



## **Joint Assessment of Employment Policy Priorities in Cyprus**

In accordance with the provisions of the Accession Partnership, the Government of Cyprus has prepared, with the European Commission, Directorate General for Employment and Social Affairs, a Joint Assessment of Cyprus' employment and labour market policy priorities. This document presents an agreed set of employment and labour market objectives necessary to make progress in adapting the employment system so as to be better able to implement the European Employment Strategy and to prepare the country for accession to the European Union. Progress in the implementation of these policies will be assessed regularly.

**7 December 2001**

*(Signed)*

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*(Signed)*

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## **Introduction**

In accordance with the provisions of the Accession Partnership the Commission is carrying out employment policy review in the candidate countries. The objective of these reviews is to examine, in collaboration with the appropriate authorities in each country, the extent to which candidate countries have made progress in adapting their employment systems so as to be able to implement the European Employment Strategy.

The reviews aim to provide information, for the use of the candidate country and the Commission, on the following questions:

- Are the labour market structures that are already in place appropriate to participation in the Single market?
- Are labour market and employment policy institutions sufficiently developed to allow an early implementation of the employment strategy in line with the Employment Title of the Treaty?
- Is the overall employment system in the respective candidate country moving towards a meaningful participation in the EU employment co-ordination process?
- What are the priorities for human resources development strategy as a background for preparatory work for ESF or ESF type action planning and programming?

The starting point in the Employment Policy Reviews is to agree on a Joint Assessment Paper, whose focus is on the fundamental challenges in the field of employment. These challenges consist first of recognition that labour markets need to reflect the needs of a dynamic market economy as part of a single market, which implies that labour needs to be mobile, adaptable and skilled. Second, to have relevant policies and appropriate institutions which support the development of a flexible labour market. This includes the need to promote a forward looking approach to industrial restructuring to adapt to knowledge based economies and to face the impacts of demographic change.

The principal tasks of the exercise are summarised under three sections. Section 1 provides a brief description of the economic performance. Section 2 examines the overall labour market situation and the progress made in modernising the labour market. Section 3 identifies major challenges and draws together the overall conclusions from the review.

## **1. Economic background**

### **1.1 Economic developments**

Cyprus has the highest level of economic development among the candidate countries. Economic growth during the 1990s was rapid by comparison with other developed economies, while rates of inflation and unemployment remained relatively low. During 1997 and 1998 there were concerns about widening macroeconomic imbalances. However, in the last two-year period the conditions of macroeconomic stability have improved markedly in most areas, notably regarding the fiscal affairs and the current account of the balance of payments, mainly as a result of policy initiatives. The only exception to this improvement relates to the increase in the rate of inflation in the year 2000, which however is of a temporary nature as it was the result of mainly exogenous and temporary factors. Some of the most important aspects of recent economic performance and policies are outlined below.

Economic growth has been rapid over the last three years with the services sector continuing to be the main engine of growth. In 1999, tourist-related sectors, such as restaurants and hotels increased by around 9.5%, while domestic factors, in particular the massive increase in the volume of equity transactions, contributed to value added in the financial sector increasing by 14.5%. Other services activities continued to expand strongly in 1999 including telecommunications and transport, international financial and shipping services and information technology services. In contrast, the primary and manufacturing sectors contributed little to growth in recent years. Although the economy is very dependent upon tourist revenues and while traditional sources of export earnings – particularly from the manufacturing and agricultural sectors – have suffered from long-term decline, export earnings from non-tourism and new manufactured products are expanding and reducing the susceptibility of the economy to external shocks.

Rapid economic growth in Cyprus has in most years been accompanied by conditions of macroeconomic stability. In 1997 and 1998 there was a widening of macroeconomic imbalances as fiscal policies became more expansionary. The fiscal position deteriorated between 1996 and 1998 when the central government deficit rose from 3.4 per cent to 5.5 percent of GDP, partly as a result of delays in taking measures to boost tax revenues, including the raising of the standard VAT rate.

Against this background the Government in 1999 prepared a fiscal consolidation programme for the period 1999 to 2002 aimed at reducing the fiscal deficit to less than 3% of GDP by 2002. In line with the implementation of this programme the government during 1999 and in the first half of 2000 took fiscal measures which helped to lower the deficit to 4.0% of GDP in 1999, and to 2.7% of GDP in 2000. Excise taxes on tobacco products, petroleum and alcohol products were raised in 1999, a tax on the volume of equity transactions was introduced as from the beginning of 2000, and the standard VAT rate was increased to 10 per cent from July 2000. In addition, government current expenditures were restrained, with the rate of growth of government employment being reduced considerably. Taken together, the fiscal consolidation measures, improved tax administration and stronger economic activity have placed the fiscal deficit on a distinct downward path.

Until recently, if the cost of oil imports in terms of Cyprus pounds rose above a certain level, the government subsidised a large part of the higher costs to the oil companies rather than passing on the increased costs in higher prices to the consumer. Indeed, the House of Representatives had been very reluctant to sanction proposed increases in domestic prices of oil products. Thus, with considerable rises in the prices of imported oil in the first half of 2000 subsidies to oil companies increased. However, from July 2000 a new pricing mechanism was introduced whereby changes in import costs above a certain level are automatically passed on into changes in domestic prices of oil products without the prior approval of the House of Representatives. With the adoption of the new pricing mechanism domestic fuel prices were raised immediately, and again in September and October 2000.

Cyprus has traditionally enjoyed a low rate of inflation, averaging 1.7% in 1999. However, under the influence of higher electricity prices, the depreciation of Euro-linked Cyprus pound, and higher local agricultural prices arising from adverse weather conditions, the rate of inflation rose to 4.1% in 2000. The underlying rate of inflation, which reflects the fundamentals of the economy, was in fact estimated to be much lower. Excluding the impact of the recent increases in taxes and in the price of oil, the rate of inflation is estimated to have been 2.2%.

The current account deficit narrowed significantly to around 2.5% of GDP in 1999 compared with nearly 7% in 1998. This improvement was mainly accounted for by a considerable increase in tourist arrivals and a reduction in one-off defence - related expenditures. In 2000 the current account deficit is estimated to have been 5.2% of GDP, largely as a result of a significant rise in oil import costs (as compared with 1999, the fuel import bill rose by CYP 136.7 million or the equivalent of 2.5% of GDP). Higher imports were to a large extent offset by a substantial increase in foreign exchange receipts from tourism and other services exports as well as from a strong revival in exports of manufactured goods. Indeed, as a result of improved external competitiveness it is estimated that real exports rose by around 9% in 2000.

Recently, Cyprus has introduced a number of measures that will further liberalise financial markets. After several years of delay, the House of Representatives passed legislation removing the nine-percent per annum interest rate ceiling, which came into effect as from January 2001. The liberalisation has taken place smoothly and without any undue difficulties. Restrictions on inward foreign direct and portfolio investments (except for banks) by residents of the EU were abolished, as from January 2000; restrictions on direct investment abroad by residents of Cyprus were also abolished as from this date. However, in this case, when the foreign exchange involved is substantial, the Central Bank of Cyprus reserves the right to take measures in order to mitigate the impact on the balance of payments. Moreover, there was a partial liberalisation of portfolio investments by residents of third countries as from August 2000. From January 2001, simultaneously with the liberalisation of interest rates, there was a liberalisation of medium-term and long-term borrowing in foreign currencies by residents, from banks in Cyprus or from abroad. However, a number of important capital restrictions remain. Residents may not purchase stocks or bonds overseas, or place deposits in foreign banks.

The interest rate ceiling and the limited availability of indirect market based monetary policy instruments have constrained the capacity of the Central Bank to conduct tight

monetary policies. Higher interest rates during 1999 might have mitigated the effects of excess demand and cost pressures in the economy. Efforts by the Central Bank to limit monetary growth have been mixed. In an attempt to restrain domestic credit expansion, the Central Bank introduced a 12 percent ceiling on the growth of bank credit. Nonetheless, credit growth during 2000 was excessive. In May, the central bank responded to the excessive credit growth by introducing monthly credit ceilings for the period June-December 2000 and increasing the minimum reserve requirements by 1 percentage point as from July 2000.

Although agriculture still makes a significant contribution to GDP, its importance has declined both in terms of GDP and employment, and there is a need for extensive structural reform. The sector is heavily concentrated in irrigation-dependent products, such as citrus fruits and vegetables. Agricultural production consumes around three-quarters of the total water supply. Moreover, the sector enjoys high levels of tariff protection and significant water-related subsidies.

In summary, Cyprus has reached a relatively high level of development, and growth has remained strong. However, there is a need to sustain and intensify the reforms that contributed to the diversification of the export-oriented services sector of the economy and strengthen the policies that have helped to reduce and reverse the macroeconomic imbalances that had emerged in 1997 and 1998.

## **1.2 Policy challenges arising from EU accession course and from globalisation**

### **Background**

EU accession, together with the ongoing process of globalisation, presents both challenges and opportunities for Cyprus.

The first serious challenge arises from the harmonisation effort itself and it constitutes the adaptation of the legal and institutional framework and policies with the full volume of the *acquis communautaire* in a relatively short period of time. A second challenge arises from the creation of conditions of intensified competition brought about by the changing external environment of Cyprus in general, and more specifically by accession. This challenge creates risks for those sectors of economic activity that may not be able to adjust to intensified competition, and the impact on the Cyprus economy will depend on the degree and speed of adjustment. At the same time EU accession, together with the globalisation of the world economy and the further liberalisation of international trade, will give unhindered access for Cypriot goods and services to the large single market of the EU and the easier access to third markets. This will provide new opportunities for growth.

### **Government policy - Accession strategy**

Responding to these challenges has required the development of a strategy for harmonisation and for adapting to intensified competition. This response is set out in the latest Strategic Development Plan, covering the period 1999-2003.

The accession strategy is based on two pillars:

- Legal and institutional adjustment for the adoption and effective implementation of the *acquis communautaire*,
- The restructuring and the further diversification of the economy in line with the comparative advantages of the island.

As regards the **first pillar** of the accession strategy the Government has adopted a gradual harmonisation approach, in order to spread fiscal and other harmonisation costs over a longer period, and to achieve a gradual adjustment to conditions of intensified competition. This gradual approach also reflects the fact that parts of the harmonisation process require a sequence of measures which take, on purely technical grounds, considerable time.

More specifically, based on the above approach and the divergences identified during the *acquis* screening phase, comprehensive sectoral harmonisation programmes, setting priorities, have been prepared for the legislative and institutional adjustment needed. Harmonisation will have been largely completed before 1 January 2003, with a few exceptions, for which special arrangements have been sought. The measures planned to be taken are included in the National Programme for the Adoption of the Acquis (NPAA) prepared by Cyprus and submitted to the EU.

Structural changes dictated by the adoption and effective implementation of the *acquis* have either taken place or are under way. The aim is both to facilitate a smooth transition towards the *acquis* and at the same time maximise the welfare gains from membership. In summary, the remaining market rigidities that have to be set aside in the coming few years are limited. They concern mainly the financial sector (restrictions on capital movements) and hindrances to market access in the utilities sectors (electricity, telecommunications, postal services and air transport). The abolition of the remaining rigidities is expected to have a positive impact on efficiency through a better allocation of resources.

Concerning the **second pillar** of the accession strategy, the Government is implementing schemes for the restructuring of the private sector in specific branches of economic activity. These schemes take account of the comparative advantages of Cyprus and aim at the modernisation of productive units and the improvement of their competitive position. They include several schemes for the restructuring of the agricultural sector as well as a new industrial policy to enhance the competitiveness of the manufacturing sector. In addition, the Government is implementing an action plan aimed at enhancing the export orientation of private sector non-tourism services, mainly through the encouragement of co-operation between Cypriot and foreign enterprises, including the formation of strategic alliances.

Particular attention is being paid to the promotion of entrepreneurship, with a focus on the encouragement of small and medium-sized enterprises (SMEs). Among the main planned measures are:

- a dedicated centre within the Cyprus Development Bank to provide integrated solutions, including tailored loans, equity and quasi-equity instruments and services to SMEs
- simplification of the business environment within which SMEs operate (e.g. through a "single registration" process; exemption of smaller firms from VAT registration)

- creation of business incubators to help new inventors to develop innovative ideas through to the setting up of new productive enterprises.
- the introduction of a Government guarantee for loans granted to SMEs together with subsidisation of the interest rate on Government guaranteed loans, to encourage the financing of SMEs under speedy procedures and favourable terms
- setting up a "one-stop shop" providing detailed information to investors concerning the prevailing national administrative procedures; initially targeted at foreign investors, its remit will be extended to include domestic enterprises.

At the macroeconomic level, the primary objective of medium-term economic policy is the achievement of a satisfactory rate of growth while preserving conditions of internal and external macroeconomic stability. Within this framework, the Government has responded to the fiscal imbalances that had been observed in the last few years, with the formulation and implementation as from mid-1999 of a fiscal consolidation programme.

### **1.3 Medium-term prospects of the Cyprus economy – Labour market implications**

Recent trends in the Cyprus economy are encouraging. The maintenance of relative external and internal macroeconomic stability provides a solid basis for the economy to face current and forthcoming challenges. The Cyprus economy exhibits, from a medium-term perspective, a very satisfactory rate of growth, with the services sector being the main driving force and conditions of virtual full employment prevailing. Foreign debt is at low and manageable levels, while the pegging of the Cyprus pound to the Euro did not lead to balance of payments disequilibria. Indeed, exchange rate developments over the last two years have contributed to a substantial improvement in external competitiveness. As noted earlier, the upward trend of the fiscal deficit was decisively reversed in 1999 and it decreased further in 2000. To build on these developments the fiscal consolidation programme has recently been revised and extended beyond 2003 to 2004, with a view to making it more specific and ambitious. The rate of inflation increased in 2000, but this was largely due to temporary factors, and from 2001 onwards it is expected to return towards its previous low levels.

The improved business climate and efforts to develop a broader and deeper capital market were highlighted in 1999 by a very large flow of funds into the Cyprus Stock Exchange. This development, characterised by the public listing of many business enterprises and numerous new capital issues, has provided considerable opportunities for the redistribution of financial resources towards funding new capital formation, particularly for enterprises wishing to restructure and modernise their activities. The large increase in imports of capital goods in 2000 suggests that a considerable part of the funds flowing into the Stock Exchange are being used to acquire physical productive assets.

Most of the structural changes required by the adoption and effective implementation of the *acquis* and/or by the globalisation of the world economy have already taken place. The remaining rigidities are limited, and in the medium and long-term overall efficiency gains can be expected from their abolition. In particular, the trade liberalisation process has generally been completed, and thus exposure to the conditions of intensified competition is already being experienced in the sectors of manufacturing and agriculture. In the services sector, Cyprus possesses comparative advantages and it envisages, as a member of the EU,

the upgrading and consolidation of its role as an international and regional services centre and its transformation into a gateway for Europe to the Middle East and North Africa regions.

The authorities estimate Cyprus' medium-term sustainable growth rate potential at 4.5%, in line with the estimates made by the IMF during its consultations with Cyprus in the year 2000. The estimate is based on the assumption of an annual increase of the labour force from indigenous sources by 1% (see section 2.4), in conjunction with an annual improvement in labour productivity of 3.5%, in line with recent medium-term trends. Success in increasing the participation rate of women, or in accelerating productivity growth through increased investment resulting from the liberalisation process, would further increase the potential rate of economic growth.

The services sector is projected to continue to be the main driving force behind rapid growth. Furthermore, within this sector there is expected to be continuing restructuring and diversification, with an increased shift towards export-oriented private services such as communications, finance, education and business services, benefiting from improved competitiveness and the comparative advantages of Cyprus. The favourable medium-term growth outlook should thus be reflected in an increase in additional employment opportunities, mainly in the tertiary sector of services, and the maintenance of conditions of full employment as well as a further rise in living standards.

These changes, and in particular the expected increased importance of economic sectors with a relatively higher human capital intensity, should lead to more efficient utilisation of the human capital endowment of Cyprus and an amelioration of qualitative imbalances observed in the labour market.

## **2. The situation on the labour market**

### **2.1 Introductory note on data sources**

The sources for data on employment are twofold. First is the Employment Survey, an establishment survey conducted by telephone on a quarterly basis by the Statistical Service. The second is a Labour Force Survey (LFS) based on households, which is carried out by the Statistical Service in the second quarter of the year and is fully harmonised with the relevant EU acquis. The first labour force survey was launched in 1999 as a pilot survey.

For unemployment data the only source until 1999 was administrative i.e. the Government District Labour Offices. Since 2000, however, the Labour Force Survey has been added and constitutes an important source for the level of unemployment.

For statistics on earnings the main source is the Wages and Salaries Survey, conducted by the Statistical Service, which is an annual enquiry conducted through personal visits to the enterprises.

### **2.2 Developments in employment**

Employment in Cyprus was on a generally upward trend through the 1990s, growing at an annual average rate of 1.5% between 1990 and 1999 to reach a level of 291,000 in the latter year. The rate of increase in employment varied across individual years, reaching as high as 4.5% in 1992, whereas small declines were registered in 1993 and 1997. There was a tendency for employment growth to slow down as the decade progressed; annual average growth was 1.9% between 1990 and 1994, but only 1.3% between 1994 and 1999.

Rapid productivity gains were made over this period – GDP per person employed rose by over 20% between 1990 and 1999.

The employment rate<sup>1</sup> remained relatively stable over the 1990s in the range of 66-68%. According to the Labour Force Survey in the year 2000, it stood at just under 66%, as compared with a rate of 63.9% in the EU overall. The male rate in 2000 is estimated at about 78% and the female rate at 53%. The female rate was slightly below, and the male rate significantly above the respective rates for the EU in 2000. The gap between male and female employment rates has become narrower during the last two decades, with the male rate declining and the female rate rising.

### **2.3 Structural shifts in employment**

#### *Sectoral trends*

All of the increase in employment in recent years has been in the services sector, where the number of jobs grew by 53,700 (37%) between 1990 and 1999. Some 55% of the increased number of people employed in services during this period were women. By contrast over this same period, agricultural employment fell by 7,200 (corresponding to a fall of 21%), while employment in the secondary sector fell by 8,900 (representing a decline of almost 12%). The slow-down in aggregate employment growth in the second half of this period is reflected at the sectoral level as well – with the pace of decline in

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<sup>1</sup> Measured here as total employment (all ages) as a proportion of the population aged 15-64.

industrial<sup>2</sup> employment being faster, and the services sector's growth in employment being slower, over the years 1994–1999 as compared to 1990-94 period.

Within the services sector, the most rapid growth in employment over 1990-98 was in finance and business services, with an increase of over 64% (women's employment growth was 77%), albeit from a small base. Employment in community, social and personal services also grew rapidly – by over 40% - and, with an absolute increase of almost 21,100 jobs<sup>3</sup>, was the single largest contributor to overall employment growth. Employment in trade, transport and communications rose by more than 30%, and the slowest-growing part of the services sector was the hotels/restaurants industry, with an increase of just 26%. Within the industrial sector, manufacturing industries had a net employment decline of 21%, while construction employment in 1999 was merely 4.3% up on its 1990 level: job-gains in construction were, however, concentrated in the first half of the decade and employment fell slightly between 1995 and 1999.

Women's employment over the period 1990-1999 remained highly concentrated in a few sectors, namely the sector of trade, hotels and restaurants, the sector of community and personal services and manufacturing. Women's employment in these sectors exhibited, over that period, an increase of 32%, 63% and a fall of 38% respectively.

The sectoral structure of employment differs somewhat from that in the EU. The share of employment in agriculture in 2000 was 5.4%,<sup>4</sup> somewhat higher than in the EU, while the industrial sector's share is 24.1%, which is below the EU average. The services sector employment share is higher in Cyprus, exceeding 70% according to the 2000 LFS compared to 66% in the EU. Its composition is rather different; employment in hotels and restaurants (10% of total employment) and the trade and transport share at 24% are higher than in the EU, while employment in financial, business and community services with a share of 37% is relatively lower than in the EU.

As regards the sectoral structure of women's employment, 55% of the employed women were concentrated in 6 out of the 60 NACE 2 – digit sectors<sup>5</sup> – i.e. retail trade, hotels and restaurants, education, public administration, business activities and health and social work – as compared to 60% in the EU.

### *Occupational trends*

Change in the occupational structure reflects changes in the structure of production, i.e. the increasing and dominant role of the services sector, as well as the tendency of Cypriots to acquire high educational qualifications. These changes have been accompanied by a rise in the share of professionals, clerks, and service and sales workers to the total gainfully employed population. Between the Population Census of 1992 and the LFS of 2000 employment increased by 10%. The category of managerial, professional and technicians expanded by 16%, clerks by 18% and the number of services and sales workers grew by 26%. Manual jobs on the other hand shrank by 3%, largely due to the severe contraction in the clothing and footwear industry in the last 5 years.

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<sup>2</sup> The industrial sector comprises mining and quarrying, manufacturing, electricity, gas and water and construction.

<sup>3</sup> Of these, almost 6,000 were foreign housemaids/ home helpers.

<sup>4</sup> Source: Labour Force Survey, 2000

<sup>5</sup> NACE is the EU system of classification of economic activities

Over the same period women's employment rose by 16% with employment in clerical jobs exhibiting a sharp increase of 37%, managerial, professional and technical employment rising by 25%, service and sales occupations expanding by 32% while manual jobs dropped by 9%. The share of women in the managerial positions is still low and amounted to 14.4% in 2000, although it has risen somewhat from 9.5% in 1992.

#### *Labour mobility*

Recent evidence on the extent of labour mobility is limited. However, according to a study<sup>6</sup> undertaken for the period 1979-1985, the overall turnover rate between occupations over the six-year period covered by the study was found to be 16%. The largest movements occurred between occupations with closely related skill profiles and low retraining costs. Upward mobility and consequent change in occupation typically occurred within the same enterprise. Labour mobility between sectors, for the period under consideration, was lower than between occupations, amounting to 9% of the total number of persons in the sample. Concerning geographical mobility, there is no available data. However, there is in general an unwillingness for job seekers to take up employment in a region different from their residence, particularly for lower paid occupations.

#### *Employment in the public sector*

The proportion of the broader public sector (which includes the Central Government, the local authorities and the Semi-Government Organisations) in total employment has increased somewhat, from 16.2% of total employment in 1990 to 17.1% in 1999.<sup>7</sup> This increase reflects the rapid growth of employment mainly in public health and public education.

#### *Self-employment/dependent employment*

The results of the 2000 LFS show that of those employed, 76% were employees, 21% were self-employed and 3% unpaid family workers. More than half (53%) of those engaged in agriculture, 23% of those engaged in industry, and 19% of those in the services sector are self-employed. At a more detailed sectoral level, the prevalence of self-employment was greatest in personal services (34%), wholesale and retail trade (28%) and hotels, restaurants and transport, at about 17%. Even in these sectors, the importance of self-employment has declined substantially between the 1980s and 1990s. Nonetheless, self-employment – particularly in industry and services – remains relatively important as compared with the typical situation in EU member states.

#### *Regional trends*

Nicosia and Limassol, the two most populous districts, together accounted for almost 67% of all employment in 2000, according to the LFS data. A comparison of the distribution of employment with that of the population shows that the employment rate was considerably higher in the main tourist resorts – 90% for Ammochostos and 76% for Pafos – while other districts had a significantly lower employment rate – Nicosia 66%, Larnaca 62% and Limassol only 59%. The urban and rural employment rate is almost the same, 66.0% for the former and 65.3% for the latter. Males in urban areas have a slightly lower employment rate, 77.6% compared to 79.3% for males in rural

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<sup>6</sup> William J. House: *Mobility in the Labour Market in Cyprus*, 1988

<sup>7</sup> Source: Labour Statistics 1999

areas. The differential in employment rate, however, is somewhat larger for females in urban areas at 54.7% while rural women have a much lower rate, 50.2%.

#### *Foreign workers*

The number of foreign workers in Cyprus has been growing steadily during the last decade. In 1995<sup>8</sup> they amounted to 15,000 or 5.3% of the employed population and by 2000 their number topped 25,000 or 8.5% of the workforce.<sup>9</sup> More than a quarter of them are employed by private households as domestic servants, 17% are employed in hotels and restaurants, 14% in wholesale and retail trade, 10% in manufacturing, 8% in agriculture and 7% in construction.

#### **2.4 Labour force**

There were 314,400 persons in the labour force in 1999 an increase of 38,400 or almost 14% over the 1990 level. This increase resulted from positive demographic trends, in conjunction with a substantial increase in foreign labour, partially offset by a slight decline in labour force participation.

The working-age population (15-64) rose from 372,000 in 1990 to 436,600 in 1999 – a rise of some 17%. The increase has been sharpest in the age groups 40-54 (up by almost 30%) and 55-64 (up by more than 24%); the population aged 15-39 grew more slowly, by approximately 10%.

In the last decade, labour force participation has been falling. Overall participation for those aged 15-64 fell from 71.2% in 1989<sup>10</sup> to 69% by 2000.<sup>11</sup> There was an increase in female participation – from 55% in 1989 to 58% in 2000 – but male participation fell from 88% to 81%. Overall participation in the year 2000 was similar to the EU average of 69%; the male rate was above the EU level of 78%, while female participation was slightly lower than the corresponding EU rate of 60%.

#### *Educational levels*

The level of education of the workforce has been rising in recent years. The proportion of workers with tertiary education rose from just under 18% in 1989<sup>12</sup> to more than 28% in 2000,<sup>13</sup> which is higher than the EU average of 25%. (Education levels are higher among younger workers – of those gainfully employed at the age of 29, 33.1% are tertiary education level graduates.) Over the same period, the proportion of workers with only primary education fell sharply from 40% to 24%.

In the overall adult population, relatively fewer women have a university degree (9% as opposed to 14% of men). Also, whether a woman is employed or economically inactive depends to a significant extent on her educational qualifications. Only 26% of women with primary and lower secondary education are gainfully employed, but this proportion rises to 54% for women with upper secondary education and 79% for women with tertiary level education.

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<sup>8</sup> Source : Social Insurance Department

<sup>9</sup> In the EU overall, 5% of workers are non-nationals. Apart from Luxembourg, only Austria (10%) Germany (9%) and Belgium (8%) have concentrations of foreign workers comparable to that in Cyprus.

<sup>10</sup> Source: Health Survey 1989

<sup>11</sup> “ : Labour Force Survey 2000

<sup>12</sup> “ : Health Survey 1989

<sup>13</sup> “ : Labour Force Survey 2000

Looking to the future, the medium-term growth of the labour force will be determined by underlying demographic trends and by expected developments in labour force participation. The demographic outlook in the period up to 2005 is relatively positive compared with that in the EU. Even on the assumption of zero net migration, the “natural increase” in the population of working age (and of the labour force, with unchanged participation rates) will be of the order of 1% per annum over the next five years.<sup>14</sup> Several factors could lead to even faster indigenous labour force growth:

- a potential increase in participation rates, especially for women,
- a containment of the brain drain<sup>15</sup>
- an increase in the retirement age, which has recently become a topic for discussion.

From 2005 onwards, labour force growth is projected to decelerate gradually, in view of the past fall in the fertility rate. While this trend might be offset by an inflow of workers from EU countries after accession, such a development is not currently anticipated by the Cypriot authorities.

## **2.5 Unemployment**

### *Overall trends*

Unemployment, though on a slight upward trend through the 1990s, has remained very low by international standards. Based on registration data, the unemployment rate dipped below 2% in 1992, and rose gradually to 3.6% in 1999, falling marginally to 3.4% in the year 2000. The rate of unemployment according to the Labour Force Survey of 2000, based on internationally comparable ILO definitions, was 4.8%.

### *Structural features*

Unemployment, according to the LFS of 2000, is higher among women (7.4% in 2000) than among men (3.0%). The gender difference is most marked among young people aged 15-24 years (female unemployment of 14% as against 4% for males) and those aged 35-44 (females 9%, males 2%).

While youth unemployment is higher than adult unemployment, the age-unemployment gap is relatively low by international standards. Youth unemployment – particularly among teenagers – therefore remains well below the EU average. The unemployment rate for those below 25 years was 8.1% in 2000, as compared with the EU average of 16.1%.

Most unemployment remains of relatively short duration – in 2000, approximately 30% of the unemployed had been out of work for more than a year as compared with 44% in the EU. The long-term unemployment *rate* – i.e. the number of long-term unemployed as a proportion of the overall labour force) is also relatively low, at 1.4%. Duration of unemployment is longer for women (36% being out of work for more than a year) than for men (21%), and the female long-term unemployment rate, at 2.7%, is almost four times that for men.

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<sup>14</sup> Based on population projections made by the Statistical Service.

<sup>15</sup> See Section 3.2 below.

It is noted that those with the highest levels of education are under-represented among the unemployed – with those with tertiary education accounting for only 16% of the unemployed as compared with their share of 28% in the employed workforce.

Regional variations in unemployment also appear small. The highest unemployment rate according to the 2000 LFS was observed in Limassol (7.2%) and Larnaca (5.3%) districts, followed by Nicosia (4.4%) and the lowest rates were recorded in the main tourist resort districts of Ammochostos (2.9%) and Paphos (1.9%)

## **2.6 Imbalances in the labour market**

Notwithstanding the fact that the labour market of Cyprus continues to exhibit conditions of full employment and high rates of employment participation, there are quantitative and qualitative imbalances at the sectoral and occupational level.

At the sectoral level, the most profound imbalances, in relative terms, are in the sectors of hotels and restaurants, construction, agriculture and manufacturing. The imbalances in these sectors have been ameliorated to a great extent through the temporary employment of foreign labour. As mentioned above, foreign labour constitutes about 8.5% of the employed workforce; however, this proportion varies widely across sectors. In 1999, 13.4% of the gainfully employed population in the sector of hotels and restaurants, 6.8% in the construction sector, 7.3% in the sector of agriculture, and 6.0% in the manufacturing sector were foreign workers. In some sectors, the presence of foreign workers co-exists with above-average domestic unemployment rates – in early 2000, for example, the sectoral unemployment rates for manufacturing and construction were 6.8% and 5.4% respectively.

At the occupational level the main imbalances between the demand for labour and the supply from indigenous sources are in the following broad categories (based on the situation in early 2001):<sup>16</sup>

- Elementary occupations, where in February 2001 foreign labour accounted for 46% of all employment. (One third of these foreign workers are domestic servants in private households.) At the same time, unemployment in these occupations was running at 6.5%.
- Service workers and shop and market sales workers, where foreign labour represented 7.9% of the employed population. The majority of foreign workers in this broad category is concentrated in the sub- category of service workers representing 12% of the employed population in this category, whereas in the sub-category of shop and market sales workers foreign labour represents only 2.1%.
- Craft and related workers, among whom the unemployment rate was 4.6% while the number of vacancies amounted to 1.3% of the employed population.
- Technicians and associate professionals, where foreign labour accounted for 6.6% of the gainfully employed population.

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<sup>16</sup> The source for the data on foreign workers by occupation is the Cyprus Police. These data should be treated with some caution. However, preliminary data from the LFS for 2000 support the broad conclusion that dependence on foreign workers is greatest in the elementary occupations, in services and sales work, and in managerial/professional jobs

In addition, imbalances have emerged in Information and Communication Technologies (ICT)-related occupations. The transition towards a knowledge based economy and the diffusion of ICTs have generated employment opportunities for computer systems designers and analysts as well as computer programmers, resulting in skill shortages that have mainly been offset through the temporary employment of foreign labour. Foreigners represented, in the year 2000, 40% of the gainfully employed population in these occupations, the vast majority being employed in international business companies producing products and providing services for the international market. Companies operating in this sector are allowed to employ their own overseas managerial /professional staff. The presence of a large number of foreign workers in this category, therefore, is not due to internal market imbalances.

## **2.7 Wage developments**

Average monthly real wages rose by 36% between 1990 and 1999, and were higher than the increase in economy-wide productivity. The increase was fastest in the early part of the decade – real wages rose at an average annual rate of 3.8% up to 1994, and 3.2% between 1994 and 1999. Women's wages rose relatively faster than men's during the 1990s, so that there was some gender-convergence; average female monthly earnings were 60% of male earnings in 1990 and 73% in 1999.

There has been relatively little recent change in the dispersion of wages by occupation, at least at the extremes of the earnings distribution. In 1999, legislators and managers were the highest-paid group, with earnings just under 2.5 times the average for all workers, while the lowest-paid – those in elementary occupations – received just under 70% of the average; in each case, relative earnings were almost unchanged between 1992 and 1999. There was, however, some movement in the earnings of intermediate occupational groups, with declines in the relative earnings of technicians and of services and workers.

These differences in earnings by occupation can be partly explained by differences in educational attainment. The most recent available data, for 1996/97, suggest that employees with university education have earnings approximately four times greater than those of workers with only primary education. Workers with completed secondary education earn approximately twice as much as the lowest-educated.

The male-female earnings gap is partly explained by the different occupational and educational characteristics of male and female workers. However, gender differences in earnings remain even within occupation and education groups. Indeed, the excess of male over female earnings tends to rise as the level of education increases; this appears to reflect more limited female access to higher occupations, despite the fact that a higher percentage of employed women than employed men have tertiary education qualifications.

## **2.8 Labour market policies and institutions**

The main responsibility for the formulation and implementation of employment policy lies with the Ministry of Labour and Social Insurance, and in particular the Department of Labour within the ministry.

The overall objective of employment and labour market policies in Cyprus is the maintenance of conditions of full employment, through policy responses that will lead to high and sustainable growth in employment and increased flexibility in the labour market. In the latest Strategic Development Plan, covering the period 1999-2003, the quantitative targets set out provide for an annual increase of employment of 1.2% whilst keeping the unemployment rate at 3%. Furthermore, a main related objective of the Strategic Development Plan is to increase the level of productivity through, inter alia, the technological upgrading of business units, the adoption of new methods of management and organisation of work, the upgrading of the educational and training systems and the promotion of lifelong learning.

In its analytical approach to policy development, the Ministry has already adopted the four-pillar structure of the European Employment Guidelines, and work has commenced on the preparation of a National Employment Action Plan in line with those now produced annually by the member states.

The two main labour-market institutions are the **Public Employment Service (PES)**, which operates under the Department of Labour, within the Ministry of Labour and Social Insurance, and the **Human Resource Development Authority (HRDA)**, a semi-government organisation established by statute, with the Minister of Labour and Social Insurance being the competent minister.

The **PES** operates both at central level and local level. There are four District Labour Offices (with the number of office staff ranging from 5 to 15) and one local branch with 3 staff. The main functions and responsibilities of the PES are:

- To assist and advise on the identification and assessment of labour market problems, through: collecting and dissemination of data on unemployment and job opportunities; studies and research on specific employment problems; analysis of the employment implications of development policies and evaluation of the impact of employment policies and measures
- To assist and participate in the development / evaluation of employment policy
- To co-operate and collaborate with other public and private bodies with a view to achieving the best possible distribution, effective use and mobilisation of human resources.
- To contribute to the smooth operation of the labour market by:
  - i) assisting job-seekers to find suitable employment and helping employers to find suitable workers through the registration and placement services
  - ii) facilitating occupational and geographical mobility through the provision of relevant information to job-seekers and employers
  - iii) initiating and operating programmes/schemes for categories of the labour force facing special problems
  - iv) providing vocational guidance and counselling on employment and training opportunities

The placement service is institutionally separated from the benefit administration but both services are co-located at local office level. Matching of vacancies to job seekers is made on a closed basis by the use of a computerised system. The PES encourages employers to report when vacancies have been filled and also re-contacts employers to find out whether their vacancy still exists and if not, whether the employer will agree to

changes that will facilitate a satisfactory match. During 1999, 12,121 vacancies were registered by the PES while PES placements totalled 3,534 resulting in an overall ratio of 29%. The placements to vacancies ratio varied across branches of economic activity, with agriculture having a ratio of 56%, (construction 45%, manufacturing 16%, trade, hotels and restaurants 14%, banking 22%, and services 60%). The PES also has frequent contact (once a month) with the unemployed in order to update the records of the unemployment register.

Passive financial support for unemployed individuals is provided through unemployment benefit and, under certain conditions, public social assistance. (The Public Assistance and Services Law guarantees a minimum standard of living to every person legally resident in Cyprus.)

An unemployed person is entitled to unemployment benefit, if s/he has an adequate record of insurable employment for which social contributions have been paid, and is capable of and available for work or is following a course of occupational training. Eligible unemployed individuals may start receiving the benefit after 3 days of unemployment. An unemployed person who was employed by a Cypriot employer abroad may start receiving the benefit after 30 days of unemployment. The duration of the benefit is 156 working days in the same period of interruption of employment. Initial registration for placement is a precondition for benefit entitlement and confirmation of unemployment status is required for continuation of benefit payment. This confirmation of continued unemployment takes place monthly through personal contact by the unemployed with the PES.

Unemployment benefit includes a basic benefit and a supplementary benefit. The weekly basic benefit is equal to 60% of the average of weekly insurable earnings in the year prior to unemployment and increases to 80% for entitled persons with one dependent, to 90% for two dependants, and to 100% for three or more dependants. The supplementary benefit is 50% of the insurable earnings in excess of the basic earnings, up to a maximum of two times the insurable earnings. Thus the level of the actual unemployment benefit depends on the level of earnings prior to unemployment and the number of dependants. On average, the unemployment benefit amounted to 68.5% of the gross earnings prior to unemployment for a skilled industrial worker with three dependants. Relative to *net* earnings in employment after taxes and social contributions, the replacement rate for such a worker is about 78%. In Q2 2000 64.4% of the LFS unemployed were receiving unemployment benefit.

It is not possible for an unemployed person to receive unemployment benefit after the entitlement period (i.e. after 156 days) unless s/he starts working again and completes at least 26 weeks in employment during which contributions to the Social Insurance Fund are paid.

Long-term unemployed persons, i.e. persons unemployed longer than 156 working days, are entitled to public assistance allowance provided that they are not voluntarily unemployed and their income is not sufficient for their basic and special needs as determined by the Public Assistance and Services Law. However, the number receiving this allowance for reasons of unemployment is very small, equivalent to just over 1% of the LFS unemployed in the year 2000.

The **HRDA** was established in 1974. It is governed by a 13-member tripartite Board of Directors that includes government, employer and trade union representatives. The Authority refers to the Government through the Minister of Labour and Social Insurance who is, by law, the competent Minister. A levy, currently set at 0.5% of the payroll of all private enterprises and semi-government organisations is channelled to the fund from which HRDA finances its activities.

The HRDA's mission is to create the necessary conditions for the planned and systematic training and development of Cyprus's human resources, at all levels and in all sectors,<sup>17</sup> to meet overall national socio-economic goals. The HRDA has the authority to co-ordinate and cater for the provision of training on a nation-wide scale.

HRDA's activities encompass five major areas: -

- The formulation of an integrated training and human resource development policy on the basis of which appropriate training activities are promoted and training costs are distributed.
- The continuous assessment (through research and data collection) of the economy's needs as a basis for training policy formulation.
- The modernisation of the training system with the creation of the necessary infrastructure, the systemisation and certification of training and the introduction of standards of vocational qualifications.
- Provision of information, vocational guidance, and advisory services to enterprises and individuals so as to raise awareness of the need for continuing training.
- The promotion of actions to bring the HRDA's training activities into line with European systems and practices.

The HRDA ensures that approved and subsidised training is organised and implemented according to specifications and that it responds to the priorities of the economy, which are set in the form of guidelines by the HRDA in co-operation with the Planning Bureau. The HRDA's training activities are divided in two parts, initial training and continuing training (discussed further in Section 3). In addition, the HRDA provides consultancy services to firms to help them increase productivity and improve competitiveness through the development and better utilisation of their human resources. It also operates a scheme aimed at strengthening the training infrastructure of enterprises, institutions and organisations in order to meet training needs in sectors, occupations or areas of priority.<sup>18</sup>

The amended HRDA Law, enacted in November 1999, provides the legal framework for the development of a competence-based structure of standards of vocational qualifications. The Board of Directors of the HRDA has decided to proceed with the development of standards and the assessment and certification mechanisms for five key occupations on a pilot basis till the end of 2001.

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<sup>17</sup> With the exception of the self-employed and civil servants.

<sup>18</sup> The term "training infrastructure" includes technical equipment (machinery, tools, instruments, audio-visual facilities and aids, furniture and fittings), specifications and contents of training programmes, training of trainers and persons responsible for training.

### **3. Identifying Challenges in the Labour Market**

#### **3.1 Strategic issues**

The labour market policies in Cyprus should be seen in the context of the overall challenges facing the economy of Cyprus. Cyprus' primary medium-term economic policy objective is the achievement of a satisfactory rate of growth while maintaining macroeconomic stability – i.e. a high level of sustainable economic growth, in order to ensure a continuous improvement in the standard of living and a further enhancement of the real convergence of Cyprus with the EU.

Sound overall macro-policies, together with the programme of broader structural reform described in Section 1, are the main tools being used to pursue these objectives. However, the Government recognises that employment policy also has a role to play, both in supporting wider economic policies and in ensuring that economic and social development go hand-in-hand. The main current and prospective issues facing employment policy are the following:

- Overall labour force participation, even though still higher than the EU average, exhibits a declining trend; female labour force participation, despite a rising trend, remains below the corresponding EU average.
- Even though the rate of unemployment remains relatively low, a number of structural features of unemployment are a matter of concern: a rising share of long-term unemployment in total unemployment; a higher unemployment rate among women than among men; relatively high unemployment among newcomers to the labour market.
- There remain inequalities of opportunity as between women and men in the labour market, as reflected in higher female unemployment (particularly long-term unemployment), in a gender pay gap and an unbalanced representation of women across sectors and occupations.
- Quantitative and qualitative imbalances are reflected in mismatches between demand and supply in a number of occupations and the significant presence of foreign workers in the Cypriot labour market. Internal labour mobility appears low.
- Further restructuring of the economy in favour of the tertiary sector of services is expected, with a corresponding decline in the contribution of the primary and secondary sectors to both GDP and employment; this will have implications for skill requirements and for increased flexibility and adaptability in the workforce to cope with labour market needs.

In these circumstances, the overriding strategic challenge for employment policies will be to prevent the emergence and intensification of labour-market constraints on overall economic growth. While the labour market in Cyprus can be considered to be relatively flexible and well functioning, there is room for improvement, taking into account existing and prospective imbalances between the demand and the supply of labour from indigenous sources, both at the sectoral and occupational level. Effort will need to focus on facilitating the employment of the unemployed, with particular emphasis on the reintegration of the long-term unemployed; increasing the flexibility of the labour market to smooth the movement of workers from declining to expanding sectors; and increasing access to employment for groups with currently low labour-force participation (women, older workers). Policy should also ensure that the young people entering the labour market are adequately prepared.

Addressing these issues has implications for two main elements of labour market policy:

- Policies and programmes in the area of human resources development in the context of a life-long learning approach – initial and continuing education, training and retraining.
- Institutions and programmes that affect the effective functioning of the labour market – mainly the wage formation process, the tax benefit system, the public employment services and active employment policy measures, and policy on foreign workers.

The remainder of this section discusses some of the priority tasks in relation to these elements of employment policy.

## **3.2 Human resources development**

### **3.2.1 Initial education and training**

Investment in initial education has been given high priority since independence in 1960. As a result, the educational attainment of the population has risen consistently. According to the LFS for the year 2000, 80.9% of people at 20 years of age have upper secondary education, and 28.3% of people at the age of 29 have tertiary education. On both of these measures, attainment is above the average level in the EU.

#### ***Initial education***

Formal initial education takes place at three levels:

1. **The basic level** lasts for 9 years and comprises primary education (taking place in the Dimotiko scholio, primary school), of 6 years duration, and the lower secondary level (taking place in the gymnasium), of 3 years duration. Education at this level is compulsory.

2. **The Upper secondary level** lasts for 3 years (for students at the ages from 15 to 18). Education at this level is free in public institutions. The public institutions, at this level, are either of general education orientation or of technical/vocational orientation.

General education in public institutions takes place in the lyceum. At present there are two types of this school, the Lyceum of Optional Subjects (Lykeion Epilogis Mathimatou or LEM) and the Eniaio Lykeio.

The LEM offers pupils a three-year programme with three categories of subjects that are structured in five streams or combinations and include compulsory core subjects, specialisation and supplementary subjects. Pupils select a combination upon registration at Lyceum. Combination I focuses on classical studies; Combination II focuses on mathematics, physics and chemistry; Combination III focuses on economics and mathematics; Combination IV focuses on clerical skills and accounting, and Combination V focuses on foreign languages and social studies. LEM schools are being phased out in the next couple of years, 2001-2002 being the last school year they will operate.

The Eniaio Lykeio is a comprehensive Upper Secondary School and as from the school year 2000-2001 it has been implemented all over the public general education upper

secondary cycle. This type of school aims to meet growing demands for mobility and flexibility. The Eniaio Lykeio offers a programme of subjects that are sub-divided as follows:

- Common core subjects that are obligatory for all pupils. These subjects set the bases of general education, integrating technological literacy alongside traditional subjects, and lead to providing general education, overall development and acquisition of general skills required by modern realities.
- Subjects of specialisation or direction. These subjects are part of a list and are selected by the pupil according to his wishes and interests. The list includes subjects in the areas of humanities and languages, mathematics and science, technology and informatics, business studies and accounting and graphic arts. These subjects are addressing a more systematic and thorough study of sectors that the pupil believes will help him in his future course in society, either for further academic studies or as a pre-vocational background.
- Subjects of special interest and/ or enrichment. These lessons are selected to offer opportunities so that a pupil can work on individual sectors to enrich and satisfy his special inclinations.

The main difference between the LEM and the Eniaio Lykeio lies in the fact that the latter provides the student with the opportunity to formulate his own programme of study by selecting topics that are of interest and useful to him while the LEM offered only a limited number of rigid streams.

Public technical/vocational schools provide the framework for upper secondary vocational education. At present this cycle provides about 17 specialisations in 10 schools, based in the large towns. The technical stream provides a larger share of mathematics and physics, while the vocational stream has a larger share of workshop practice. The former trains for technician and middle level qualifications while the latter aims at training craftsmen.

As from the school year 2001-2002 the technical/ vocational upper secondary cycle is undergoing a major reform. Under this reform the technical schools curriculum will concentrate on a balanced coexistence of general education subjects with technical subjects, giving emphasis to the acquisition of general skills and abilities. It is also being enriched with new topics and areas that reflect new technological trends and the emerging needs of the Cyprus economy. The technical/ vocational schools are to provide programmes that in general can be sub-divided into two major orientations, one of theoretical character and the second of practical character.

According to data provided by the Ministry of Education and Culture, in 1998-99 about 75% of the pupils in upper secondary schools attended public general education schools, 10% attended private secondary schools and the remaining 15% attended public technical schools. Completion rates at second level are relatively high. In the school year 1997-98, 89.6% of the pupils enrolled three years earlier, successfully completed the lower secondary cycle; and about 80% of the pupils that first enrolled at secondary level education six years earlier graduated from the upper secondary cycle from one of the types of schools, mentioned above.

Students in the public secondary and technical schools, and other young persons, can avail of the services of the Counselling and Career Education Service (C.C.E.S.) operated by the Ministry of Education and Culture. The C.C.E.S. assists students in developing personal awareness, making suitable decisions about their education and career; developing the necessary skills for the acquisition of objective educational and occupational information, and dealing with any psychological, personal, family and/or social problems they might be facing. In the school year 2000 – 2001, there were 95 permanent, qualified counsellors in public secondary Schools and at the CCES central office, corresponding to about 600 secondary students per counsellor. Counsellors offer individual and/or group counselling to the majority of the student population of the Public Secondary and Technical Schools. In 1999, 31,287 students (55.3% of the total number of students) were assisted during the year through individual counselling. The service also provides aptitude testing, as well as a number of publications (books, booklets or brochures) to help students with their educational and career choices.

3. The **tertiary level** comprises several institutes of higher education and, since 1992, the University of Cyprus.

There are 8 public tertiary institutions. Of these, 7 offer programmes at the sub-degree level (college) and one offers a post graduate diploma programme in the area of management for university graduates. The institutions are under the auspices of different ministries, such as the Ministry of Labour and Social Insurance (Higher Technical Institute, Higher Hotel Institute, Mediterranean Institute of Management), the Ministry of Agriculture and Natural Resources (Cyprus Forestry College), the Ministry of Health (School of Nursing and the Public Health Inspectors School) and the Ministry of Justice and Public Order (Cyprus Police Academy). The Tourist Guides School functions under the Cyprus Tourism Organisation.

There are about 27 private tertiary education institutions in various fields of study offering programmes of between one to four years. Some of these colleges have also been registered to offer post-graduate programmes. The Council for Educational Accreditation is responsible for accrediting the programmes of these private schools. As yet not all of the programmes offered have been accredited.

The University of Cyprus offers programmes in four faculties:

- Humanities and Social Sciences: Departments of Education, Foreign Languages and Literature, Turkish Studies, Social and Political Science;
- Pure and Applied Science: Departments of Mathematics and Statistics, Computer Science, Natural Science;
- Economics and Management: Departments of Economics, Public and Business Administration;
- Letters: Departments of Byzantine and Modern Greek Studies, History and Archaeology, Classics and Philosophy.

According to the latest data of the Statistical Service, in the academic year 1999-2000 69% of upper secondary school leavers – or approximately 55% of all young people in the relevant age-cohort<sup>19</sup> – continued their studies beyond the secondary level. About

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<sup>19</sup> In the case of male students, because of military service, the relevant cohort is those who completed upper secondary education two years earlier.

40% of those who continued their studies beyond the secondary level attended higher education in Cyprus and the remainder attended higher educational institutions abroad. Out of the total number of tertiary students in that academic year, 46% were studying in Cyprus and 54% abroad. Of those studying in Cyprus, 25% followed degree programmes and 75% sub-degree programmes, whereas of those studying abroad, 91% followed degree programmes and 9% sub-degree programmes. The main countries of destination for tertiary students studying abroad were Greece (53%), the United Kingdom (23%) and the USA (14%).

Financial support is provided for participation in third level education. Where the education takes place within public tertiary education in Cyprus, tuition is free, and parents can also deduct up to CY£1,500 from taxable income for each child in full-time higher education. For education outside Cyprus, there is an annual grant of CY£500 towards tuition fees and of CY£1,000 towards other related costs. Grants for study abroad are provided through the Cyprus State Scholarship Authority, and priorities as regards subjects of studies are set on the basis of the economy's needs. The holders of the scholarships are required to return to Cyprus on completion of their studies.

### ***Initial training***

Initial out-of school training is provided through an apprenticeship scheme as well as through shorter courses organised by the Human Resource Development Authority (HRDA).

The **Apprenticeship Scheme** is designed for persons aged 15 years and above who have completed the three years of compulsory secondary education and have a vocational outlook. The system is administered by the Ministry of Labour and Social Insurance in co-operation with the Ministry of Education and Culture. Apprentices are employed in industry and receive general education and vocational training, on a day release basis, for a period of two years, and the wage costs for the days that apprentices spend in school are subsidised by the Human Resource Development Authority. The programme combines technical training with practical experience in industry and aims at facilitating the transition from schooling to the workplace. Since 1963 7,345 young people have completed the Apprenticeship Scheme. The annual outflow in recent years amounts to 270 apprentices.

In recent years the Apprenticeship Scheme has faced a number of operational and structural problems, the most important of which are the following:

- The low educational level of candidates and the lack of uniformity of the classes;
- The lack of opportunities for instructors to adopt modern teaching techniques;
- The insufficient infrastructure in technical schools to cover the needs of the enrolled students;
- Only a few companies have adequate facilities to provide on the job training;
- Its operating rules and regulations need modernisation.

The main initial training activities of the **HRDA** include:

- **Enterprise-based initial training:** Design, organisation and implementation of training programmes by enterprises for their newly employed personnel.

- **Accelerated training:** Training of mainly new entrants into the labour market to meet needs in occupations where there are significant labour shortages.<sup>20</sup> These programmes are organised by the HRDA in collaboration with the Higher Hotel Institute (HHI) and the Cyprus Productivity Centre (CPC), last from 12 to 24 weeks and include practical training. These programmes are mainly addressed to unemployed school leavers who either before the training begins or by the end of the training (with the help of HRDA, HHI and CPC) will become employed. In 1999, around 250 persons received training in technical and hotel occupations.
- **Management training of tertiary education graduates:** New university and other tertiary education graduates may participate in these training programmes. Enterprises select graduates for employment and training. These programmes last either 6 or 12 months depending on the needs of the post and the qualifications of the graduates involved and include both theoretical and practical training. In 1999, 110 graduates were trained under this scheme.

The HRDA also subsidises the Apprenticeship Scheme, the Postgraduate programme of the Mediterranean Institute of Management (run by CPC) and the practical training of students in certain tourism-related and engineering occupations (secondary school hotel section, HHI and HTI).

### 3.2.2 Continuing education and training

The main **continuing training** activities of the HRDA are:

- **In-company (single company) training programmes:** Design, organisation and implementation of training programmes by enterprises to meet the training needs of their employees. Training can be implemented by trainers who are company employees or by other trainers, from Cyprus or from abroad. More than 21.300 persons (7.3% of employment) participated in such programmes in 1999.
- **Multi-company training programmes:** Participation of employees in training programmes implemented by public or private training institutions and organisations. Participation is arranged between the enterprises and the programme organisers. More than 150 training institutions operate under this category and they cater for a multitude of training themes.<sup>21</sup> During 1999, around 17.800 persons (6.1% of employment) were trained at these programmes.
- **Multi-company high priority training programmes:** Training programmes with institutional and in-house components in issues that the HRDA categorises as of high priority for enterprises. The HRDA subsidies are paid to training institutions and organisations for the total costs incurred for the organisation of these programmes.
- **Single or Multi-company training abroad:** This training takes place abroad to meet enterprise needs, especially in the areas of new technology and innovative

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<sup>20</sup> Shortages and surpluses are anticipated through an annual research study that the Authority carries out (Human Resources Balance). In this study the supply and demand for every occupation (ISCO 88 level 4) and district of Cyprus, is estimated. The comparison of these two factors provides the estimates for the balance (shortages and surpluses) for each occupation and district. This is a short term forecasting exercise covering one to two years in advance. A study to identify medium to long term needs of the labour market has been recently initiated by the HRDA.

<sup>21</sup> The priority thematic areas for training programmes are set on an annual basis by the HRDA. Public and private training institutions are informed well in advance about these priority areas.

management methods. Subsidies can cover up to 70% of employers' expenditure on fees, subsistence allowance and airfares.

In addition to the programmes supported by the HRDA, there are other possibilities for adult/ continuing education through both public and private educational institutions. In the case of public education institutions this type of education is provided through:

- evening secondary schools offering education to adults leading to a secondary school leaving certificate
- evening technical schools offering programmes leading to a technical/ vocational education leaving certificate or to the acquisition of vocational qualifications
- state Institutes of Further Education giving opportunities for learning foreign languages and informatics
- adult education centres offering programmes in a very broad range of topics like music, dance, etc.

### **3.2.3 Issues and policies**

A number of policy concerns can be identified in respect of the future development of education and training.

First, at upper secondary level, the drive towards higher education has resulted in vocational and technical education becoming a sort of second choice and apprenticeship having an even lower degree of attractiveness (and social status). In this respect, the Apprenticeship Scheme is seen primarily an alternative route mainly for secondary school dropouts. As a result, a considerable number of young people enter the labour market without qualifications beyond compulsory schooling.

The main response to these problems is the re-organisation and reform of upper-secondary education that is already under way. The introduction of the *eniaio lykeio*, and the reform of technical/vocational schools, are intended to develop a school system at this level that will provide the means for further academic/professional/vocational studies or training as well as a pre-vocational background. Both types of schools are to place considerable emphasis on solid general education combined with the development of basic skills and abilities. In both cases there is a systematic effort for a balance between basic areas of learning, new technological developments related to the shift towards a knowledge-based economy, and the needs of the labour market. Within this framework, there is an effort for integrating education and vocational education and training into an overall human resource development strategy. One objective of these reforms is to raise the completion rate of those enrolling at second level (at the age of twelve) and ultimately graduate successfully at upper secondary level, to 90%. In addition, the apprenticeship scheme is currently under review. More specifically, a study has recently been completed, the objective of which is the restructuring and modernisation of the apprenticeship scheme, with a view to transforming it into an alternative path to acquire vocational qualifications rather than a last opportunity type for vocational education and training for school dropouts. Finally, apart from these reforms within the initial education and training system, measures have been taken to make it possible for someone, after finding employment, to acquire a qualification through the so-called accelerated vocational training programmes offered by the HRDA in collaboration with the Higher Hotel Institute and the Cyprus Productivity Centre. (See Section 3.2.1 above).

Second, there have been concerns about a "brain drain" problem related to the extent to which young people leave Cyprus to undertake tertiary education. Estimates of the level of the problem are available from a study conducted by the HRDA (Career Paths of Tertiary Education Graduates in the Labour Market of Cyprus 1996-98). According to this study, 14.4% of Cypriot students graduating from tertiary level educational institutions abroad remained abroad after the completion of their studies. There are also marked differences with respect to the level of education. The proportion remaining abroad two years after graduation was 17% for higher (post-secondary) education graduates, 12% for university graduates, and 25% for postgraduates. This is not just a recent phenomenon — in fact the proportion of students staying abroad after graduation fell somewhat between the 1980s and the 1990s. According to a study conducted by the Statistical Service in 1986 and 1987, about 23% of the Cypriot graduates studying abroad at that time remained overseas after the completion of their studies.

In part, this brain drain reflects the labour market experience of third-level graduates within Cyprus. While there has been a marked drop in the share of tertiary education graduates in total unemployment, from 30.7% in 1990 to 15.9% in 2000 (i.e. to levels considerably lower than their share in the total labour force), some graduates appear to find employment below their level of qualification and take positions previously occupied by school leavers with lower levels of education.

However, the reduction in the unemployment rate among tertiary education graduates in the 1990s is also related to structural changes in production, notably the increased importance of the tertiary sector of services. As already noted, a major objective of economic policy is the further development of export services – particularly business services, education and health, activities with a relatively higher human capital intensity. Success in meeting this objective, combined with the general trend towards a knowledge based economy, should lead to improved employment opportunities for higher education graduates, including for those who currently live abroad.

A number of major initiatives are also underway to increase opportunities for third level studies within Cyprus. These include the decision to establish a University for Applied Sciences and Arts and an Open University, as well as to expand the University of Cyprus through a School of Law, a School of Medicine etc. In addition every effort is made to increase research and development activities, particularly through the expansion of institutions in specific areas such as biomedicine.

A number of strategic issues have also been identified in relation to work of the HRDA. First, there is a need to further promote the participation of the unemployed in training programmes in order to meet needs in occupations where there are identified labour shortages. The co-operation and support of the Ministry of Labour and Social Insurance and in particular the PES is recognised to be of crucial importance in these efforts. Second, there is a need to increase the participation of micro-enterprises in training activities. The coverage of enterprises employing 5 to 9 persons in the consultancy services scheme is designed to encourage such a development, and consideration is also being given to possible inclusion, on a selective basis, of the self-employed in the scope of HRDA activities. Third, the planned system of standards of vocational qualifications should be introduced as soon as possible. Finally, there is a need to continue to improve the quality and relevance of training provision, through improved medium-term

occupational forecasting and by continued investment in training infrastructure (including support for the adoption of E-learning methods and techniques).

#### *Assessment*

*In the context of the move towards a knowledge-based society, the reforms aimed at improving the quality and relevance of upper secondary general and vocational education (while also raising completion rates) are appropriate to Cyprus' needs. Effective implementation of the reforms in line with the planned schedule is thus an important priority. The government should also move quickly to promote the restructuring and modernisation of the apprenticeship scheme and the effectiveness of the reforms in tackling the identified problems will need to be monitored closely.*

*Economic growth and structural change are likely to widen opportunities for highly qualified people within Cyprus, thus further reducing the "brain drain". The planned expansion of opportunities for students to attend third-level education within the country will also contribute to this objective.*

*Efforts to increase participation of adults (particularly the unemployed and potential re-entrants to the labour market) in continuing education and training are also required. Movement towards a more active approach by the PES can contribute to these efforts. It will also be important to increase the involvement of the social partners in VET at different levels, from decision making to co-financing and participating in VET provision. In particular, greater efforts are required to encourage employers to invest in training.*

*The Government should continue to develop and implement policies to further improve the quality, transparency and attractiveness of technical and vocational education and training (including apprenticeship). Relevant measures include the continuous modernisation of curricula to take account of economic changes and labour market needs, particularly those relating to new skills and competencies identified by employers; modernising teaching methods through the introduction of new pedagogical approaches as well as reform of initial and continuing training for teachers and trainers; new approaches to integrating work and learning in schools, training centres and companies.*

*Finally, development of a coherent system of lifelong learning requires that the links between initial and continuing vocational education and training should be reinforced. In particular, the Government should accelerate its efforts to establish an integrated national system of vocational qualifications. A transparent qualification system, covering both academic and professional qualifications and mutual recognition of qualifications at EU level, will also contribute to higher occupational mobility.*

### **3.3 Wage developments – wage setting system**

Terms and conditions of employment, including the level and the rate of increase of wages and salaries are mainly determined through collective bargaining. Most collective bargaining is at the industrial or branch level and at the enterprise level. Collective agreements typically cover wages, pay systems and any other issues to do with conditions of employment and work relations. The latter include hours of work, overtime pay, holidays, sickness pay, provident funds and other retirement benefits; and also check-off systems, trade union facilities, rules for recruitment and dismissal and

other procedural matters. Due to the existence of the economy-wide indexation system (see below), the wage setting part of collective bargaining is essentially restricted to agreeing on the rate of increase in wages and salaries, over and above that covered by the indexation system.

Occasionally, there are also national-level negotiations on particular issues (such as the indexation of wages and the reduction of working hours). Under the retrospective indexation (COLA) system, – established through collective agreements – wages and salaries are automatically adjusted twice a year (on 1<sup>st</sup> of January and 1<sup>st</sup> of July) to reflect the change in the average level of prices in the preceding six months. Such systems have been seen, in other countries, to present risks to the flexibility of the labour market in responding to external shocks. However, the COLA is seen as having made a positive contribution to harmonious labour relations and industrial peace; it has also been seen to allow for flexible responses to shocks in the past. Thus in 1974, after the Turkish invasion and occupation of part of the island and the resulting huge unemployment problem, the trade unions accepted not only a temporary suspension of the COLA system, but also a massive cut in wages and salaries. The Government is confident that, should serious economic problems arise in the future, the social partners would consider any necessary adjustments to the COLA system. A recent example of flexibility has been the adjustment of the COLA System, as from the second half of 1999, to exclude the impact of a rise in excise taxes.

The Government has traditionally seen its role as one of “minimum intervention in labour relations”. However, the Government has also assumed a more specific role in industrial relations, i.e. in the settlement of labour disputes and the provision of technical assistance and advice to the two sides. Finally, there is legislation fixing minimum wages for employees in a very limited number of non-unionised occupations – clerical workers, retail shop assistants, childcare and nursing assistants. Legislated minimum wages are not intended to substitute for collective bargaining, and are thus set at levels that do not exceed those in collective agreements.

#### *Assessment*

*Wage developments will continue to be of decisive importance in the competitiveness of Cypriot goods and services and the profitability of investment. It is important that wage developments contribute to an employment friendly policy mix and that the social partners pursue a responsible course and conclude wage agreements on the basis of productivity growth, having in mind wage developments and productivity increases in the trade partners of Cyprus. The COLA system should be kept under review in the light of actual experience of its responsiveness to a changing domestic and external environment.*

### **3.4 Tax and benefit system**

#### *Tax system*

Taxation on labour in Cyprus has three main constituent parts:

**Direct income tax** is levied on all personal income. The first CY£6,000 of income<sup>22</sup> is tax-free. Thereafter, tax is levied at 20% on the first CY£3,000, 30% on the next

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<sup>22</sup> Equivalent to almost 60% of average economy-wide earnings.

CY£3,000, and 40% on all further earnings. The basic tax-free allowance was increased from CY£5,000 to CY£6,000 as from January 2000.

The Social Insurance Scheme in Cyprus covers compulsorily all employed, including government employees, apprentices and the self-employed, and provides pensions and benefits in all areas of social security. **Social insurance contributions** are payable by both the employee and the employer. Both rates are currently set at 6.3% of earnings, subject to a monthly earnings ceiling of CY£1,699. Self-employed people pay a contribution of 11.6% of earnings. (For this group, the earnings base is an imputed potential income calculated for each occupation. Self-employed individuals earning less than the imputed potential income for their occupation contribute according to their actual income.) In respect of both employees and the self-employed, the state makes a further contribution of 4% of earnings to the social fund; this contribution is funded from the general budget.

No major reforms are envisaged to the Social Insurance Scheme in the short term. However, an actuarial valuation of the scheme is carried out every three years in compliance with the Social Insurance Law, with a view to ensuring the scheme's long-term viability of the Scheme in the light of socio-economic and demographic trends. The last such valuation, with reference year mid-1997 and projection period 1998-2050, indicated that under the existing legislative arrangements the financial viability of the scheme is ensured until the year 2020. With a view to sustaining the financial viability of the scheme in a longer-term perspective, a number of recommendations which are included in the recent actuarial study for the Scheme are under consideration.

The **Defence Levy**, a special contribution for the defence of the Republic, is also levied on all sources of income. For workers, the levy is currently set at 4% of earnings – 2% paid by the employee and 2% paid by the employer. Currently, there is a proposal tabled before the House of Representatives by a member of the House for the substitution of the existing defence levy through an increase of 2 to 3 percentage points in the standard VAT rate.

Overall, the tax burden on labour is relatively low by international standards. For a single worker without children earning the average wage, the "tax wedge" stood at 23.2% of total labour costs in 1999; for a one-earner family with two children the wedge was 20.2%. The burden falls further at lower earnings levels – for a single person on two-thirds average earnings the wedge was just over 17%.<sup>23</sup>

The wedge does however rise fairly steeply as income rises, particularly if attention is focused on marginal rather than average rates. While the highest marginal tax rate of 40% is not exceptionally high by international standards, it starts at relatively low income levels – in 1999, at approximately 129% of average earnings for a single worker and at 145% for a married worker with two children. Beyond these income levels, the marginal tax wedge is about 48%. This could potentially act as a disincentive to further supply of labour in the form of additional hours for existing workers.

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<sup>23</sup> In 1998, the latest year for which comparable international data are available, the lowest wedge for this category of worker in the EU was in Ireland, at 23.4%. The median value across the EU member states was just over 39%.

One feature of taxation systems that has received increasing attention in the recent past is their impact on the employment participation decisions of married women. In this respect, the tax system in Cyprus is relatively "individualised" by international standards. As a result, where one member of a couple is already working and earning the average wage, and the second member takes up a job at the same wage-level, the rate at which income tax and social contributions, combined, are levied on these additional earnings is low, at 13.5%.<sup>24</sup> The tax system is thus relatively favourable in its impact on married women's labour market participation.

### ***Benefit system***

As noted in section 2, unemployment benefit for a married worker represents about 78% of net income while in employment. This is at the upper end of the range of "replacement rates" for such workers among the existing EU member states.<sup>25</sup> Benefit duration in Cyprus however, at six months, is relatively short by EU standards.

Some measures have been taken to avoid potential "unemployment traps" in the public assistance scheme, which provides income support for those who have exhausted their entitlement to unemployment benefit, and to encourage the participation of public assistance recipients in the labour market. For example, for a recipient who works, provided that the eligibility criteria are met, a fixed amount of the salary is not taken into account when estimating the level of public assistance. In addition, vulnerable groups (such as persons with disabilities, single parent families, families with four children or more) may be eligible to supplementary public assistance even if the applicant is in full employment.

### ***Assessment***

***The tax burden on labour in Cyprus is relatively low by international standards, and the tax structure is positive in its impact on incentives to take up and remain in employment. Possibilities for tax reform are now under consideration; in particular the government is examining the implications of the ageing of the population and a rise in the dependency ratio for the longer-run financial viability of the Social Insurance Scheme. It will be important to ensure that the positive features of the system be retained under any reforms that ultimately emerge.***

***While replacement rates in the unemployment benefit system are relatively high, this appears not to have impacted adversely on incentives to take up or remain in employment. This in part reflects the extremely strong demand conditions in the labour market in recent years. The risk of disincentive effects emerging will be reduced by the move towards a more active approach to unemployment through the PES as discussed below.***

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<sup>24</sup> In the existing EU member states, the equivalent rate ranges from a low of 21% in Portugal to a high of 57% in Belgium. (OECD, *Benefit Systems and Work Incentives*, 1999).

<sup>25</sup> Direct international comparisons in this field are difficult given differences in the structure of tax and benefit systems. However, data in OECD *Benefit systems and Work Incentives 1999* indicate that for this category of worker in the first month of unemployment, basic unemployment benefits in 1997 (after tax, where relevant) ranged from approximately 40% of previous net earnings in Greece and Italy to approximately 70% in Portugal and Spain. (After inclusion of housing and family benefits, the replacement rate ranged from approximately 50% in Greece and Italy to over 80% in Sweden, Finland and the Netherlands.)

### **3.5 Public Employment Services**

The PES is already an important instrument of employment policy, providing a range of services to both employers and job seekers. However, as compared with emerging practice in the EU under the Employment Strategy, the relationship between the PES and individual unemployed people can be characterised as relatively re-active rather than active. Regular PES-initiated contact with the unemployed is limited to monthly confirmation of continued compliance with the administrative requirements for receipt of benefits. The capacity of a PES to develop a more active approach depends in part on the level of resources devoted to it and on how those resources are deployed.

In the year 2000, the average number of dependent employees in the Cypriot economy, per PES staff member, was 3,763. The number of registered unemployed per PES staff member was 203 in 1999 and 195 in 2000. Both ratios are at the upper end of the international range, suggesting that the PES is relatively under-resourced, particularly in the context of its undertaking any increased responsibilities.

The Government recognises the importance of providing quality and timely services to the labour market. Current priorities for development include vocational guidance and counselling activities, and a more customer-oriented approach to both job seekers and employers. To this end, action is planned to create additional PES services points and to raise the competence of the PES to deal effectively with difficult groups and with vacancy cases requiring high specialisation.

As from May 2000 placement activities have been computerised, and this should permit additional staff resources to be devoted to systematic engagement with the unemployed. The computerised system should also provide more extensive statistical data, giving the PES an improved insight into the supply and demand of labour in order to support both the placement function and the policy formulation process. Additionally, a self-service approach to the PES provision is now under consideration in connection with the offer of additional services by the PES

#### *Assessment*

*To enhance the effectiveness of the PES, it will be important to move towards active engagement with the unemployed as part of a preventive and employability-oriented strategy. This will involve earlier and more regular PES-initiated contact with those who become unemployed, building on early identification of individual needs. The emphasis should be on support for active job-search and, where necessary, access to relevant labour-market programme opportunities. To achieve this, additional resources will need to be devoted to these areas of PES activity.*

*The 2000 LFS results indicate that almost one third of the unemployed are out of work for over one year. Preventive policies should therefore be supplemented by PES action to support the reintegration of the long-term unemployed.*

### **3.6 Active labour market programmes**

With near-full employment having prevailed for many years, there has been limited development of active labour market programmes. The major activity relates to human resources development where, as is clear from Section 3.2, most provision has focused on multi-company training and on in-firm training of the employed. There are however

a number of additional measures aimed at improving the employability of certain categories of the labour force:

The **Self-employment Scheme for tertiary education graduates** provides financial incentives in the form of an interest rate subsidisation for loans undertaken with a view to creating self-employment. An evaluation in 1996 showed that the scheme had a positive impact on employment creation. During the first ten years of its operation, the scheme had contributed to the self-employment of 260 persons and the projects promoted had generated employment opportunities for an additional 420 persons. Moreover, the scheme led to additional investment expenditure amounting to 225% of the level of the original investment financed through the scheme. Overall, even though the scale of the scheme is limited, it can be considered to have been successful in the creation of permanent self-employment opportunities for a number of university graduates.

Based on the evaluation the scheme was revised in 1998 to make it more attractive and accessible to a wider range of occupations in all sectors of the economy. The size of loan offered was increased and interest rates were lowered. To encourage innovation and co-operation, more favourable terms were introduced for innovative or for group projects.

A **self-employment Scheme for older persons** is to be introduced this year. Its aim is to keep older persons (63 years and over) actively involved in economic and social activities. The scheme will provide grants to engage in activities such as agriculture and stockbreeding, home made sweets and jams, embroidery, ceramic work etc.

Three measures to enhance employment opportunities of **people with disabilities** were introduced in 1993. A specific self-employment scheme for this group provides technical assistance and required technical aids, as well as investment grants and interest-rate subsidies. Under a separate scheme, persons with disabilities are also entitled to reimbursement of training costs involved in courses of their own choice aimed at improving their employment prospects. Eligible training includes apprenticeship as well as training with individual employers. Finally, employers are entitled to a reimbursement of part of the costs involved in providing facilities for newly engaged disabled persons (e.g. ramps, ergonomic alterations to machinery). Taken together, these three schemes have provided assistance to approximately 140 people to date.

An employment support scheme for people with disabilities was introduced in 1996 to further facilitate their placement and employment in the open labour market. It is aimed at persons with mental or multiple disabilities whom training and employment in sheltered settings or care institutions failed to prepare for open employment. Support is provided in the form of a job-coach, who after assessing the person's overall disabilities and capabilities and after obtaining the family's consent and co-operation, proceeds in placing him/her in a job which matches the person's capabilities and interests. The programmes promoted through the scheme are run by voluntary organisations, and are financed up to 75% by the Government, which also provides technical assistance to the voluntary organisation, and follows up and assesses the operation of the programme. For the period 1997-2000, 103 persons with severe disabilities have been integrated in the labour market through 11 individual supported employment programmes.

Overall, schemes for the vocational rehabilitation of persons with disabilities are seen as having been successful, in the sense that opportunities for employment are provided to a group of persons facing particular difficulties in integration to the labour market. However, the authorities see room for improvement in extending the utilisation of the schemes to an even larger number of persons with disabilities.

#### *Assessment*

*Given current and recent labour-market conditions, the existing range of active programmes (with the inclusion of relevant HRD measures discussed in Section 3.2) appears appropriate to Cyprus' needs. However there is a need to further promote the participation of the unemployed in training programmes in order to meet needs in occupations where there are identified labour shortages. Increased access for this group should result from the more active approach being adopted by the PES and supported by the HRDA. In addition, there may be more scope for existing programmes to contribute to the integration of groups currently not in the labour force – primarily women.*

*It is probable that provision for these additional groups can be met with only limited expansion in the current scale of active programmes, although some programme enhancements may be required to address their particular needs. This should include more emphasis on vocational guidance. Continuous monitoring and evaluation of the programmes and their impact, on existing and new target groups, will be needed to ensure that they remain relevant to clients' needs.*

### **3.7 The role of foreign workers**

The role of foreign workers is relatively important in Cyprus, and has expanded substantially in recent years, contributing greatly to the alleviation of potential labour-market tensions and thus raising the growth potential of the economy. At the same time, foreign workers remain concentrated in a limited range of sectors and occupations. Access to a wider range of occupations could further enhance their contribution to labour market flexibility.

Although increased flexibility in the domestic labour force can be expected from current and planned policies, it seems certain that Cyprus will continue to have a relatively large foreign workforce in the future. The pattern to date has been one mainly of temporary employment of foreign workers. Even so, continued inflows of foreign workers over a long period inevitably involves an increase in the number of such workers with a deeper attachment to the Cypriot labour market. Parallel developments in other European countries are giving rise to widespread review of policies on foreign workers. A similar review would provide a useful basis for the formulation of future policy in Cyprus, particularly in the context of Cyprus' own accession and of the wider enlargement of the EU.

#### *Assessment*

*The likelihood of the continued presence of a significant number of foreign workers will inevitably raise issues related to the place of such workers in overall employment policy. As elsewhere in Europe, therefore, there is a case for a strategic review of policies in relation to foreign workers.*

### **3.8 Equality of opportunities**

As already noted, women's labour participation rate (58%) although it increased considerably in the last two decades it is still much lower than men's (81%) and still below the corresponding EU average. Moreover, women – especially young women and rural women – seem to face a higher unemployment problem. Relatively high female unemployment for those aged 35-44 also suggests that women returning to work after a period outside the labour force face particular difficulties. Gender imbalances in occupations are also evident, and these in turn are reflected in a significant overall pay gap between men and women.

The medium-term Strategic Development Plan of the Government attaches particular emphasis to promoting the principle of gender equality. This is in part prompted by emerging labour shortages as reflected in the significant presence of foreign labour. The SDP identifies the need for a further increase of female participation levels, a more balanced representation of women and men in all sectors and occupations and further narrowing of the gap between men and women earnings.

Currently, the relevant measures/actions for the promotion of these objectives include the following:

- The improvement and upgrading of the facilities offered to employed parents in order to reconcile work and family life. Priorities include the expansion and improvement of child-care facilities (through a Government grant scheme to NGOs providing such facilities); the provision of special allowances to working people with elderly parents at home in order to secure carers; and the promotion of part-time employment and other flexible forms of employment.
- The encouragement of women to participate in ab-initio and continuing training programmes and to enter new fields of occupations. The HRDA allows no discrimination on the basis of sex or other characteristics in access to training. However, women accounted for only 37% of participants in training activities in 1999, as compared to their 39% share in total employment, and their share of 62% in total unemployment)
- Raising awareness on equality issues through appropriate training of staff in the education system, the promotion of special campaigns and the encouragement of the media to contribute to this effort.
- Subsidisation of NGOs and National Machinery of Women Rights to promote and implement gender equality programmes
- The introduction of a Gender Managerial System, which will be the tool for the integration of women's issues into all Government policies.
- Improvement of the equality legal framework through the legislative transposition of the *acquis* and its effective implementation.

#### *Assessment*

***Raising employment and reducing unemployment for women, together with a reduction in gender gaps both in pay and in access to higher occupations, are urgent priorities both from the point of view of equality of opportunities and of the achievement of overall employment-policy objectives. Every effort should be made to speed up the implementation of planned gender-equality measures. Particularly important will be increased access for women to training and retraining programmes; full implementation of the "acquis" in relation to both equal pay and equal***

*opportunities; support for "family-friendly" employment patterns and practices; and efforts to raise awareness on equality issues.*

### **3.9 Regional disparities**

Economic development, despite the particular emphasis attached to regional and rural development within the framework of the Five-Year Development Plans, has not been uniform throughout the island. Thus, the promotion of the development of the areas that are lagging behind constitutes one of the main priorities of medium-term economic policy. To this end work is underway on developing a coherent and explicit regional policy with the overall objective of promoting balanced development of the whole territory of the island and thus enhancing economic and social cohesion. The main planned measures include the implementation of regional development programmes, which will include schemes for the restructuring and modernisation of the local economy; and the further development of the infrastructure (mainly the road network and environmental infrastructure), in order to raise the economic and employment potential of the less advantaged regions. It is recognised, however, that complementary labour market policy measures may be required to support this effort.

#### *Assessment*

*The development of regional policy should pay more explicit attention to the contribution of employment and human resources measures. In particular, care should be taken to ensure sufficient access to education and training programmes for those living in the less-advantaged areas.*

### **3.10 Preparation for Implementation of the European Social Fund**

This Joint Assessment Paper constitutes an important preparatory document for developing policy and action with respect to future effective use of assistance from ESF in Cyprus after accession. The medium term priorities set out in the JAP should therefore also be reflected in the planning and implementation of human resource development (HRD) policies in the context of the pre-accession Financial Regulation.

The Planning Bureau will be the single Managing Authority for the Community Support Framework or the Single Programming Document, according to Structural Funds Regulations. The Ministry of Labour and Social Insurance will be the authority responsible for the ESF. A Special Preparatory Programme (SPP) project for Structural Funds (to be financed through EU pre-accession funds) will soon be implemented which will review, amongst others, the envisaged Structural Funds implementation system. Within this project the role of each government authority (Planning Bureau, Treasury Department, Ministry of Labour and Social Insurance, Ministry of Agriculture, Natural Resources and Environment and Ministry of Interior) will be determined especially in relation to Managing and Paying Authorities and the management of the various Funds, including ESF. Following the implementation of the SPP the necessary structures will be set up.

The role of the Planning Bureau, which will be the single Managing Authority for preparing the National Development Plan, in co-operation with the Ministry of Labour and Social Insurance, will ensure the linking of ESF priorities to those in the NDP.

Thus the JAP, together with domestic policy documents (the National Development Plan, and the National Employment Plan), will support the preparation of the

Community Support Framework and the Operational Programmes for Structural Funds interventions in Cyprus at national and regional level. This process will require effective monitoring mechanisms (including Monitoring Committees) and monitoring methods based on meaningful indicators.

The JAP priorities, taken together with the relevant national planning documents, constitute an important support for deriving the necessary indicators and for the establishment of a monitoring system in the fields of employment and HRD that will prepare the ground for future ESF-monitoring.

#### *Assessment*

***The Government should take all the necessary preparatory measures in order to take full advantage of the opportunities offered by its future participation in ESF programmes and activities.***

## **4. Conclusions**

As noted in the Commission's *Regular Report* for 2000, Cyprus "is a functioning market economy and should be able to cope with competitive pressure and market forces within the Union". Cyprus has reached a relatively high level of development, the economy continues to grow strongly, and the country has been operating at full employment for some time. Some macroeconomic imbalances emerged over recent years – with rising fiscal and external deficits in 1997-98, and rising inflation in 1999-2000. However, policy action has now placed the fiscal deficit on a downward path; the external deficit was reduced sharply in 1999, and although it widened somewhat in 2000 this is seen as largely due to temporary factors; and inflation has abated significantly in the first half of 2001. The authorities' policy stance aims to sustain and intensify the reforms that contributed to the diversification of the export-oriented services sector of the economy and to strengthen the policies that have helped to reduce and reverse macroeconomic imbalances.

In these circumstances, the main focus of this JAP has been to identify actual and potential labour-market imbalances that might constrain economic growth, and to assess how employment policies might be improved to deal with these imbalances. While the labour market in Cyprus can be considered to be relatively flexible and well functioning, a number of areas have been identified where employment policies can contribute further to economic and social development. The main priorities identified include:

- Full and effective implementation of the reforms in upper secondary education in line with the planned schedule, together with restructuring and modernisation of the apprenticeship scheme.
- Implementation of planned measures to raise further the returns, to Cyprus, from the substantial public and private investment in tertiary education.
- Efforts to increase participation of adults (particularly the unemployed and potential re-entrants to the labour market) in continuing education and training. These should be accompanied by the development of a coherent system of lifelong learning, based on improved links between initial and continuing vocational education and training and an integrated national system of academic and professional qualifications.
- Wage developments should reflect productivity growth, having in mind wage developments and productivity increases in the trade partners of Cyprus. The COLA

system should be kept under review in the light of actual experience of its responsiveness to a changing domestic and external environment.

- Maintenance of the broadly "employment-friendly" character of the system of taxation, social contributions, and unemployment compensation.
- Moving the PES towards more active engagement with the unemployed as part of a preventive and employability-oriented strategy. This will involve earlier and more regular PES-initiated contact with those who become unemployed, building on early identification of individual needs. Preventive policies should also be supplemented by PES action to support the reintegration of the long-term unemployed. The emphasis should be on support for active job-search and, where necessary, access to relevant labour-market programme opportunities. This may require some additional staffing and other resources in the PES.
- While the existing range of active labour-market programmes (including human resources measures) appears appropriate to Cyprus' needs, improved access to these programmes is required for a number of important target groups such as the unemployed, and certain groups currently not in the labour force – primarily women. Continuous monitoring and evaluation of the programmes and their impact, on existing and new target groups, will be needed to ensure that they remain relevant to clients' needs.
- Every effort should be made to speed up the implementation of planned gender-equality measures. Particularly important will be increased access for women to training and retraining programmes; full implementation of the "acquis" in relation to both equal pay and equal opportunities; support for "family-friendly" employment patterns and practices; and efforts to raise awareness on equality issues.
- There is a case for a strategic review of the overall policy on temporary employment of foreign workers in Cyprus, both in terms of its contribution to labour-market flexibility and of rights and opportunities for migrant workers.
- The development of regional policy should pay more explicit attention to the contribution of employment and human resources measures. In particular, care should be taken to ensure sufficient access to education and training programmes for those living in the less-advantaged areas
- Continuing the Government's work on establishing the institutional structures necessary for the implementation of ESF, taking account of the policy priorities outlined in this JAP

Employment and human resources issues have already been an important focus of attention in successive 5-year *Strategic Development Plans*. Work has also commenced on the preparation of a more detailed National Action Plan for Employment Thus Cyprus is making rapid progress in its preparations for implementation of the European Employment Strategy and for meaningful participation in the EU employment co-ordination process.

The Commission and the Government of Cyprus intend that the preparation of this Joint Assessment will form only the first stage in an ongoing process of employment policy review. Further co-operation will concentrate on joint monitoring of progress in implementing the measures outlined above, *inter alia* through the preparation of regular implementation reports.