

Adaptivity of the labour market in Ukraine during the COVID-19 pandemic: Analysis and policy recommendations

- Summary of results -

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1. Introduction

Background

- The COVID-19 pandemic plunged the Ukrainian economy into severe crisis
- Many companies were hit hard by the lockdown (e.g. being forced to close) or sudden drops in demand due to the crisis
- In order to remain financially afloat, companies had to quickly cut labour costs as one of their largest cost components
- Labour market regulation constrains companies' ability to quickly reduce labour costs by firing workers or reducing working hours and pay
- Government undertook measures to improve adaptation on the labour market
- This policy briefing summarizes the results from PS/01/2021

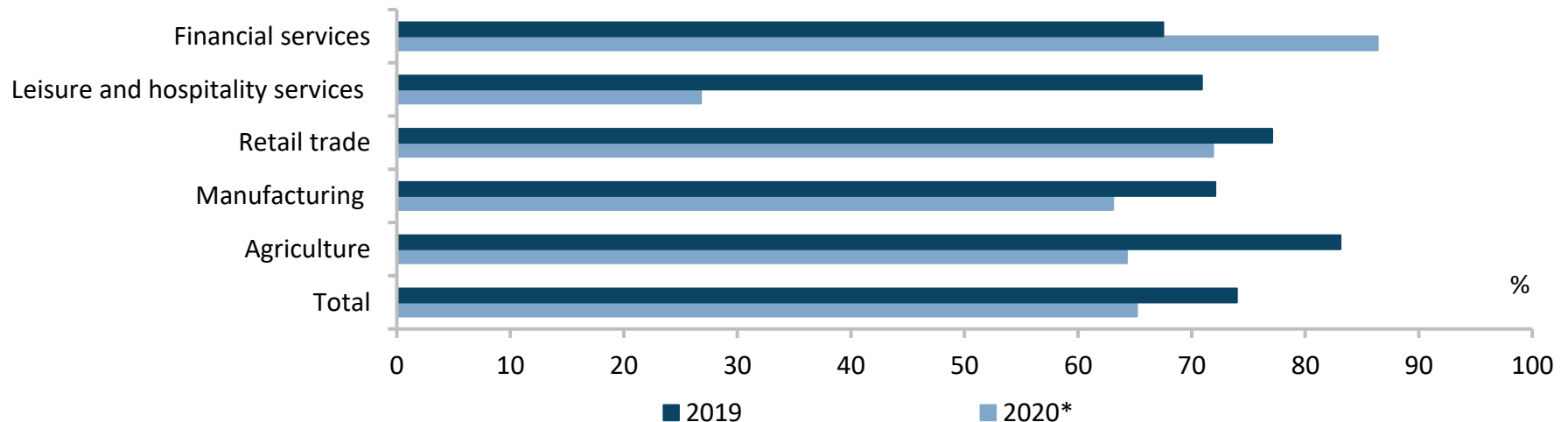
Purpose of this study

- Analysis of different ways for companies to adjust to the crisis with regard to their workforce
- Generating conclusions of how the adaptivity of the Ukrainian labour market to crises can be improved in future

2. How severe was the shock?

- Shock hit the economy through domestic and external channels:
 - Domestic quarantine measures, e.g. closures of non-food retail, hospitality sectors
 - Drops in demand e.g. due to stoppage of car production in EU
- Result: Sharp crisis with -4.0% yoy GDP growth in 2020

Share of SMEs that reported positive profits



Source: Ukrstat, *January-September data.

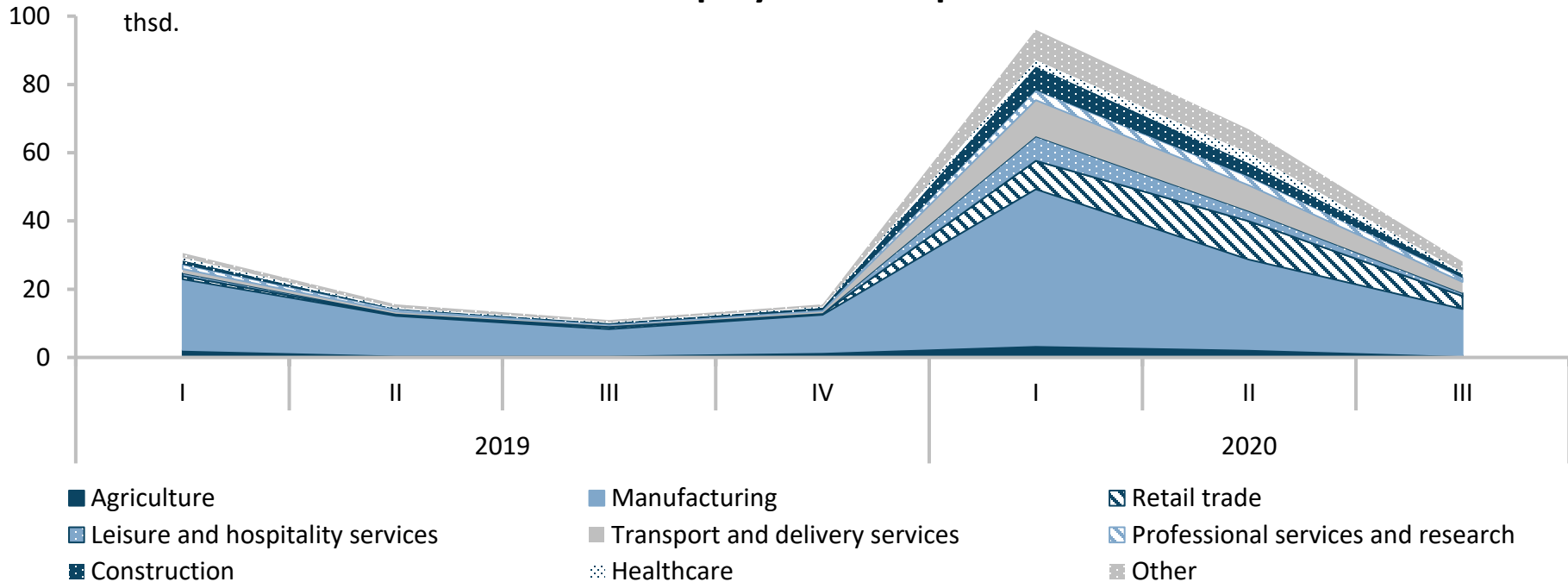
- Many companies were making losses and had to cut costs quickly
- Impact differed across sectors

3. Four mechanisms of labour market adaption

- When faced with a sharp, but temporary crisis (forced business stoppage or sharp demand slump), companies would ideally prefer to
 - Reduce labour input with corresponding decrease in wage costs
 - Maintain contractual links to skilled and trained workers
- Due to labour market regulation, companies' options are constrained and they cannot unilaterally change the labour input at will without consent of workers
- We analyse four main mechanisms for companies to adapt to the crisis:
 1. Asking workers to take paid or unpaid leave
 2. “Partial unemployment”: The state furlough scheme
 3. Reduction of working hours of employees
 4. Layoffs of workers
- Objective: Find out what options existed for companies to reduce labour costs, what conditions applied and how the options were used

3.1 Paid and unpaid leave of employees

Number of employees on unpaid leave

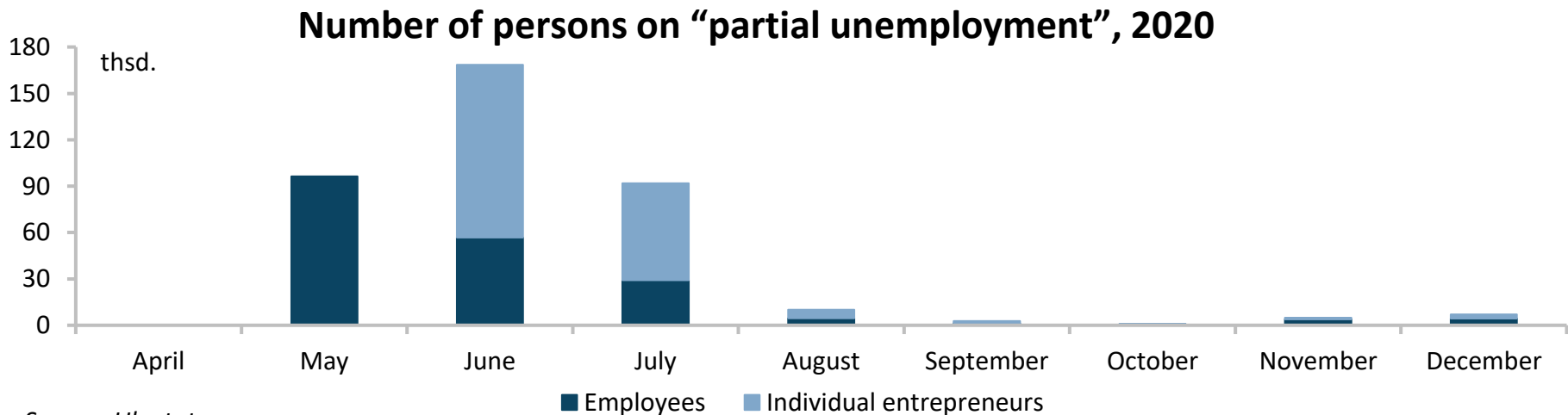


Source: Ukrstat

- Aim: Quickly reduce labour input and costs without firing employees
- But unpaid leave must be requested by employees (but often informal pressure from employers)
- Government relaxed restriction on number of unpaid leave days during crisis
- Limited usage: At peak of crisis, 96 thsd. employees on unpaid leave

3.2 “Partial unemployment”: The state furlough scheme

- New line of partial unemployment scheme was launched in crisis
- Available to SMEs and individual entrepreneurs whose business was stopped due to government measures
- Wage costs taken over by the state: Two thirds of regular salary, capped at minimum wage level (4723 UAH per month)
- No need for consent of workers



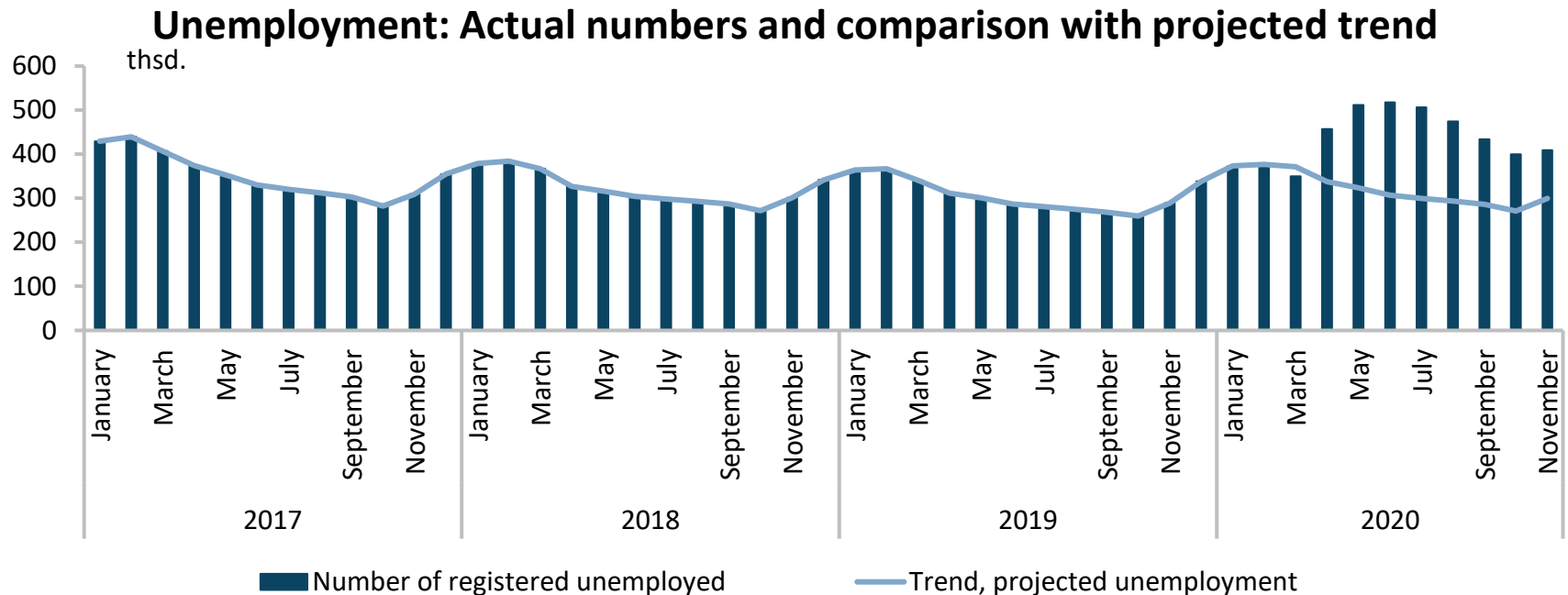
Source: Ukrstat

- Limited take-up, although such programmes are usually highly attractive for companies (immediate labour cost cuts whilst retaining workers)
- Possible reasons: Limited eligibility and generosity of scheme, lack of information about the scheme

3.3 Reduction of working hours of employees

- Without labour market regulation, this should be the preferred option for employers: Reducing working hours and pay of employees
- However, such changes require the consent of employees in Ukraine as in most other countries
- Uncompensated reductions in working hours may have occurred in Ukraine due to cooperation between employers and employees or informal pressure being exerted
- Data is not fully conclusive:
 - Average hours worked per employee and month dropped from 140 in March to 122 in April and 119 in May
 - But this includes paid/unpaid leave, partial unemployment and compensated reductions in working hours (=without pay cut)
- We conclude that there was some usage of this adaption mechanism, but labour market rigidity restricted wider usage

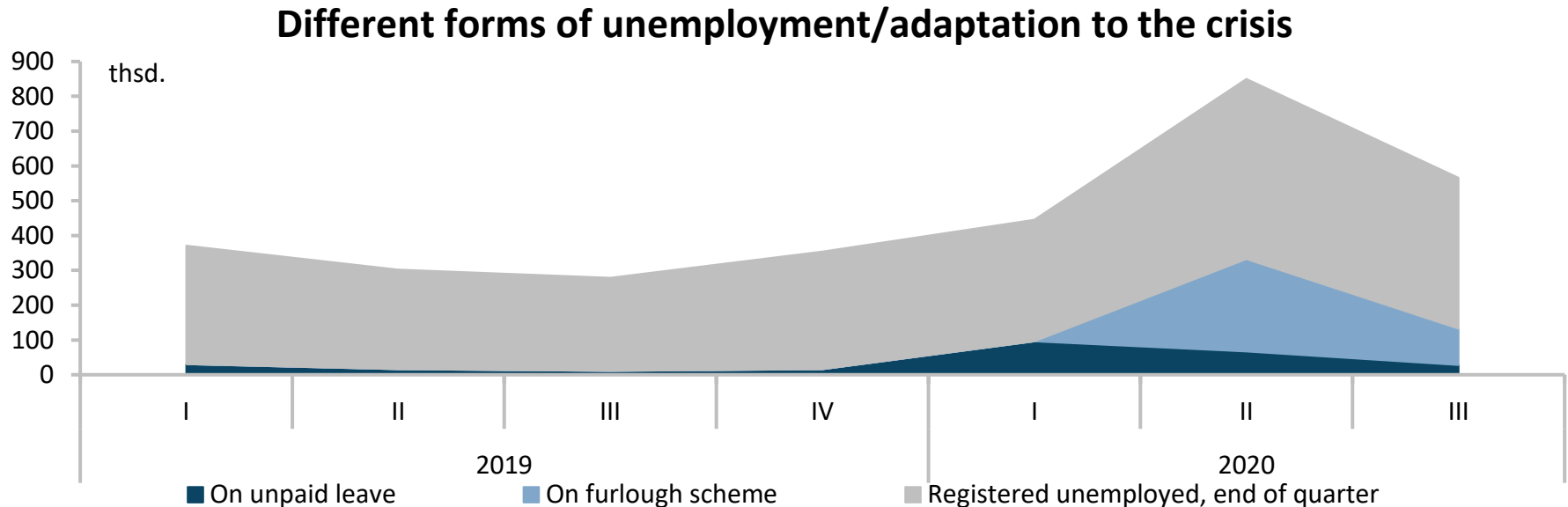
3.4 Laying off employees



Source: NBU

- Layoffs require “organizational reasons” (e.g. must close a business unit), 2 months notice and 1 month severance pay to be permissible in Ukraine
- Not really ideal for companies: Lose link to trained/skilled employees and only effectively reduce labour costs after three months
- Nevertheless, this was the main adaption mechanism used during the crisis!
- Peak during May/June, 2 months after beginning of severe lockdown

3.5 Consequences for the labour market



Source: Ukrstat, State Employment Service

- All four adaptivity mechanisms were used by companies
- Despite formal and rigid labour law, layoffs were the most widely used mechanism of adaptation
- Only a limited number of SMEs used the “partial unemployment” scheme

4. Conclusions and policy recommendations

Conclusions

- Labour law in Ukraine is quite rigid and constrained the ability of companies to flexibly react to the crisis
- Although clearly sub-optimal and constrained itself, layoffs were the main response of companies to the crisis
- Also, high rigidity appears to have encouraged the development and use of informal ways to work around labour law rigidities
- A better balancing of the interests of workers and companies should be pursued that leads to better outcomes for both

Policy recommendations

- **Considering extending the “partial unemployment” scheme into a full-blown short-time work scheme**
- Adding “adverse economic circumstances” to the permissible grounds for layoffs to avoid difficult workarounds of “organizational reasons”

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