

# “Strategic management and management of personnel costs: employing young people in the Slovak Republic”

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## SECTION 3. General issues in management

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### Strategic management and management of personnel costs: employing young people in the Slovak Republic

#### Abstract

This paper focuses on evaluating strategic management of the labor market through legislated active labor market measures introduced in the Slovak Republic to support youth employment. Based on the presented statistical data and managerial and legal analysis of the labor market in the Slovak Republic, with particular emphasis on the economic status of young people, two key parts of the adopted strategic document should provide better economic security for young adults. From the point of view of employers the initiatives are an attractive means for incorporating young adults into the economy, especially because this allows for increased active management of personnel costs that are directly related to compensatory incentives from the side of state agencies for employment of young people. This strategic management creates possibilities for employers to gain access to lower labor costs and to realize significant cost savings. Supporting data are presented graphically and at the same time the cost savings for employers are calculated. Overall, these two analyses demonstrate the practical effect of the new strategic measures on corporate management of personnel costs.

**Keywords:** strategic management, management costs, youth unemployment, labor regulation, right to first employment.

**JEL Classification:** K31, M12, M54, O15.

#### Introduction

A high level of youth unemployment brings multidimensional costs that can be significantly higher than even potentially-expensive public policy interventions. Finding a solution to the high rate of youth unemployment has been a significant challenge for initiators of public policy in the developed world during the post-industrial period. Due to structural changes in society, it is apparent that conventional solutions to youth unemployment will not be successful (Olšovská, 2010; Švec-Schuszteková, 2013). Practical experience from individual corporations in the manufacturing sector in the Slovak Republic highlights significant issues in the long-term planning of production processes (Raisová-Đurčová, 2013; Olšovská-Švec, 2014; Novotný, 2014; Barinková, 2014). This has been caused primarily by the lack of a qualified workforce within the desired age range since potential employees with technical education younger than age 30 are in short supply. But there is a relatively large group of unemployed youth in the labor market, who due to various objective conditions (e.g. lack of education) or subjective conditions (generation Y culture) do not want to work and participate in economic activity (Lisý et al., 2011; Čapošová, 2013; Mura, 2014; Novotný-Polčíková, 2010). This unsustainable state has also been explored by Grmanová-Havierníková (2008) and Vojtovič (2012). The existence of this group of

unemployed youth has led Slovak lawmakers to search for suitable measures to improve their employability (Poór et al., 2015; Novotná-Volek, 2014). Except for limited corporate initiatives (Buleca, 2013; Buleca, Raisová, Michalski, 2014) most businesses also rely on some support by lawmakers to actively address the youth unemployment crisis (Šimo-Mura, 2015; Hadvabný, Korimová, Buleca, 2012). Legislators have an incentive to introduce measures addressing this issue because of the negative effects of long-term youth unemployment on the national economy and the unfavorable social phenomena that are correlated with high levels of long-term youth unemployment such as an increase in criminal activity and an increase in use of narcotic and psychotropic substances. A long-term level of high youth unemployment equally threatens the cohesion of society and can lead to an increase in radical and fringe groups within society. Vojtovič (2011), Švec (2015), Čapošová (2015) and Dolobáč (2014) pointed out the need to apply strategic and personnel management to solve this macroeconomic, social, and societal issue. Major strategic measures to improve the level of youth employment were implemented in the Slovak Republic in the last two years (Olšovská, 2014).<sup>1</sup>

These measures are expected to contribute to a reduction of unemployment among young people and at the same time can be a significant source of cost savings for "initiative employers" and allow them to quickly gain access to a lower-cost labor

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<sup>1</sup> The Ministry of Labour, Social Affairs and Family of the Slovak Republic. Report on the Social Situation of the Population of the Slovak Republic for Year 2014. [online] [cit. 2015-09-16]. Available at: [http://www.employment.gov.sk/files/slovensky/ministerstvo/analyticke-centrum/sprava\\_o\\_socialnej\\_situacii\\_obyvatelstva\\_za\\_rok\\_2014.pdf](http://www.employment.gov.sk/files/slovensky/ministerstvo/analyticke-centrum/sprava_o_socialnej_situacii_obyvatelstva_za_rok_2014.pdf).

force. Understandably, the unanswered question is the sustainability of these measures and the level of interest among employees and employers in taking advantage of the possibilities. Based on the initial number of applications for these programs, the interest of the employers appears to be quite high.

## 1. Goals and research methodology

The main goal of this paper is to evaluate and analyze the effect of strategic legislative measures focused on supporting employment of people younger than 29 years of age in the Slovak Republic as a means of ameliorating their high unemployment rate. At the same time, we emphasize the relationship between the legislated strategic management measures and the opportunities they provide for employers to achieve active and sustainable management of labor costs. Further, this paper presents an analysis of the possibilities in corporate personnel management to move beyond their traditional pool of applicants. The primary data presented in this paper were collected as part of the scientific project VEGA No. 1/0805/13 "Optimization of the layout of the model of work relations in the labor market in the Slovak Republic" financed by the Ministry of Education of the SR and the secondary data come from a review of various literature sources.

## 2. Initial labor market conditions and youth unemployment

The long-term unemployment rate in Slovakia is one of the higher ones within Europe and the recent economic crisis has only deepened this problem. The overall unemployment rate dropped slightly in 2015 but it is still above the EU average (12.5% compared to 9.9% across the EU-28 in December 2014). Additionally, unemployment in Slovakia has been usually related to structural issues rather than cyclical issues and has tended to have a long-term character. In Q2 2015, unemployment declined by 2% compared to Q2 2014 and the current unemployment rate in the Slovak Republic is 11.2% (Statistical Office of SR, Ministry of Labor, Social Affairs and Family of SR). However, weak demand for labor and a low number of job openings relative to one of the lowest workforce turnover rates in the EU has still created one of the highest unemployment rates in the EU (10% when compared to 5.1% in the EU-28 in 2013). The main causes of the labor market weakness include: low employment levels of certain groups of citizens (young people and people over age 55); a system of taxation and social benefit-based factors that discourage people from seeking work; a weak capability of public services in assisting the most discriminated applicants for jobs; and relatively low internal workforce mobility geographically. The youth unemployment rate in December 2014 (more recent statistics are not yet available) dropped slightly to 28.9% (the lowest rate

since 2009). However, the Slovak Republic is still among the top eight highest rates for youth unemployment in the EU. Almost two-thirds of the unemployed young people have been looking for work for one year or longer, which is the highest rate among all EU member states. The rate of young people who are unemployed and not in the process of education or professional training is getting close to the EU average. Approximately 60% of the unemployed in Slovakia are workers with low qualifications and almost 70% of the long-term unemployed (out of work a year or longer) also tend to lack advanced qualifications. Both percentages are among the worst in the EU-28. While the tax burden on workers with low incomes was approximately at the EU average level in the years 2013-2014, the overall support by social welfare is relatively low in Slovakia. Nonetheless, certain factors may still persist that discourages work in certain types of households at the lower end of the income spectrum.

In regard to education and the workplace, the transition from school to work remains problematic and the education system does not react quickly enough to the needs of the labor market. This issue especially impacts graduates of vocational education and training programs as well as college graduates. Vocational education and vocational training necessary for the labor market are inflexible from the professional management point of view as well as for regional development and do not allow long-term sustainable development of Slovakia's regions. The relevancy of a college education and its quality for the labor market is also troublesome at best. We believe that all these are arguments for implementation of strategic management of the labor market. Predicting the required skills for labor force success thus far has been unsatisfactory, which contributes to the dissonance between the demand and supply of qualifications and skills.<sup>2</sup> Econometric modelling of this and some other phenomena were explored, for example, by Bánociová and Pavliková (2013), Benda Prokejšová-Paluchová (2014) or Olšovská et al. (2014). The ratio of bachelor's study programs designed towards specific occupations is still very low and there are no individual accreditation criteria for these programs. There is also a persistently high ratio of college graduates working in jobs that do not require college education. The current financing system for education, based on the number of students, is more suitable for socially-oriented study programs, which is contrary to the current requirements and needs of the labor market.

<sup>2</sup> Employers in the auto industry complain that when entering the labor market, only 6% of the graduates of middle vocational schools are properly trained. For more details see the Report on the Social Situation of the Citizens of the Slovak Republic for Year 2014.

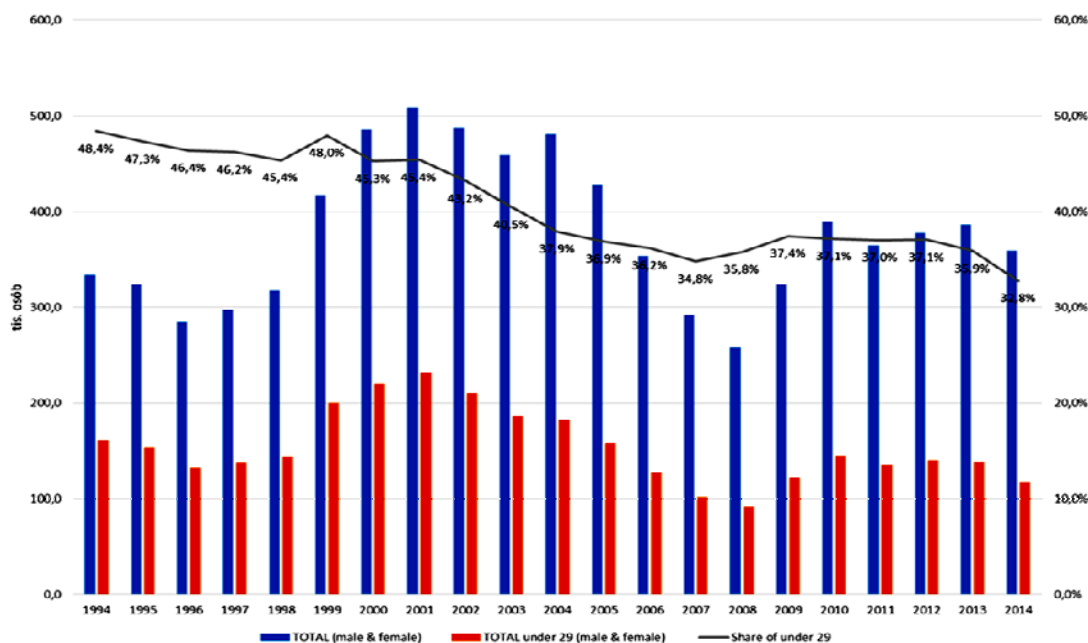


Fig. 1. Youth unemployment rate

Source: Statistical Office of SR, Ministry of Labor, Social Affairs and Family of SR.

Overall, the key factors that significantly contribute to high youth unemployment include: structural dissonance (i.e. the education that young graduates receive and their regional distribution does not correspond to labor demand); forecasting of labor demand and its structure is lacking; employers are focused on the qualified segment of the workforce; the education system is not responding or is not responding well enough to the needs of the labor market (obsolete fields of study); and finally a modular educational system is lacking. These structural issues are also entrenched in a period when the strong demographic effect of “baby boomers” entering the labor market is fading. However, we also must consider the decline of Slovakia’s traditional industries (especially metallurgy and the arms industry), saturation of the services sector, introduction of new technologies replacing the workforce, and similar additional factors that are driving up structural unemployment, particularly among youth. The level of income earned by people younger than age 29 does not correspond to their needs or to the real costs for securing necessities of life, while according to employers an increase in salaries is prohibited by the lack of professional experience as well as the high costs of hiring because of the employer’s obligation to pay levies to the social and health insurance systems.

### 3. Key measures and cost savings generated through strategic management and incentivizing the employment of young adults

Due to structural changes in society it is obvious that conventional solutions to youth unemployment will not be successful. Given the labor market

shortcomings discussed in the previous section, strategic measures to support employment of young people have been postulated, which do not have the traditional form that has been based largely on providing subsidized jobs. Measures of strategic management falling in the area of mid-term technical solutions tend to generate jobs immediately. Public policy makers have used this conclusion to create programs to incentivize the employment of young people through so-called guarantees for youths related to the 2020 Strategy of the European Union and the Recommendations of the Council of the European Union. Measures in the guarantees for young people consist of legislative reforms and specific initiatives (programs and projects) designed exclusively for people younger than 29 years of age. As part of the employment services, supportive conditions for finding a first job have been created for young workers, particularly those who traditionally have been passed over by employers due to their perceived lack of qualifications. The guarantees for young people are also conceived on the principle of programs and projects focused on a “second chance for education” for job applicants from socially weaker groups (finishing primary school, obtaining qualifications), preparation for starting self-employment, and support and counselling to help young people (including an increase in the number of professional counsellors) during their transition from school to work (counselling in choosing a profession, skill training and help or assistance with integrating into the labor market, a job or self-employment). Key measures such as a “right to a first job” and introduction of the “levy deductible item” have received the most support among employers.

#### 4. The right to a first job

The right to a first job should facilitate better youth access to the labor market, which is particularly difficult not only because of a lack of work experience and on-the-job skills but also because of insufficiently specialized education and the weak economic conditions facing small and medium-sized businesses, which are a primary source of new jobs. The right to a first job focuses on employing graduates younger than 29 years who have not previously held a regularly paying job lasting at least six consecutive months (a job applicant aged 25 to 29 years had to be registered as unemployed for at least 6 months and a job applicant younger than 25 years had to be registered as unemployed for at least 3 months). The state will subsidize part of the costs to hire and employ such a graduate for 6 to 12 months. In order to receive this benefit the employer must subsequently maintain the job for at least half of the agreed time period after the end of the subsidy. For example, if an employer accepts the benefit for 8 months, the job must be maintained for additional 4 months. Also, the employer must ensure that the subsidized employee will represent an actual increase in the annual number of employees. The amount of the subsidy depends on the rate of registered unemployment in one of the eight regions of the Slovak Republic. The monthly subsidy is 90% of the total cost of the employee but no more than the minimum overall cost of labor for the year 2015. Therefore the maximum amount of the subsidy to an employer for an employee in any month of 2015 is €475.76. Significant cost savings to the employer are also reflected in a levy deduction that is further discussed later in this paper. The effectiveness of this initiative can be seen in the small increase of the minimum overall cost of labor of an employee to €475.76, relative to the major 8.2% increase in the

minimum monthly salary from €352 to €380 (in 2013 the minimum overall cost of labor was €456.54 with a minimum salary of €337.70 and in 2014 the minimum overall cost of labor was €475.89 with a minimum salary of €380).

From the point of view of territorial distribution, the initiative has been particularly emphasized in the regions with the highest long-term unemployment and with the highest number of jobs being occupied by the previously long-term unemployed workers. Thus far more than 12,500 jobs for young unemployed people have been created under this initiative. The success rate of the measure has been reflected by the fact that after the end of its application almost 80% of these young employees stayed with the employer after termination of the subsidy.

#### 5. Levy deduction

On 1 January 2015 a deduction for the levy for health-care contributions for low-income employees was introduced.<sup>3</sup> This measure follows the concept of employment security for young people and their right to a first job because young workers are also frequently among the group of employees with lower incomes. An employee qualifies for this deduction if his or her monthly income does not exceed €570. Through this deduction the assessment base for purposes of social insurance system is reduced, i.e. when the employer applies this deduction for the levy, the overall cost of labor for the employee will directly drop as shown in the chart below. From a macroeconomic point of view the €200,000 loss to the state-based health insurance system will be compensated for by other subsidies from the state budget.

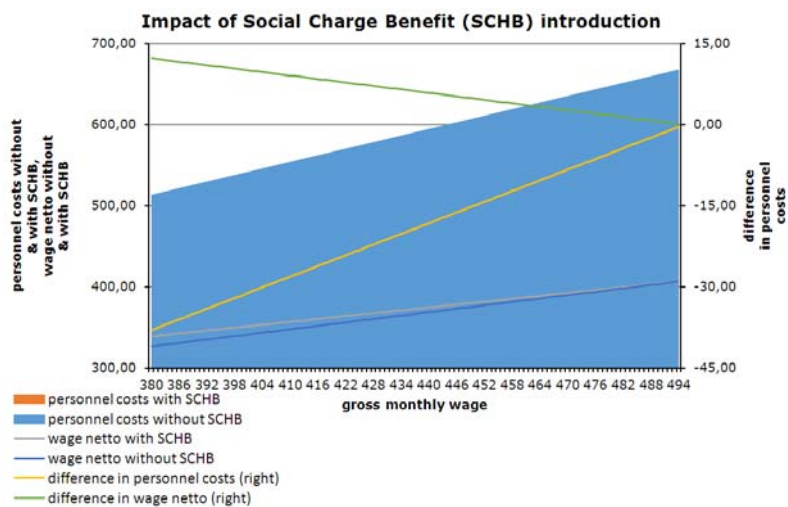


Fig. 2. Comparison of the total cost of labor and the net salary of the employee, including and excluding the levy deductible item

Source: Statistical Office of SR, Ministry of Labor, Social Affairs and Family of SR.

<sup>3</sup> Employers in the auto industry complain that when entering the labor market, only 6% of the graduates of middle vocational schools are properly trained. For more details see the Report on the Social Situation of the Citizens of the Slovak Republic for Year 2014.

Those employees entitled to the levy relief are those who earn less than €570 per month or €6,840 per calendar year. The levy deductible item is set in an amount corresponding to the current minimum salary in 2015 of €380 per month or €4,560 for the calendar year. An employee with a salary in the amount of the minimum salary will not pay any health insurance levy. For each additional €1/month in salary, the amount of the levy deductible item will drop by €2. The entitlement to the deductible item ceases when an employee's income reaches €570/month. If an employee's income is lower than €380/month, the deductible item cannot be higher than the amount of income. If the employee was not employed for the whole calendar month, the deductible item is reduced pro rata based on the number of calendar days in the month he or she was employed. The deductible item is

not reduced when an employee is not working due to sick leave, taking maternity benefits, etc.

Calculation of the levy deductible item:

$$DI = 380 - 2x(S - 380)$$

$DI$  = levy deductible item;

$S$  = salary of the employee per month.

To illustrate: An employee with a gross salary of €450 will pay €8.40 per month for health insurance rather than the original €18. The direct cost savings to an employer is even higher as the employer pays only €21 for health insurance for the employee instead of the original €45. The net income of an employee at the level of the €380 minimum salary will consequently increase by €32.

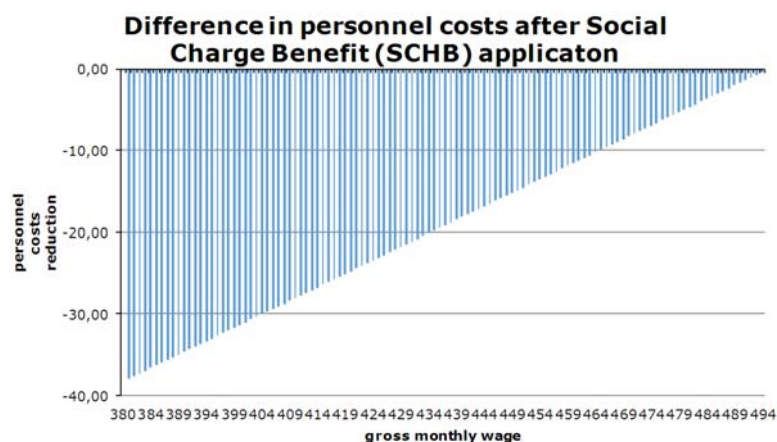


Fig. 3. Depiction of the reduction of the levy deductible item as salary increases

Source: Statistical Office of SR, Ministry of Labor, Social Affairs and Family of SR.

In regard to vocational education and training of people younger than 29 years of age, certain measures for improving their practical education through partnerships with companies have been adopted. The government approved the new act in January 2015 with a planned effective date of September 2015. The budget for 2015 contains confirmation of tax incentives for employers who are working to develop vocational education and training programs. The effect of the new act will significantly depend on support by companies and professional organizations to properly train students directly in the workplace. Projects with Austrian, German and Swiss employers, for instance like the very successful project called Young Stars, support this reform. A revised school financing system is being introduced that is focused on quantitative criteria such as the employability of school graduates.

## Conclusion

Many current mid-term strategic solutions to youth unemployment unfortunately focus on creating new jobs of a temporary character and do not establish a presumption of long-term sustainability. This form of

employment support for young people is positive but it does not incentivize employers to maintain those jobs. Nevertheless, current interest on the part of employers to implement the recent legislative measures reflects the incentives created by these measures for the active management of personnel and its associated cost-savings. Additionally, the new legislative initiatives are focused on creating a highly-qualified workforce prepared for the specialized conditions of employers in Slovakia's modern economy. In the future, additional legislative cooperation with social partners is expected to initiate further steps in strategic management that will lead to building a knowledge-based society and strengthening of the services sector as the future fields in which to create new, modern jobs.

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