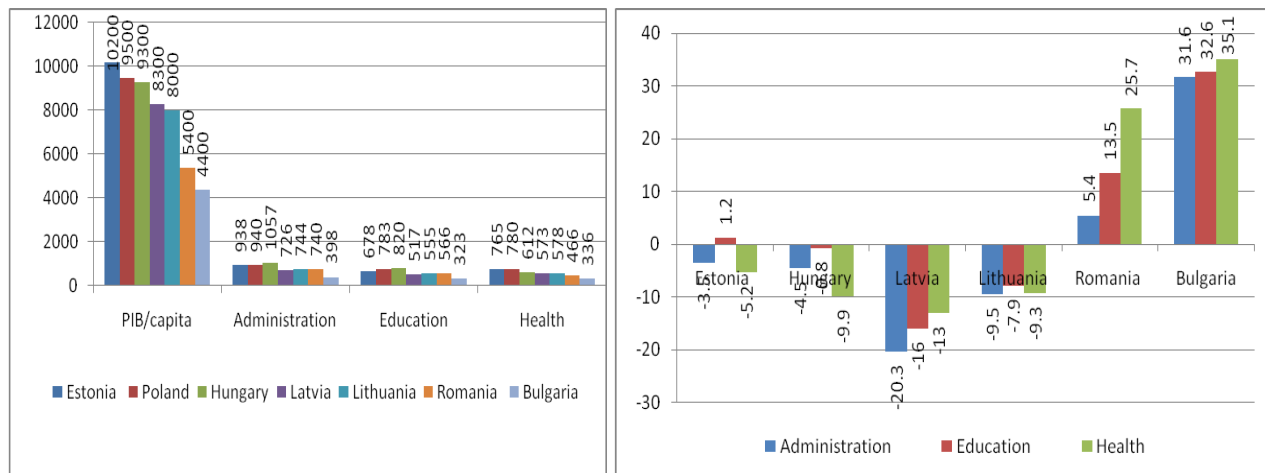
To establish a starting base, we need a ranking of GDP per capita, this indicator reflecting the economic capacity to sustain a certain level of wages. From the seven countries considered, Estonia has the highest GDP per capita, ie 10,200 euros in 2009. Follow Poland 9500 EUR, Hungary 9300, Latvia and Lithuania 8300, 8000 respectively, and long distance Romania and Bulgaria are 5400, 4400 euros respectively. Normally, it should be ranking in terms of public sector wages, but as you see, things are not quite so.

In public administration, the highest gross income is realized by the operation in Hungary 1057 euro. Polish and Estonian officers collects an amount of approximately 940 euros, while those from Romania and Lithuania 740 euros. Last in the ranking are Latvians and Bulgarians, with revenues of 726 respectively 398 EUR.

It should be noted that Romania pays similar wages like Latvia and Lithuania, although the two countries have a GDP per capita with 50% higher.

In Education, the highest salaries are still paid in Hungary (820 euros), followed by Poland (763 euros), Estonia (678 euros), Romania (566 euros), Lithuania, Latvia and Bulgaria, details below. And in this area, the Romanian government pays higher wages than two of the Baltics.

Graphic 1 Monthly Income and GDP per capita Graphic 2 The evolution of wages over the past two years: 2008-2010



Source: the sites of statistics institutes in the countries considered

In Health, the highest average income is recorded in Estonia (EUR 765), Romania being on the penultimate position with 466 euros. In Bulgaria, the average income is only 336 euro.

Now we compare the wages from Q1 08 and Q1 10. In Latvia, the average income in the first quarter of 2010 in public administration sector was 20.3% lower than two years ago, Hungary was 4.5% lower (although the Hungarians have the highest average salary), in Romania was higher by 5.4% and 31.6% in Bulgaria with more details below. The percentages show the variation of income in local currency.

In education, the percentages range from -16% to +32.6% in Latvia and Bulgaria, and in health between 13% and 35%. As we can see easily, in education and administration, the wages in Romania are comparable to those in more developed countries than ours, and health continues to be "Cinderella" of the budget sector.

HOW HAVE EVOLUTED THE WAGES OF ROMANIAN PUBLIC EMPLOYEES INTO THE LAST 13 YEARS

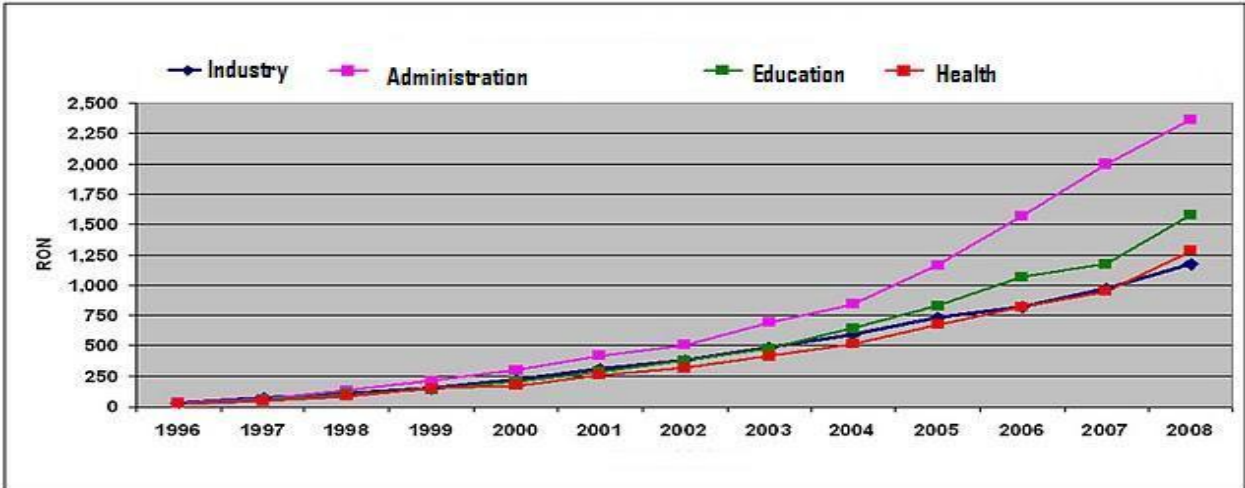
It was also mentioned recently about the evolution of wages of different categories of employees in the public system, the unions from this sector very often claiming that those who work "for state" would be disadvantaged compared to those working in private because the state pays poorly, and the wage increases recent years do not keep up with what private companies offer.

To see how things are, let's take a look at the evolution of wages in Education, and Health Administration since 1996 and compare these figures with the average wage in industry evolution.

In 1996, the highest average net salary was in the industry, an amount of 35 RON, after which were in Public Administration and Defense 30.5 RON, Education 27.6 RON and Health and Social Care by 22.8 RON. The values seem extremely low compared with the amounts of today but should not make such a comparison because there were other times in 1996.

After 13 years, respectively at the end of 2008, first among the four segments the Defense and Administration employees arrived with a net income of 2.364 RON, up 7661% (76 times) compared to 1996. In second place is education with a monthly net income of 1.579 RON, up 5630% compared with 1996 and third place came those who work in Health and Social Work, with a gain medium 1288 RON, up 5508 %. This explosion of salaries in the public sector has made the industry to move from first in 1996 to last place in 2008 with a net income increase of only 3250%, the amount reaching 1173 RON. The chart below tells all about this trend.

Graphic 3 Evolution of net wages between 1996 and 2008 comparison between the economy sectors



Source: National Institution of Statistics

If we consider just what happened between 2004 and 2008, we see that civil servants and the army have received an average increase of 179.8%, those in education have received more than 143.7%, those of health also had a of 147.4%, while last place in terms of net monthly earnings growth is still the industry, only 95.5% extra.

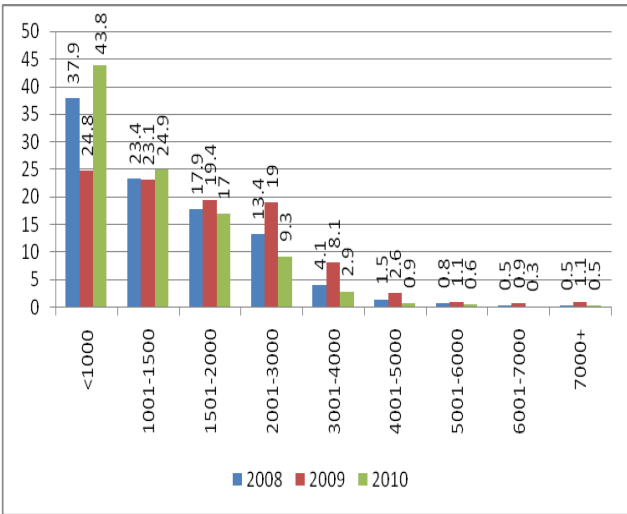
It is obvious that there are so huge salary discrepancies between different categories of state employees and especially between those within the same category and those few who earn more than the average shoot up, but the figures do not lie. In a society that would have developed normally, it was impossible those in just four years to have an increase in public sector wages that exceed more than 50-70% growth in the private sector. In Romania, this happened for all these

years, because the public sector unions knew how to push governments in the sense of granting wage increases that were not linked to any index of performance.

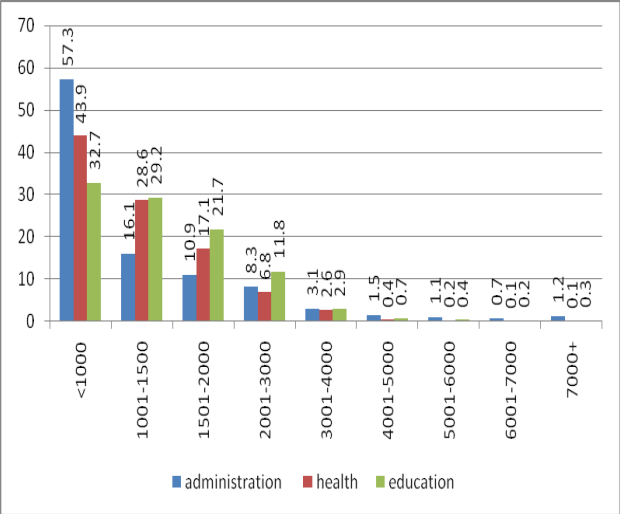
THE DISTRIBUTION OF PUBLIC SECTOR WAGES: THE MOST EMPLOYEES HAVE AN INCOME LESS THAN AVERAGE PENSION

In October 2010, the total number of full-time employees who worked in Administration, Education and Health was 888,165, down 61,653 people from October 2009, and 20,890 people from October 2007. From these, 20.3% made a gross earning less than 701 lei, 43.8% recorded a gross earning less than 1,000 lei, while 85.6% earned less than 2,000 lei gross. For comparison, in October 2009, before 25% reduction in wages, the share of those earning less than 1,000 lei was only 25%. Distribution of employees by installments to win the last 3 years has been joined in the graphic 4.

Graphic 4 Employees’ distribution of income installment between 2008-2010 and by public sectors



Source: National Institution of Statistics



Source: National Institution of Statistics

By public sectors, the figures look like this:

I. Public Administration

In this sector, in October 2010, 282.991 people were working, compared to 325.909 in October 2009 and 286.256 in October 2007. The distribution portions of the employees gross salary shows that one-third of them earned less than 701 lei gross and 57.3%, 1.000 lei less gross. In other words, nearly 6 in 10 full-time employees charged after a working month less than 741 lei net (180 euros respectively). Moreover, do not forget that the average pension is 730 lei, which

means that most employees from Administration earn less than an average retiree. In October 2009, the percentage of those earning less than 1,000 lei was 40%. At the other extreme are those who earn more than 7,000 lei gross, increasing their number from 4967 to October 2009, at 5158 in October 2010.

II. Education

The number of full-time employees in October 2010 was 350.526, down 9112 from October 2009, and 23.781 from October 2007. From these, one third has lower gross wages of 1,000 lei, while 72.6% had salaries of less than 1,500 lei. In 2009, before the pay cut, the share of those earning less than 1,500 lei was only 37.5%, which means cutting wages by 25% in this area has a total payroll of over 80.000 people.

III. Health

The number of full-time employees was 254.848, down 9623 from October 2009 but in 6156 compared with crestre October 2007. In employees' share of income installment, 43.9% of the employees earn less than 1,000 lei, while 72.6% less than 1,500 lei gross; at the opposite side being located just 345 employees who gains more than 7,000 lei gross.

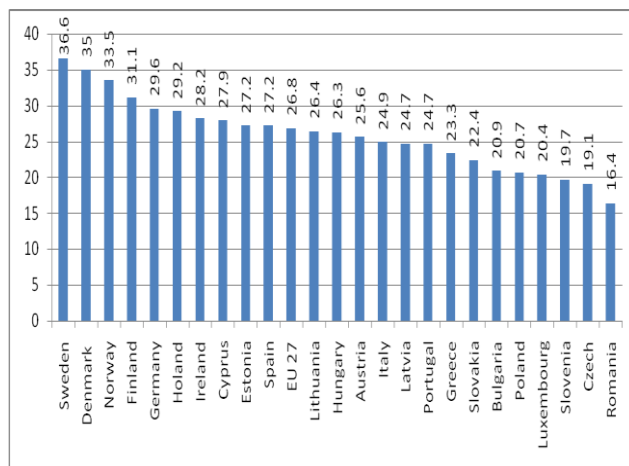
The above figures show that in public sector, the wages do not generate large costs to pay staff, but the number of employees is doing that. The expenditure on staff salaries budget is 8-9% of GDP, compared to 5-6% in Western countries and that wage growth does not lead to a further unbalancing the budget can only be done while reducing the number of employees.

HOW MUCH MONEY PRODUCES A PUBLIC EMPLOYEE? A COMPARISON ROMANIA VS OTHER COUNTRIES

We seem often to say that teachers and doctors do not produce money, but this is not true. From an economic perspective, any person who produces value-added are working, and this added value is converted into money, thus contributing to the GDP.

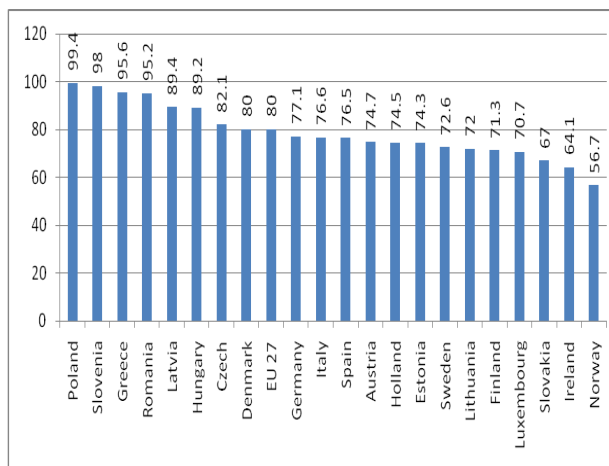
According to Eurostat, the value added generated by the public sector in Romania (Administration, Defense, Education, Health, Social, etc.) was 18 billion euros in 2009 and 16.4% of GDP, our country being on the last place the EU in this regard.

Graphic 5 Share of public sector in GDP (%)



Source: OECD

Graphic 6 Public sectors GDP versus private sector GDP (%)



Source: Eurostat

For comparison, the average share is 26.8% in the EU, with the Nordic countries located in the top with a percent of more than 30-35%.

By sectors, the figures look like this:

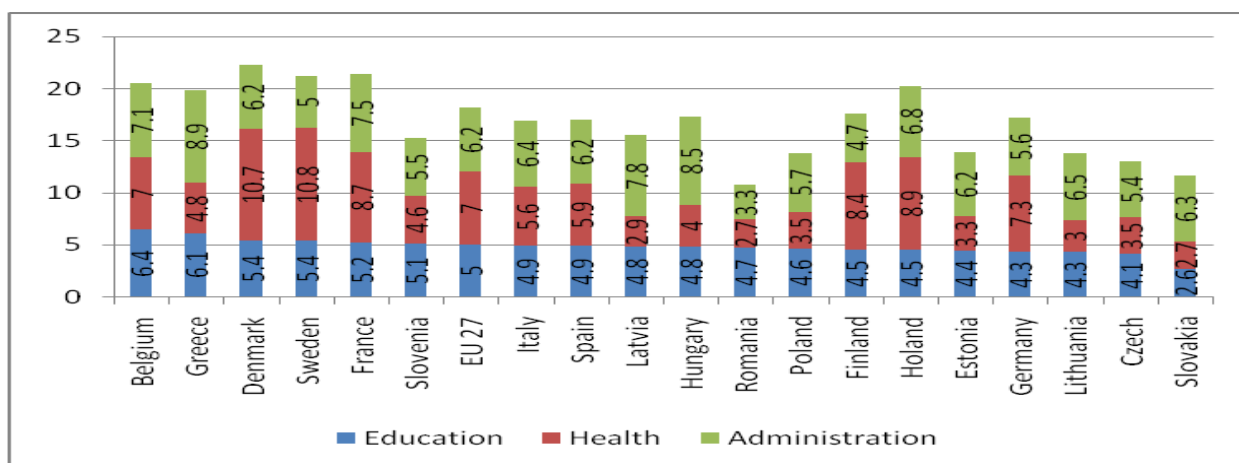
1. *Education* in 2008 generated a value added of 5.6 billion euros or 4.7% of GDP, the EU average is 5%. In absolute amounts, each employee has produced an average of 5.5 euros per hour, while the EU was the sum of 26.5 euros per hour. In the Eurozone, an employee in the Education sector has produced an added value of 32.6 euros per hour.
2. *Health* (plus social activities) generated 3.2 billion euros or 2.7% of GDP, while in the EU sector share was 7%. Value added averaged 4.5 per hour of work, while the EU average was 25.8 euros per hour.
3. *Administration and Defense* produced the added value of 3.3 billion euros or 3.3% of GDP, the EU average is 6.2%. A Roman officer produced 6.9 euros per hour, significantly less than the EU average is 27.6 euros.

Overall, the number of people working in the above sectors totaled 1.495 million last year, and considering that the gross added value produced by them was 18 billion euros, it follows that each employee's work was worth an average of 12,040 euros. The EU average was 38.540 euros. Now, we report the national GDP of the active population, namely people who contribute to its formation. Eurostat data show that in 2009, Romania's active population was 9.17 million persons, while the GDP was 116.4 billion euros, which means that the average per capita was 12,693 euros, a value similar to that generated in the public sector (12040 EUR).

How the things are in other countries can be seen below. In Norway for example, a public employee generates a value-added of 53.600 euros, a figure that represents only 56.7% of the

added value generated by an active person. And another chart shows the share of Education, Health and Public Administration in GDP. Please Note especially the differences between us and others countries regarding the education sector share in GDP.

Graphic 7 Shares of Education, Health and Administration in GDP



Source: Eurostat

CONCLUSIONS

Despite popular belief that the classical Weberian bureaucratic organization tends to become too rigid, resulting in procedures that are slow, with employees and citizens frustrated, yet there is not a universal alternative to bureaucratic model.

Most countries have attempted to formalize the link between evaluation and promotion of the civil servants and their wages. In most countries, part of the total remuneration of civil servants is variable. While all countries with a career orientation have implemented variable pay schemes for civil servants at the opposite pole lies systems that are based on performance criteria (Belgium, Spain, France and Mexico).

Countries with a system based on the orientation functions have generally implemented a salary system based on performance (UK, U.S., New Zealand, Finland, Italy and Canada).

In developed countries, employees of the Education, Health and Administration are generally paid better than average economy, but this situation is possible because the active population involved in areas that „cause money" (industry, construction, financial) generates a added value significantly higher than public sector employees. In Germany for example, the gross added value generated by an active person is 30% higher than that generated by public sector employees, making it possible to "subsidize" the latter by others.

In Romania, a value-added active person with only 5% higher than a public sector employee, making it extremely difficult, "subsidizing" those in education and health by other employees. Share in GDP of the sectors discussed above should grow, which means that in coming years, the value added generated by the employees of these sectors have to grow faster than the overall average. How we do it? We know that the state is a poor manager, so the best way we can increase the value added is to outsource as many activities to the private sector.

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