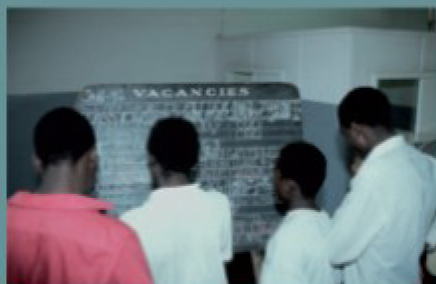
DECENT WORK AND FAIR GLOBALIZATION: A GUIDE TO POLICY DIALOGUE



DECENT WORK AND FAIR GLOBALIZATION: A GUIDE TO POLICY DIALOGUE

UNITED NATIONS
New York and Geneva, 2010

The responsibility for views and ideas expressed in this publication rests solely with the author, and publication does not constitute an endorsement by the United Nations Non-Governmental Liaison Service or any other part of the UN system of the opinions expressed.

NGLS publications are published for non-governmental and civil society organizations and others interested in the institutions, policies, and activities of the UN's agenda, including economic and social development, human rights, environment, peace and security. This publication, and all other NGLS publications, can be found on the NGLS website (www.un-ngls.org). Text from this publication may be reproduced unaltered without authorization on condition that the source is indicated. For rights of reproduction or translation, application should be made to NGLS, Palais des Nations, 1211 Geneva 10, Switzerland.

Photo credits
Front cover: Top (SOLIDAR)
Bottom (from left to right): UN Photo/Eskinder Debebe; ILO/Crozet, M.; ILO/Maillard J.
Back cover: ILO/Sovannara K.

UNCTAD/NGLS/2010/2

Sales No. E.10.I.10

ISBN 978-92-1-101221-7

©2010 United Nations. All rights reserved.
Published in May 2010 by
UN Non-Governmental Liaison Service (NGLS)
Palais des Nations, CH-1211 Geneva 10, Switzerland
Room DC1-1106, United Nations, New York NY 10017, United States

"A fair globalization requires greater convergence of economic and social policies around the goal of decent and productive work for all. New policy thinking and strong advocacy are critical.

"This NGLS guide is extremely timely. It challenges much of the conventional thinking that guided policy making over the past three decades and which the crisis has shown to be profoundly flawed. Furthermore, it collects a broad set of proposals for alternative approaches to macroeconomic, financial, trade and employment and social protection policies that place the drive for decent work at their heart.

"As such it is a unique resource for civil society organizations, social movements and all those who campaign for economic and social justice."

Juan Somavia, Director-General of the International Labour Organization (ILO)

"In the last few years, there has been an increasing level of support for policy coherence to achieve a fair globalization, full and productive employment and decent work for all. To get global consensus on these core objectives has been a major achievement. But implementing the policy implications that derive from these commitments would require nothing short of a major overhaul in the way economic policies have been formulated in the last two or three decades. The global economic crisis provides an opportunity for a dramatic change of course, but in the face of pressures for a return to 'business as usual' we need to broaden political support around this alternative agenda.

"This NGLS guide to policy dialogue provides many thought-provoking suggestions for alternative economic strategies at national and international levels to realign macro-economic, financial and trade policies so as to meet the imperatives of full and decent employment. I strongly recommend that all interested in the decent work agenda find the time to read and consider its proposals."

Guy Ryder, General Secretary of the International Trade Union Confederation (ITUC)

ACKNOWLEDGEMENTS

This NGLS publication, *Decent Work and Fair Globalization : A Guide to Policy Dialogue*, was prepared by **Hamish Jenkins**, United Nations Non-Governmental Liaison Service (NGLS).

NGLS gratefully acknowledges the generous support of the Royal Ministry of Foreign Affairs of Norway to a project on Supporting Policy Dialogue with Civil Society on the Decent Work for a Fair Globalization Agenda, which made this publication possible. It enabled NGLS to organize a number of workshops and side events as well as a global civil society consultation for the Commission of Experts of the President of the General Assembly on Reforms of the International Financial and Monetary System (the "Stiglitz Commission"), which generated new and innovative thinking on which this publication draws heavily.

The lead author would like to thank in particular Stephen Pursey and Aurelio Parisotto (International Labour Office) and Thoralf Stenvold (Royal Ministry of Foreign Affairs of Norway) in helping to shape the original project. The author also owes his gratitude for substantive inputs from Radhika Balakrishnan (Center for Women's Global Leadership), Christophe Bellmann (International Centre for Trade and Sustainable Development), Esther Busser (International Trade Union Confederation), Aldo Caliari (Center of Concern), Joshua P. Greenstein (New School for Social Research), James Heintz (Political Economy Research Institute at University of Massachusetts), Massimo La Marca (United Nations Conference on Trade and Development) and Sanya Reid Smith (Third World Network). The author is also very grateful for the comments from his colleagues Zachary Bleicher, Jolanda Groen, Beth Peoch and Elisa Peter (NGLS).

contents

Preface VII
Executive Summary VIII
Acronyms XI

1. INTRODUCTION 1

- Decent work and fair globalization go hand in hand 2
- Decent work is a human right 3
- The global decent work deficit: a primary cause of the global economic crisis 3
- Impact on people: unemployment, poverty and the threat of wage deflation 5
- Decent work at the heart of a successful recovery: the Global Jobs Pact 6
- Policy coherence for decent work and a fair globalization: broadening the movement 7

2. GLOBALIZATION AND EMPLOYMENT: A BROAD PERSPECTIVE 9

- Growing socio-economic insecurity and low employment-intensity of growth 9
- The "global" at the expense of the "local" 10
- Putting the cart before the horse? 10

3. BUILDING A SOCIAL FLOOR UNDER THE GLOBAL ECONOMY 13

- Social protection as an economic investment 13
- Elements of a social protection floor 14
- Cash transfers and employment guarantees 15
- A universal basic income guarantee? 16
- How much does basic social protection cost? Is it affordable? 17
- The fiscal space challenge 18

4. MACROECONOMIC POLICIES FOR DECENT WORK 19

- The forgotten lessons of the Great Depression 19
- Strengthening the employment and decent work content of stimulus packages 20
- "Pro-cyclical" IMF conditionalities? 20
- Impacts of financial liberalization 22
- Capital management for employment and decent work 24
- Central banks as agents of employment creation 26
- Do higher wages and full employment accelerate inflation? 28
- Heterodox financial and monetary tools to support employment 30

5. A DEVELOPMENT PARADIGM SHIFT:
POVERTY REDUCTION THROUGH PRODUCTIVE EMPLOYMENT GROWTH 35

- What is pro-poor growth? 35
- The neglected importance of local demand 36
- Agricultural growth linkages, employment and poverty reduction 37
- Resource mobilization and State capacities 38
- The balance-of-payments constraint (part 1) 39
- A development-led approach to trade 40

6. TRADE RULES FOR DECENT WORK AND A FAIR GLOBALIZATION 43

- The trade and labour standards debate 43
- The impact of trade liberalization on employment 44
- Policy space in trade rules for national decent work strategies 46
- Industrial tariff liberalization (NAMA) 47
- A Special Safeguard Mechanism for Agriculture 48
- Financial services liberalization 49
- Proliferation of North-South regional and bilateral trade agreements 50
- A governance vacuum 50

7. SYSTEMIC REFORMS FOR FULL EMPLOYMENT AND DECENT WORK 53

- International tax issues 53
- A new international debt architecture 54
- The balance-of-payments constraint (part 2) 55
- Towards a new global reserve system? 55
- How would the system work? 57
- A "bottom-up" regional approach? 58
- Staving off currency speculation for stable employment 59

8. CONCLUSIONS 61

1. A framework for accountability and coherence 61
2. Connecting with national political processes 61
3. Decent work is a "win-win" programme for society and the economy 61
4. The MDGs and the decent work agenda 62
5. A human rights agenda for economic reform 62
6. "Deglobalization" or better "localization"? 63
7. Creating space for alternatives 63

References 65

Annex I 71
- Competing Theories on Wages and Full Employment: An Overview 71

preface

In 2005, Heads of State and Government gathered in New York at the UN World Summit and agreed to strongly support a fair globalization and make full and productive employment and decent work for all a central objective of national and international policies, including poverty reduction strategies, as part of ongoing efforts to achieve the Millennium Development Goals (MDGs).

This decision represented a major paradigm shift in the global economic and development discourse as it was the first time governments formally acknowledged the importance of full and productive employment for people to get out of the cycle of poverty and as a means to achieving equitable, inclusive and sustainable development. A new target on decent work was added under MDG 1 and since then, the United Nations has worked to mainstream the decent work agenda in its programmes and activities in an effort to turn the 2005 political commitment into concrete policy changes supportive of workers' rights, job creation, social dialogue and social protection.

Yet, as the 2008-2009 global financial and economic crisis painfully reminded us, the realization of decent work remains a distant dream for millions of people in the world. In an analysis of the impact of the global recession, the *World of Work Report 2009* of the International Labour Organization projected that unless adequate measures are adopted, more than 40 million people could drop out of the labour market in 2010. Other ILO studies estimate that some 200 million workers, mostly in developing economies, could be pushed into extreme poverty.

This guide from the United Nations Non-Governmental Liaison Service (NGLS) aims to broaden understanding of the concept of decent work and demystify the complex linkages that exist between macroeconomic, trade and financial policies and the creation of decent jobs. It builds on the findings of the 2002-2004 World Commission on the Social Dimension of Globalization, which stressed the need to bring coherence between macroeconomic, trade and financial policies on the one hand and development and social goals on the other.

It is hoped that this guide will help the emerging decent work movement to engage more effectively with the economics discourse in order to better articulate the human right to decent work into specific economic policies. Global well being and human progress require a fair globalization that reinforces both economic development and social justice at the international, national and community levels. This guide provides some innovative means to get there.

Elisa Peter
Acting Coordinator
United Nations Non-Governmental Liaison Service (UN-NGLS)
May 2010

executive summary

The recent world economic and financial crisis has dramatically increased the credibility of UN, civil society and other voices calling for a major overhaul in current approaches to economic governance. An essential anchor to leverage such change is the 2005 commitment of all Heads of State and Government to strongly support a "fair globalization" and to make "full and productive employment and decent work for all" a central policy objective in all relevant national and international policies.[1]

The policy implications of reintegrating full productive employment on the global economic and development agenda have not yet been fully explored. This NGLS guide to policy dialogue aims to map out what the ramifications of this commitment mean in terms of better holding economic governance institutions (whether finance ministries, central banks or international economic bodies) accountable to full and decent employment goals. It also aims to help strengthen the advocacy of civil society organizations campaigning for greater economic and social justice by providing tools for more informed policy dialogue on how to align macroeconomic, trade and financial policies with these new objectives.

MAIN FINDINGS :

- The current model of economic globalization is morally unacceptable and politically unsustainable. Its imbalances and deflationary bias cause massive regressions in the progressive realization of the human right to decent work. The current approach of deep global economic integration and liberalization as a path to full employment has failed.

- Growing socioeconomic insecurity associated with trade and financial liberalization makes it essential to achieve a quantum leap toward establishing a basic "social protection floor" under the global economy. This floor should be capable of preventing people from falling into destitution and help them climb up the socio-economic ladder. Some developing countries could achieve such a floor with internal shifts in resources, but many others will need external assistance to kick-start meaningful basic social protection systems.

- The global economic crisis has necessitated unprecedented interventions in the economy – even among governments elected on a free market platform. However, stimulus and other measures to limit the damage of the global recession have not sufficiently focused on employment and social protection. Worse, many countries facing difficulties in their public finances are told to take measures to reassure international investors at the expense of deepening the recession. This is delaying recovery and unnecessarily increasing the time lag between economic recovery and employment recovery to pre-crisis levels – which themselves were already far too low to meet legitimate aspirations of a growing working age population.

1. Paragraph 47 of the 2005 UN World Summit Outcome Document.

- One of the underlying causes of the global economic crisis was the “crisis before the crisis,” a “global decent work deficit” expressed in terms of high unemployment, growing income inequality, and an increasing growth of informal employment correlated with the working poor. These trends had the perverse economic effect of taking money away from people who would spend to keep the economy going, thus contributing to a deficiency in “global aggregate demand.” This was compensated for a while by debt-driven consumer spending in the United States, but which ended abruptly with the collapse of the US sub-prime mortgage market. A major challenge is how to reverse the worldwide tendency of stagnant or declining wages – how to better share the benefits of growth, for example by closer aligning wage growth with productivity growth.

- To change course, a broad panoply of “Keynesian” or “heterodox” macroeconomic policy options tailored to each country situation is called for. These include capital controls and prudential regulations (capital management techniques) that can limit the havoc caused by the free flow of capital across borders, penalize irresponsible risk-taking and reward long-term investments in productive employment. Central banks must begin playing a much more active role in controlling “profit inflation” on financial markets (not just consumer price inflation), while promoting full employment as part of their core monetary policy objectives. “Employment targeting” in macroeconomic policy-making is one practical way forward.

- A new development paradigm focused on building productive capacities in a way that expands productive employment in developing countries (especially low-income countries) is necessary to make any significant progress in reducing poverty. It means an overhaul of conditionalities and aid packages informed by a wrong development model which has created lop-sided patterns of growth that have been neither inclusive nor employment-intensive. It means a greater focus on local sources of demand as an incentive for more domestic productive investments which in turn create more productive jobs. This can happen if development strategies focus not only on supporting dynamic sectors with export potential, but also small enterprises producing for the local market where the majority of people (and the poor) work. Major investments to support smallholder agriculture are essential, not only for food security, but also to revive local demand for locally-produced goods and create a virtuous cycle of poverty reduction.

- The controversial debate on trade and labour standards has to an extent diverted attention from another key dimension of the trade and labour nexus: the impact of trade liberalization on employment. The international trading system needs to make important changes to be consistent with the goal of full and productive employment. It means ensuring as far as possible that trade policies do not undermine local employment in sectors that are not yet in a position to compete internationally. It also means that it is not sufficient to focus on the need to have effective social protection systems in place as a means to cushion the socio-economic dislocations of a trade agenda that continues to treat liberalization as an end in itself. It implies a new approach to “policy space” for developing countries in international trade rules, especially in the areas of agriculture and industrial tariffs. Trade agreements that impede adequate regulation of financial services and the use of capital management techniques must also be reviewed.

- Systemic reforms to free up resources to support full employment and social protection are needed in the areas of international taxation (such as an international financial transaction tax); international tax cooperation (to reverse a "race to the bottom" in progressive fiscal revenue); and the international debt architecture. The global economic crisis has also brought to the fore a major limitation of the post-World War II international financial architecture: the incompatibility of the current global reserve system with financial stability and global full employment. Among the most inequitable and economically counter-productive characteristics of the current economic system is the conventional approach to the "balance-of-payments constraint" that places the burden of global adjustments on trade deficit countries with weaker currencies. Proposals for new global and regional reserve systems discussed at the United Nations and elsewhere are essential steps towards correcting global imbalances and asymmetries that are at the root of many causes of unemployment worldwide. It would give countries greater policy space needed to pursue a genuine full employment policy that is not at the expense of other countries, but is mutually beneficial to all.

The decent work and fair globalization agenda can therefore help articulate a broad range of UN and civil society concerns into a coherent platform for change. It can help connect campaigns on complex international economic issues with national political processes that invariably gravitate around people's primary concerns about jobs and livelihoods. It helps to demystify economic debates and outlines concrete alternatives to the prevailing doctrines of the last three decades.

acronyms

ASYCUDA	Automated System for Customs Data
BIG	Basic Income Grant
BWIs	Bretton Woods institutions
CEB	Chief Executives Board for Coordination
CEPR	Centre for Economic Policy Research
DAC	Development Assistance Committee of the OECD
DCF	Development Cooperation Forum
DESA	UN Department of Economic and Social Affairs
ECB	European Central Bank
ECOSOC	Economic and Social Council
ELCRN	Evangelical Lutheran Church in the Republic of Namibia
EPZs	export processing zones
Eurodad	European Network on Debt and Development
EWI	Employing Workers Indicator
FAO	Food and Agriculture Organization of the United Nations
FDI	foreign direct investment
FES	Friedrich Ebert Stiftung
FTT	Financial Transaction Tax
G-20	Group of Twenty
G-33	Group of Thirty-three developing countries
GATS	General Agreement on Trade in Services
GDP	Gross Domestic Product
ICT	Information and Communication Technology
ICTSD	International Centre on Trade and Sustainable Development
IILS	International Institute for Labour Studies
ILO	International Labour Organization
IMF	International Monetary Fund
ITUC	International Trade Union Confederation
LDCs	Least Developed Countries
MDGs	Millennium Development Goals
NAIRU	Non-Accelerating Inflation Rate of Unemployment
NAMA	Non-Agricultural Market Access
NAMTAX	Namibian Tax Consortium
NGLS	UN Non-Governmental Liaison Service
NGO	Non-governmental Organization
NREG	National Rural Employment Guarantee
ODA	official development assistance
OECD	Organisation for Economic Co-operation and Development
PRSPs	Poverty Reduction Strategy Papers
SAPs	Structural Adjustment Programmes
SCM	Subsidies and Countervailing Measures
SDRs	Special Drawing Rights
SCRER	Stable and Competitive Real Exchange Rate Policy
SMEs	Small and Medium-sized Enterprises

SSM	Special Safeguard Mechanism
TRIMs	Agreement on Trade-Related Investment Measures
TRIPs	Trade-Related Aspects of Intellectual Property Rights
TWN	Third World Network
UNAIDS	United Nations Joint Programme on HIV/AIDS
UNCTAD	United Nations Conference on Trade and Development
UNDAF	United Nations Development Assistance Framework
UNDF	United Nations Development Forum
UNDP	United Nations Development Programme
UNESCO	United Nations Educational, Scientific and Cultural Organization
UNFPA	United Nations Population Fund
UNICEF	United Nations Children's Fund
UNIDO	United Nations Industrial Development Organization
UNHCR	United Nations High Commissioner for Refugees
UNRISD	United Nations Research Institute for Social Development
WHO	World Health Organization
WTO	World Trade Organization

1. INTRODUCTION

At the last major international review of progress towards realizing the Millennium Development Goals (MDGs), the 2005 United Nations World Summit, a major qualitative policy shift took place. All Heads of State and Governments committed to strongly support a "fair globalization" and in this context, resolved to make "full and productive employment and decent work for all" a "central objective" of "relevant national and international policies," including development strategies to meet the MDGs.[2] Until then, access to decent employment and livelihoods as an essential route out of poverty was absent from the MDG framework – and more broadly from the global economic agenda. Since then this objective has been added as a new formal target under MDG 1 on poverty reduction and is being mainstreamed across the UN and multilateral system.[3]

Turning this commitment into concrete policy changes is now the major challenge. The reintegration of full and productive employment into the economic policy agenda can greatly contribute to the "paradigm shift" that a growing number of voices have been calling for in the last few years – and made all the more imperative in the wake of the confluence of global crises (from the global economic, food to climate crises). It offers potentially very powerful levers to strengthen the accountability of economic policy making bodies – if their decisions are now to be judged and reoriented in terms of their impact on the quantity and quality of employment; and on broader decent work objectives such as social protection. ILO Director-General Juan Somavia has noted that a "global decent work movement" is in the making, but it will need significant broadening in order to increase the chances of moving from agreement in principle to meaningful socioeconomic transformation. United Nations Assistant-Secretary-General for Social and Economic Affairs Jomo K.S. posited in this regard that:

> "After twenty-five years of the Washington Consensus, a worldwide 'social protection' counter-movement is emerging in response to the consequences of the trend towards economic globalization and liberalization. One focus of this counter-movement is the promotion of full and decent employment" (Jomo 2007:17).[4]

The purpose of this NGLS policy guide is to support the emerging global decent work movement by providing civil society organizations, policy makers and other actors with tools to engage in informed policy dialogue on the nexus between macroeconomic, trade and finance policy in relation to full productive employment and decent work goals.

---

2. Paragraph 47 of the 2005 UN World Summit Outcome Document.

3. The United Nations Economic and Social Council (ECOSOC) also prioritized full productive employment and decent work for all during its 2006 session, which called on UN system agencies and invited international financial institutions to mainstream these goals in their policies, programmes and activities.

4. "A historical antecedent for such a 'double movement' was described in Polanyi's *The Great Transformation*, first published in 1944. In late 19th and early 20th centuries, economic transformation was inspired by a liberal market philosophy, while social protection initiatives emerged in response to the disruptive effects of the market on the community" (Jomo 2007:17).

This guide draws from various sources from the UN system, civil society and academia with the aim of explaining and helping to democratize complex economic policy debates. One of the lessons of the global economic crisis is that economic policy-makers cannot anymore hide behind obscure concepts and terminology to advise the public that "there is no alternative." There are plenty of alternatives, some of which can be drawn from recent economic history, and have been echoed by many dissident voices within civil society and the UN. These can help overcome what Richard Samans, Managing Director of the World Economic Forum, described as the "comparative amnesia" that has plagued mainstream global policy circles in the last two or three decades (when employment and other social objectives were carved out of the economic agenda).[5]

Many civil society constituencies not directly connected to the world of work are contributing in various ways to the decent work and fair globalization agenda, whether in the areas of finance, trade or social development. This guide aims to help determine whether they could gain leverage by connecting their advocacy strategies more explicitly with this new and highly demanding "standard of accountability" embodied in the global commitment to full productive employment and decent work for all.

DECENT WORK AND FAIR GLOBALIZATION GO HAND IN HAND

The concept of Decent Work grew out of deliberations at the ILO since 1999 to reframe labour and employment goals into four pillars. Namely, these are :

1. Full employment (including enterprise creation) ;
2. Respect for basic workers' rights ;
3. Social protection ; and
4. Social dialogue.

Decent work is not a uniform prescription applicable to all countries, but a development framework that can help shape social and economic strategies at national and international levels. However, the four pillars of decent work do represent universal goals and aspirations to create conditions for a dignified life. People at work need **rights** (especially rights of association and collective bargaining) to claim decent remuneration and working conditions ; but for that there has to also be enough productive **employment** and livelihood opportunities. People need **social protection** when they fall ill, reach old age, lose their job or source of livelihood. And people need voice to defend their rights – through peaceful demonstration when necessary ; around the negotiating table through **social dialogue** when possible.

In the face of growing social discontent with the evolution of the global economy, "global social dialogue" at the ILO soon made it clear that decent work objectives cannot be separated from progress towards a "fair globalization" – which would address global inequities, imbalances and asymmetries, as well as failed economic policies. The need to bring coherence of macroeconomic, trade and financial policies with development and social goals – especially decent work for all – was a central conclusion of the World Commission on the

5. Intervention at one of the thematic discussions during the Global Jobs Summit held in Geneva, June 2009.

Social Dimension of Globalization established by the ILO in 2002. The Commission also concluded that the current model of globalization has failed to meet people's basic and legitimate aspirations for a decent job and a future for their children. The imbalances are "morally unacceptable" and "politically unsustainable." [6]

DECENT WORK IS A HUMAN RIGHT

The decent work agenda is firmly rooted in the foundation of universal human rights. Former UN High Commissioner for Human Rights Mary Robinson noted that "sixty years ago, the drafters of the Universal Declaration of Human Rights knew that decent work was fundamental to their vision of a world where all human beings would be born equal in dignity and rights." [7] Article 23 of the Declaration is remarkably straightforward, in terms of the "right to work." Employment must be "freely chosen," under "just and favourable conditions" and equally giving right to "just and favourable remuneration," "protection against unemployment" and "to form and to join trade unions." The universal right to social security is clearly referred to in Article 22. In light of globalization and increased interdependence of national economies, implementation of these rights has to be all the more understood in conjunction with Article 28, which states that: "Everyone is entitled to a social and international order in which the rights and freedoms set forth in this Declaration can be fully realized."

Decent work-related rights were further elaborated in the International Covenant on Economic Social and Cultural Rights under Articles 6 to 11, and in ILO legal texts, including its core conventions captured in the 1999 ILO Declaration on Fundamental Principles and Rights at Work.

The human right to decent work has been neglected in both the development and human rights discourse, but this is beginning to change. Economic policy makers are not used to framing their policy choices in terms of which ones are in greater conformity with the human rights obligations of States. *A challenge for the human rights and decent work movement is to engage much more forcefully with the economics discourse in order to articulate human rights principles into specific economic policy and reform options*. The feminist economics discourse has been on the forefront of building this bridge (see Box 1.1).

THE GLOBAL DECENT WORK DEFICIT: A PRIMARY CAUSE OF THE GLOBAL ECONOMIC CRISIS

Mainstream media coverage of the causes of the world financial and economic crisis placed the emphasis on dysfunctions of poorly regulated global financial markets and the collapse of the US housing market. Increasingly, attention has been brought to underlying macroeconomic

6. The conclusions of the World Commission were politically all the more robust that they span the political spectrum with members ranging from Heads of the State from North and South to civil society activists and corporate executives. The Commission's final report, *A Fair Globalization: Creating Opportunities for All,* published in 2004 – and the ILO campaign that followed – were instrumental in building consensus around the new global commitments to decent work and a fair globalization adopted at the 2005 UN World Summit (ILO 2004a; Jenkins, Rodgers and Lee 2007).

7. "Working out of crisis: Aligning finance with decent work and a fair globalization," workshop organized by NGLS, ILO and Realizing Rights on 1 December 2008 as part of the UN Conference on Financing for Development, Doha.

BOX 1.1

FEMINIST ECONOMICS: ON THE FRONTLINE IN BRIDGING MACROECONOMICS AND HUMAN RIGHTS

In her contribution to a UN Development Forum on productive employment and decent work in May 2006, feminist economist Diane Elson noted that: "Macroeconomic policy has been increasingly characterized by 'deflationary bias,' with governments cutting expenditures and raising interest rates, reducing aggregate demand and stifling the growth of decent employment in both public and private sectors.... Feminist economics suggests that women are particularly likely to be disadvantaged by 'deflationary bias,' because it interacts with other biases, such as 'male breadwinner bias,' the assumption that men are more deserving of decent jobs because they are the principal economic support of families, while women's incomes are supplementary and not essential to family wellbeing. In fact, many women provide the principal economic support for families, and in many other families, women's earnings are critical for lifting families above the poverty line. Moreover, the right to work is equally a right of women and men, and non-discrimination in employment is one of the core labour standards set out in the ILO Declaration on Fundamental Principles and Rights at Work. To ensure gender equality, *both deflationary bias and male breadwinner bias need to be addressed*" (Elson 2007, emphasis added).

The need to address deflationary bias is a recurring theme throughout this NGLS guide.

More recently, Diane Elson and other feminist economists have developed the concept of "human rights auditing of economic policy" examining macroeconomic policies through the lens of human rights principles, including the right to decent work. Specific case studies so far include Mexico and the United States (Balakrishnan, Elson and Patel 2009).

causes, including global imbalances between large deficit and surplus countries but also growing income inequalities, which themselves are in great part an expression of the "*global decent work deficit*." Juan Somavia recently described the problems of persistent or growing unemployment (even during periods of high global growth), stagnant or declining real wages, and the increasing informalization of work (correlated with the number of working poor), as "*the crisis before the crisis*." [8]

Guy Ryder, General Secretary of the International Trade Union Confederation (ITUC), took stock of this "*crisis of distributive justice*" in the following terms: "We have seen decades of growing inequalities and distributive injustice within and between countries, where the share of national income going to labour relative to capital has declined to the levels of the 1930s: in effect, we got to the Great Depression even before this crisis hit, in terms of returns to labour." [9]

8. Statement to the High-Level Segment of the UNCTAD Public Symposium on "The Global Economic Crisis and Development – the Way Forward," 18-19 May 2009, Geneva.

9. "Working out of crisis: Aligning finance with decent work and a fair globalization," workshop organized by NGLS, ILO and Realizing Rights on 1 December 2008 as part of the UN Conference on Financing for Development, Doha.

At a lecture to the ILO Governing Body on 12 March 2009, Nobel Prize Laureate Joseph Stiglitz demonstrated how the global decent work deficit was one of the primary underlying causes of the crisis. The prevailing doctrine of deregulating labour markets as a path to full employment exercised a downward pressure on real wages, while the systematic weakening of social protection systems also weakened "automatic stabilizers."[10] "Over the past 30 years, we have been transferring money from the poor to the rich, from people who would spend the money to people who do not spend the money, and the result is weaker **aggregate demand**" – the total amount of goods and services that people and enterprises are willing and able to buy in the economy at a given time. In the aftermath of the East Asian crisis (1997-98), this *deficiency in global aggregate demand* was exacerbated by the legitimate self-insurance measures taken by developing countries through a build-up of reserves (foreign currency savings) as a precaution in case of future crises (see also Chapter 7).

Under these conditions, the global economic system was relying more than ever on the US market as the "consumer of last resort." But since the wages of the average American were also stagnant or declining in real terms, the only way to keep the system going was to engage (often through sophisticated financial instruments) in debt-driven consumer spending. The inherent unsustainability of the system eventually led the collapse of the US housing sub-prime mortgage market before spreading to the rest of the global financial and economic system.

IMPACT ON PEOPLE : UNEMPLOYMENT, POVERTY AND THE THREAT OF WAGE DEFLATION

The ILO estimates that by the end of 2009, some 34 million additional people were made unemployed relative to 2007 (most of it attributable to the crisis), meaning that global unemployment reached 212 million – the highest record ever. These figures do not include a large increase in the numbers of discouraged workers, those on involuntary part-time work or pushed into informal work. Although global job losses were on average gender neutral, women have been disproportionately affected with higher levels of unpaid work resulting from job or income losses within the household. Another ILO estimate suggests that more than 200 million workers, mostly in developing countries, were at risk of falling into poverty due to the crisis (ILO 2010). The World Bank, for its part, predicts that the crisis will push some 64 million people into poverty in 2010 (World Bank 2010).

In the face of the greatest economic catastrophe since the Great Depression, much attention has focused on avoiding a repeat of "*beggar-thy-neighbour*" policies of the type that prevailed during interwar period (an escalation of protectionist measures or competitive devaluations). But the ILO (backed by UNCTAD) points to an even more preoccupying risk that prolonged durably the Great Depression : the threat of generalized *wage deflation* (ILO/IILS 2009 ; UNCTAD 2009). Workers around the world are increasingly faced with the dilemma of losing their job or accepting a pay cut. Without support from the government, their employers often face the same dilemma : go broke or cut labour costs. What seems rational at the enterprise level could be self-defeating if the pattern becomes generalized, as more jobs would be lost as result of further contraction of global aggregate demand.

10. Already existing policies to stabilize consumption demand, such as progressive taxation or unemployment pay (see following chapter on establishing a social protection floor, as well as Annex I).

BOX 1.2

THE GLOBAL JOBS PACT : SOME HIGHLIGHTS

The Global Jobs Pact includes measures to :
- retain as far as possible people in employment and sustain enterprises, especially small, medium and micro-enterprises ;
- promote investments in employment intensive sectors, including green jobs and special support for agricultural employment in developing countries ;
- address wage deflation through social dialogue, collective bargaining and statutory or negotiated minimum wages that should be regularly reviewed and updated ;
- prevent a downward spiral in labour conditions, especially through increased respect for workers' basic rights to freedom of association and collective bargaining – and counter any efforts to use the crisis as an excuse to erode workers' fundamental rights ;
- strengthen existing social protection systems and build up a basic "social protection floor" in all countries, including through development assistance and budgetary support where needed ;
- act simultaneously on labour demand and labour supply, including by helping workers identify job opportunities and provide additional skills and training ;
- build a stronger, more globally consistent supervisory and regulatory framework for the financial sector so that it serves the real economy, promotes sustainable enterprises, decent work and better protects the savings and pensions of people ; and
- avoid protectionism while taking into account the varying development levels of countries in trade rules (policy space).

DECENT WORK AT THE HEART OF A SUCCESSFUL RECOVERY : THE GLOBAL JOBS PACT

In response to such widespread devastation and potential new threats, the ILO convened a Global Jobs Summit in June 2009 which adopted the **Global Jobs Pact**. The Pact outlines measures to reverse these trends, speed up recovery and lay the foundations for the transition to a socially and environmentally sustainable global economy. One objective is to significantly reduce the time lag between economic recovery and employment recovery. Without a much greater focus on jobs and social protection than contained in the initial stimulus packages, the ILO estimates that it could take up to five years to simply return to pre-crisis levels of unemployment – which themselves were already widely criticized as economically, socially and politically unsustainable.

The Pact combines a set of policy options and concerted actions to deal with both the crisis in global aggregate demand and with broader systemic deficiencies. Placing a "social floor" under the global economy is a key priority (see Box 1.2 and Chapter 3).

One of the key underlying objectives of the Pact is to increase the share of wages in national incomes, and the share of finance going to long-term productive investments, particularly for small and medium-sized enterprises where most of the new jobs are created. The task at hand is to mobilize the range of actions necessary to ensure that average wages and disposable incomes begin rising in line with productivity growth ; and to make finance serve the needs of people and the real economy rather than the other way around.

The Pact was referred to in the Outcome Document of the UN Conference on the World Financial and Economic Crisis and Its Impact on Development (June 2009); it was integrated in the coordinating work of the UN Economic and Social Council (July 2009); and was taken up at the September 2009 G-20 Summit in Pittsburgh (September 2009), which committed to adopt key elements of its general framework.

POLICY COHERENCE FOR DECENT WORK AND A FAIR GLOBALIZATION: BROADENING THE MOVEMENT

Now that decent work for all and a fair globalization have been identified as a global cross-cutting policy priority, it is essential to broaden the mobilization. The ILO's core constituency of workers, employers and labour ministries have long recognized that they cannot achieve these changes alone because the issues cut across ministerial portfolios and the mandates of international organizations. This is why considerable effort has been exerted in recent years to *integrate decent work into the broader multilateral system and into the MDG framework*, with particular efforts aimed at critical engagement with the international financial institutions (Jenkins, Rodgers and Lee 2007).

Employment and decent work have been identified as a strategic priority of the UN's Chief Executives Board for Coordination (CEB).[11] In 2007, the CEB asked the ILO to develop a "Toolkit for Mainstreaming Employment and Decent Work" across the multilateral system. The Toolkit aims to enable international organizations to determine how their policies, strategies, programmes and activities are interlinked with employment and decent work outcomes and how they can be enhanced.[12] In addition, the CEB has identified the Global Jobs Pact and the Social Protection Floor as two among its nine joint initiatives to address the global economic crisis.[13]

The Toolkit checklist approach has since been adapted for use by UN Country Teams.[14] The 2009 Guidelines for developing UN Development Assistance Frameworks (UNDAF) have incorporated the Toolkit to analyse the national context prior to the joint programming exercise (see example of Argentina in Box 1.3).

In addition, national tripartite constituents have been developing Decent Work Country Programmes with support from the ILO Office in a growing number of countries. These programmes identify local decent work priority areas, including national responses to globalization. The programmes aim to influence broader national poverty reduction and development frameworks, including Poverty Reduction Strategy Papers (PRSPs) financed by the international financial institutions and bilateral donors.

Initial evidence suggests that it is still an uphill battle to integrate meaningfully employment and decent work in PRSP-type frameworks and to change the orthodoxy of previous

11. The CEB regroups the secretariats of UN bodies, the Bretton Woods institutions and the WTO, and is chaired by the UN Secretary-General.

12. http://www.ilo.org/public/english/bureau/dgo/selecdoc/2008/toolkit.pdf.

13. "The promotion and enhancement of a coordinated response of the United Nations development system and the specialized agencies in the follow-up to and implementation of the Outcome of the UN Conference on the World Financial and Economic Crisis and Its Impact on Development," Report of the UN Secretary-General (E/2009/114).

14. http://www.ilo.org/public/english/bureau/pardev/download/toolkit_country_en.pdf.

structural adjustment programmes (SAPs) as far as the core macroeconomic and structural reform packages are concerned (ILO 2002; Jomo 2007). To change the development paradigm, national political leadership and the ability to mobilize different ministries, external partners and the broader civil society behind the decent work agenda is critical.[15]

The decent work and fair globalization agenda provides a timely opportunity to ***build synergies among various constituencies*** working across a broad range of complementary issues. These encompass: social development; pro-poor macroeconomic polices; international financial architecture reform; debt relief/cancellation; global taxation; trade justice; alternative development; human rights; gender equality; and many related issues. The following chapters examine how different entry points from these constituencies are essential components for decisive progress on the decent work and fair globalization agendas; and what are the specific policy options and challenges involved, especially in the wake of the global economic crisis.

BOX 1.3

MAINSTREAMING DECENT WORK IN ARGENTINA

When the first UNDAF for Argentina was being prepared in 2008, eight out of the 15 UN entities active in the country went through the Toolkit checklist to identify the links between their own activities and the Decent Work Agenda. A presentation was then made to demonstrate how decent work contributes to the achievement of the Millennium Development Goals. At the same time, FAO, UNAIDS, UNDP, UNESCO, UNFPA, UNICEF, UNHCR, WHO, the World Bank and ILO also went through the country-level checklist with Technical Assistance from the ILO focal point. The UNDAF was signed in May 2009 and will cover the period 2010-2014. The application of the Toolkit by the UN entities in Argentina contributed to a strong inclusion of employment and decent work in the UNDAF and programme outcomes.

UNDP representatives involved in the implementation of the Toolkit in Argentina have indicated that the Toolkit has helped organizations understand how their mandates, programmes and activities are related to decent work outcomes and that better results can be achieved by working in collaboration with other agencies. The Toolkit facilitates inter-agency work and helps to promote coherence at policy and operational levels.

Source: ILO EXREL/PARDEV October 2009, No. 6

15. NGLS participated in one original attempt to achieve this broader mobilization in the context of supporting a decent work approach to post-conflict reconstruction in Liberia (a high-level international forum organized by the Liberian presidency, the ILO and the NGO Realizing Rights in Monrovia, September 2009). See background paper for the Forum prepared by NGLS "A Decent Work Approach to Post-Conflict Reconstruction and Development in Liberia," available at: http://www.ilo.org/integration/events/events/lang--en/docName--WCMS_098106/index.

2. GLOBALIZATION AND EMPLOYMENT: A BROAD PERSPECTIVE

The recent phase of economic globalization, starting in earnest some two or three decades ago, has been characterized by rapid liberalization and expansion of trade and capital flows and a growing spread of global production networks, in conjunction with a major information and communication technology (ICT) revolution. The 2004 World Commission on the Social Dimension of Globalization highlighted the benefits that globalization could bring, if wisely managed, in terms of growing connectivity, exchange and productive capacity. But it also warned that in its current form, globalization had dramatically exacerbated existing problems of inequality within and between nations, generating a pervasive sense of insecurity and social fragmentation, and increasing the exposure of national economies to systemic risks and external economic shocks (ILO 2004a).

GROWING SOCIO-ECONOMIC INSECURITY AND LOW EMPLOYMENT-INTENSITY OF GROWTH

The global integration of labour markets in this context has been unprecedented in recent history. The total number of workers producing for international markets in goods alone more than doubled between 1980 and 2000 – from 300 million to 800 million (Akyüz 2006). Labour market turbulence provoked by trade liberalization, technological change, global production shifts and increased financial instability have aggravated insecurity among workers and enterprises in developed and developing countries alike. One immediate priority is to make a quantum leap in progress towards establishing a global "**social protection floor**." This will be addressed in the next chapter.

Besides growing socioeconomic insecurity, the deeper problem is that the global economy has been far from producing enough decent employment for all those willing and able to work. This applies especially for the fast growing number of young people entering the global workforce. The "*employment-intensity of growth*" has been weak – a tendency often referred to as "**jobless growth**." In 2004, for example, a year of robust global growth at 4 percent, the rate of global job growth was only at 1.7 percent. This was reflected at the national level, where in the United States for example, growth was at 4.4 percent, but job growth was only at 1.3 percent.[16] Moreover, official unemployment figures vastly underestimate the problem, leaving out not only those who have given up looking for work but also involuntarily working part-time, or working for a poverty wage in the informal economy. In the great majority of developing countries, the formal economy (where official

16. Source: ILO. This is reflected in average global growth between 1996-2006 at 4.1 percent per annum, in comparison to 1.6 percent employment growth over the same period, which meant that global unemployment stagnated at 6.2 - 6.3 percent, barely keeping up with the growth of the global workforce (ILO 2008a).

unemployment statistics exist) accounts for less than half of employment, and in large regions such as in Africa, for less than 10 percent (Jenkins, Rodgers and Lee 2007). The rest of people in the workforce are employed or self-employed in the informal economy, typically without legal protections and rights, and with earnings below the poverty line.

One perspective on the problem is that global economic integration is serving more to redistribute investment and jobs among countries than to accelerate job creation. Until the 2008 crisis hit, international trade and capital flows were growing much faster than global income and the world economy was allocating a smaller proportion of its income to fixed capital formation needed to generate more and better jobs. A growing share of income was directed at unproductive purposes, including speculation, regulatory arbitrage and financial services intermediation (UNCTAD 1997 ; Akyüz 2006 ; DESA 2008 ; ILO 2009c).

THE "GLOBAL" AT THE EXPENSE OF THE "LOCAL"

Another way to look at the problem is a tendency of the prevailing policy framework to favour "the global" – the global movement of goods and capital – at the expense of "the local" : policies aimed at nurturing and revitalizing local economies and societies, creating jobs where most people would like to stay if given a chance.

This was a core message of the 2004 World Commission on Social Dimension of Globalization. In presenting the Commission's report to the United Nations Economic and Social Council in June 2004, Juan Somavia emphasized : "***there can be no successful globalization without a successful localization.***" For example, when one refers to a "favourable investment climate" in international policy circles, the bias in favour of the global is so ingrained that it is usually understood as an enabling framework for foreign direct investment (FDI). Under the right conditions, foreign investments can bring important benefits such as know-how and technology transfer. However, these kinds of investments are not where the volume of work is being created. It is the myriad domestic small- and medium-sized enterprises, micro-enterprises, cooperatives and self-employment schemes which generate the bulk of employment worldwide. These must be supported and enabled to flourish, but may also require different enabling investment frameworks than those favouring foreign investors. In some cases, the two may even be at odds, for instance when particular foreign investments end up "crowding out" small domestic producers unable to compete at a given point in time (see Chapter 5).

PUTTING THE CART BEFORE THE HORSE ?

According to former UNCTAD chief macroeconomist Yilmaz Akyüz, at the heart of this problem is a major shortcoming in current approaches to international economic integration. Rather than aiming at full employment and expansion of productive capacities as a basis for increasing international trade and investment, the policy focus has emphasized liberalization and deep global economic integration as the way to deal with high unemployment and inadequate productive investment (Akyüz 2006). Many critiques of the current model have described this approach as "putting the cart before the horse" (for example emphasizing unilateral trade liberalization as the engine of productive growth, rather than productive investments as the main drivers of trade expansion).

The prevailing model stands in sharp contrast to the approach adopted by the architects of the post-World War II economic system which saw full employment, expansion of production and consumer demand as a necessary condition for closer economic integration.[17] This alternative approach to the current one is widely seen to have produced what many economists call the "Golden Age of Capitalism" (*les "trentes glorieuses"*) – which up till the mid-1970s was characterized by low levels of unemployment, steadily improving living conditions in the industrial economies and parts of the developing world as it was gaining independence, the strengthening of the welfare State ; and active public interventions designed to favour a virtuous pattern of growth whereby average real wages tended to rise in line with productivity growth (UNCTAD 1995 ; DESA 2008). This "*decent work link*" has been progressively lost since the 1980s.

The global economic crisis has generated much discussion on the need to find a better balance between domestic demand-led and export-led growth. This implies a shift in development strategies that should be aimed at boosting domestic productive capacities for local and regional markets while generating a steady rise in wages and incomes through productive employment generation (see Chapter 5). ILO research confirms that wage-led consumption growth has accounted for around two-thirds of overall growth in most regions of the world for most years in the past quarter century (ILO 2008a).[18]

There are many policy challenges involved in this change of course. Before we turn to the national and international measures needed to reduce job insecurity and expand productive employment opportunities, let us first focus on the need to place a social floor under the global economy. A "social protection floor," building on the existing body of human rights norms, would be an important step to upgrade current approaches to meet the MDGs, especially in view of the major setbacks caused by the global economic, food and climate crises.

17. For instance, the 1948 Havana Charter, which could have laid the foundation for an international trading system that would have integrated full employment and special conditions of developing countries, stated : *"The Members recognize that the avoidance of unemployment or underemployment, through the achievement and maintenance in each country of useful employment opportunities for those able and willing to work and of a large and steadily growing volume of production and effective demand for goods and services, is not of domestic concern alone, but is also a necessary condition for the achievement of… the expansion of international trade, and thus for the wellbeing of all other countries"(Chapter 2, Article II of the Charter).* The Charter, which would have established the International Trade Organization (ITO), was never adopted primarily because of opposition by the US Congress, but it did capture the prevailing approach of the time (Drache 1997).

18. See also the results of the UNCTAD Public Symposium on "the global economic crisis and development – the way forward" in *NGLS Roundup 137*, September 2009, http ://www.un-ngls.org/IMG/pdf_RU_137_PLACED12-2.pdf.

3. BUILDING A SOCIAL FLOOR UNDER THE GLOBAL ECONOMY

Even before the food and financial crises hit in 2008, there were alarming figures showing that the world was much further behind in meeting the MDGs than previously assumed.[19] A change of policy directions is all the more urgently required and a good starting point is from the perspective of ordinary people. From that angle, Juan Somavia has noted that it is an "aberration" to measure progress simply because there might be some statistical movement in the number of people that live on US$1/day to US$2/day: this is not how people define their goals and aspirations in life. The measure is rather in terms of their prospect of securing a decent job or livelihood and a future for their children. An immediate priority is ***a social floor that can prevent people from falling into destitution*** and help them move up the social and economic ladder.

"Everyone, as a member of society, has the right to social security" states Article 22 of the Universal Declaration on Human Rights. Yet, some 80 percent of the world's working women and men have little or no social protection.[20] To many people, a basic set of social benefits could make the difference between a liveable and a miserable life, or even the difference between life and premature death. Even in countries with long-established social protection systems, many workers are not fully covered for essential health care, old age and contingencies such as unemployment and sickness – a trend that is expanding with the proliferation of casual and part-time work especially for youth. In fact, over the past 15 years, social transfers as a percentage of gross domestic product (GDP) have declined on average in developed countries (Prasad 2008).

Social protection is a powerful tool to alleviate poverty and inequality. It has reduced poverty and mitigated inequality in many countries of the Organisation for Economic and Co-operation Development (OECD) by almost 50 percent. There are good and positive examples of successes with modest universal social benefit systems in Africa, Latin America and Asia (see below). But investing in social security has not yet become a widely accepted development strategy.

SOCIAL PROTECTION AS AN ECONOMIC INVESTMENT

Why have the stabilization of social security, or the introduction of at least basic social protection systems, not played a bigger role in economic and development policies? Or worse, why have they been downgraded in a number of countries?

19. The global food, fuel and financial crises have caused a major setback on progress towards meeting the MDGs. However, even before their manifestation, the World Bank had issued new revised estimates suggesting that extreme poverty in the developing world is much more pervasive than previously assumed (Chen and Ravallion 2008).

20. In ILO terminology, social protection and social security tend to be used interchangeably, although social protection is usually understood as broader than social security.

The most common argument against extending social security is its economic cost. In a nutshell: a large welfare State is not compatible with a competitive economy; and social protection expenditures are too expensive for developing countries. Furthermore, limited resources are best invested in more productive endeavours.

In response to the competitiveness argument, studies show that there is a fairly strong correlation between per hour productivity and per capita expenditure on social protection in OECD countries. The OECD now argues that some of the most successful open economies are also the ones with the most extensive welfare States (ILO 2008c).

Social equity and economic efficiency are not necessarily contradictory. Quite the opposite: ***social protection systems are an economic investment***. In particular, social protection plays an essential stabilizing (or "counter-cyclical") role during an economic downturn or financial crisis by maintaining some degree of effective demand in the economy, thus helping domestic businesses to stay afloat. ILO studies had already suggested that the social and economic impact of the 1997-98 East Asian crisis would have been much less severe had countries adequately invested in social protection schemes. Argentina's much quicker than expected recovery from its 2001-03 crisis is partly attributed to the *Plan Jefas y Jefes de Hogar Desocupados*, which was introduced in the wake of the crisis to provide basic income to unemployed households in exchange for public utility work (see Box 3.2).

In addition, well-designed social protection schemes can help ensure that children are more adequately nourished and get a basic education and, combined with active labour market policies (such as training and job-search assistance), boost the chances of people finding a job and being "employable." Social protection can also serve to play other functions not directly related to decent work such as providing some cushion against food price hikes or climate change-related disasters (an element of climate change adaptation).

ELEMENTS OF A SOCIAL PROTECTION FLOOR

The shift in perspective regarding social protection – from cost to investment – needs to be accompanied by a change in paradigm, from "exclusive protection," which covers only civil servants and formal economy private sector employees, to "progressive universalism" covering all population groups, including the poorest in the informal economy (Jomo 2007). World Bank research showed that universal approaches are the most efficient, as targeted approaches risk excluding as much as three-quarters of potential beneficiaries (ILO 2009a). In order to be non-exclusive (to reach out to workers in the informal economy), many argue that social protection schemes should be "non-contributory" (meaning not financed through insurance schemes but fiscal transfers).

The crisis also brought into sharp relief the limitations of private social insurance, especially privatized pension schemes, which have recorded substantial losses with the collapse of capital markets. Well-designed public pension systems have been much less affected. This has motivated a policy shift in the stance of certain international organizations which now advocate greater focus on more stable, security-oriented public pension systems (ILO/IILS 2009).

The exact definition of a **social protection floor** will vary from country to country, but it is generally understood that it would include the four following components:
- Basic health care for all;
- Child benefits conditional on schooling;

- Self-selected targeted social assistance; and
- Universal benefits for the elderly, the disabled, and in the event of loss of the household breadwinner.[21]

CASH TRANSFERS AND EMPLOYMENT GUARANTEES

In the wake of the crisis, much attention has focused on the effectiveness of cash transfers and employment guarantee schemes. **Cash transfer schemes** are defined as regular non-contributory payments of money provided by government or non-government organizations to individuals or households, with the objective of decreasing chronic or shock-induced poverty, addressing social risks and reducing economic vulnerability. They can be unconditional, or subject to conditions such as sending children to school. Today, almost 200 million people are covered by such schemes in 25 developing countries. The impact of cash transfer schemes is well illustrated by the success of Mexico's *Oportunidades* and Brazil's *Bolsa Família* (see Box 3.1), which have reduced poverty substantially. Evaluations find that between the mid-1990s and the mid-2000s, these programmes were responsible for a 21 percent reduction in income inequality in Brazil and Mexico, and constituted 50 and 25 percent of incomes of the poorest households, respectively (ILO 2009b).

Employment guarantee schemes have elements in common with the idea that the State should act as an "employer of last resort," to provide employment at a basic wage for those who cannot otherwise find work. This should be seen not only as an emergency measure

BOX 3.1

THE BOLSA-FAMÍLIA PROGRAMME IN BRAZIL

Introduced in 2003, the *Bolsa-Família* Programme consists of a conditional cash transfer to families of up to a maximum of US$60 per month, requiring children's regular school attendance and regular health visits for the whole family. In 2006, over 11 million household benefits were disbursed through this scheme. Between 2003 and 2006, the poorest decile in household survey data rose by 10 percent while the richest grew at lower rates, suggesting a positive contribution of the scheme to reducing poverty and inequality. The cost of the programme amounted to 0.3 percent of GDP which had been financed out of revenue earmarked for social security. In recent years the availability of funds was strengthened by the positive results of the public service pension reform in 2003 and (for some time) the proceeds of a tax on financial transactions, fixed at 0.38 percent. According to the Ministry of Social Security of Brazil, the tax did not have the negative economic consequences its detractors had warned of when it was first introduced. One key challenge, the Ministry notes, is to achieve the institutionalization of the *Bolsa Família* as a State policy to ensure its continued existence beyond the current government (ILO 2008c).

---

21. The ILO with WHO and other development partners developed a manual to provide guidance for a Social Protection Floor Approach at country level. The manual gives an overview of steps to take and tools to use for country operations of UN agencies and other institutions that might want to join Social Protection Floor initiatives on a local level. The manual offers a checklist for possible country activities rather than a prescription for action.
See: http://www.socialsecurityextension.org/gimi/gess/ShowNews.do?nid=6043.

in times of crisis but a permanent complement to private sector employment (Wray 2007). The Jefas Plan in Argentina is often cited as an example[22] (see Box 3.2). A more institutionalized example is India's National Rural Employment Guarantee (NREG) Act, which was adopted by the Indian Parliament in 2005 and came into effect in April 2006. The Act provides mandatory assurance of at least 100 days of public employment every year at the minimum wage, for at least one person in every rural household. The budget for the NREG in 2006-2007 was 0.3 percent of GDP. The scheme is expected to cover the entire country within five years (ILO 2008c; ILO/IILS 2009). Civil society movements in the country are playing an important role in pressing for the NREG's faster implementation, ensuring knowledge of the scheme is spread to the most remote areas, and contributing to improving the quality of delivery, in terms of responding to local needs and promoting greater transparency and accountability (Centre for Environment Concerns 2009).

BOX 3.2

THE *PLAN JEFAS Y JEFES DE HOGAR DESOCUPADOS* IN ARGENTINA

The *Plan Jefas y Jefes de Hogar Desocupados* (hereafter the "Jefas Plan") was introduced by Presidential decree in early 2002, in the midst of Argentina's 2001-2003 financial and economic crisis and signed into law in April of that year. The Jefas Plan paid 150 pesos (~US$50) per month to a household head for a minimum of four daily hours of public utility work. This corresponded to half the sum needed to stay above the poverty line, so participants were expected to search for additional hours of work. At its peak, the programme provided work for 2 million people or 5 percent of the population and 13 percent of the workforce within just a few months of its creation. Peak spending on the programme amounted to about 1 percent of GDP. The "multiplier effects" resulting from the boost in aggregate demand were estimated to be about 2.5 percent of GDP. More recently as the economy recovered, the Plan has been redesigned in a "Families for Social Inclusion" programme to support unemployed female-headed households (most of the beneficiaries of the Plan) and a Training and Employment Insurance Scheme for the unemployed having difficulties in finding formal employment (Novick, et al 2007; Wray 2007).

A UNIVERSAL BASIC INCOME GUARANTEE?

The ILO has also raised the question as to whether a basic minimum income – essentially a regular and unconditional cash grant from the State – could become an unconditional right of all citizens (ILO 2004b). Many civil society movements have been actively campaigning for this right, including in the context of Namibia where a coalition of civil society organizations implemented a pilot Basic Income Grant (BIG), a proposal emanating from a commission appointed by the Government of Namibia. The results of the initiative produced very high social and economic returns in the pilot area in a short period of time. The coalition argues it is affordable to implement BIG on a national scale (see Box 3.3).

---

22. It should be noted that this emergency programme has since been transformed into more conventional models of social protection and active labour market policy.

BOX 3.3

THE BASIC INCOME GRANT (BIG) PILOT PROJECT IN NAMIBIA

The original proposal for a Basic Income Grant in Namibia was made in 2002 by the Namibian Tax Consortium (NAMTAX), a commission appointed by the government to review the tax system in Namibia. The Basic Income Grant in Namibia was conceived as a monthly cash grant of not less than N$100 (~US$13) which should be paid to every Namibian citizen as a citizen's right. Every Namibian, regardless of age or income, would receive such a grant until the age of 60, after which he/she would be eligible to the existing universal State Old Age Pension of N$370. The money paid to people not in need or not in poverty would be recuperated through adjustments in the tax system.

In 2007, a Basic Income Grant (BIG) Coalition of civil society organizations decided to implement a pilot BIG project, in order to demonstrate the impact of a BIG in practice. Since the introduction of the BIG, household poverty has dropped significantly in the pilot area. The proportion of residents living below the food poverty line fell from 76 percent to 37 percent within one year of the BIG. Child malnutrition was reduced within a year of implementation from 42 percent to 10 percent. The positive economic spin-offs in terms of increased economic activity were considerable. The average per capita income in the pilot area increased from N$160 to N$303, far exceeding the value of the BIG. The rate of those engaged in income-generating activities increased from 44 percent to 55 percent. The grant enabled recipients to increase their productive income earned, particularly through starting their own small business, sustained by increased buying power in the area.

Based on econometric analysis, the BIG Coalition has put forward a number of options to fund BIG on a national scale, which would amount to between 2.2 percent to 3 percent of Namibia's GDP. These include reprioritization of the national budget or increasing the current tax collection rate to its full capacity, which itself, the Coalition affirms, would be more than enough to cover the net costs of BIG (Prove 2009).

HOW MUCH DOES BASIC SOCIAL PROTECTION COST ? IS IT AFFORDABLE ?

According to ILO calculations, less than 2 percent of global GDP would be necessary to provide a basic set of social security benefits for all the world's poor (ILO 2008b). Some estimates suggest the cost of a basic package of social transfers would amount to between 1 and 4 percent of GDP in developing countries (ILO 2009a). These might be higher in some cases, depending on the measures and assumptions used. Box 3.4 presents the results of various cost simulations, which suggest that a basic social protection package could be affordable in some developing countries, provided there is enough political will to significantly increase the share of public spending attributed to social protection. But for others, even a significant increase (of 20 percent) would not even cover a third of the projected costs in 2010.

Therefore, even if domestic political will is strong, many developing countries would still need substantial budget support to kick-start meaningful social protection schemes, as called for in the Global Jobs Pact. Some donors are starting to see the pay-off, but there is still a long way to go in mainstreaming social protection in development debate and policy.

THE FISCAL SPACE CHALLENGE

These calculations pre-date the global economic crisis and its catastrophic impact on the fiscal space available to developing countries. There is potential in expanding the domestic tax base and the progressivity of tax structures in most jurisdictions, but these may face limitations in the absence of significant international action. The recent phase of financial globalization has coincided with intensified tax competition, a "*race to the bottom*" that makes progressive taxation on mobile capital much more difficult. At the same time, widespread trade liberalization has been causing very significant tariff revenue losses in developing countries not recouped from other sources. These phenomena are draining public resources at precisely the time when greater fiscal revenue is most needed to buffer the intensified social dislocations associated with globalization.

We will return to the issue of international taxation in Chapter 7. But first, let us examine how macroeconomic policies can be made more employment-oriented (that is, contribute to more employment-intensive patterns of growth) in the context of crisis recovery.

BOX 3.4

THE COST OF A SOCIAL PROTECTION FLOOR : SOME PROJECTIONS

The ILO (2008b) has undertaken two different sets of simulations of costs and affordability of a basic social protection package in a representative sample of African and Asian developing countries. These were in Africa: Burkina Faso, Cameroon, Ethiopia, Guinea, Kenya, Senegal, United Republic of Tanzania; and in Asia: Bangladesh, India, Nepal, Pakistan and Viet Nam.

The first simulation set looks at individual elements of a basic social protection package as follows:

Social protection component:	**Cost as a percentage of GDP in 2010 depending on country specificities**
Universal basic old-age and disability pensions	Between 0.6 and 1.5 percent
Basic universal child benefits	Between 1.2 and 3.6 percent
Universal access to essential health care	Between 1.5 and 5.5 percent
Social Assistance/100 day employment scheme	Between 0.3 and 0.8 percent

The second simulation set looks at an overall package composed of universal cash benefits and access to health care that would cost between 3.7 percent and 10.6 percent of GDP in 2010 depending on country specificities under two scenarios:

Scenario 1: Status quo (share of public expenditure devoted to basic social protection remains constant) →	**Share of total basic social protection costs covered by existing allocated resources:** Between 4 percent and 25 percent depending on country specificities
Scenario 2: Policy change (spending levels increase to 20 percent of government expenditure) →	**Share of total basic social protection costs covered by increased allocated resources:** Between 30 percent and 100 percent depending on country specificities

4. MACROECONOMIC POLICIES FOR DECENT WORK

The June 2009 UN Conference on the world financial and economic crisis committed "...to work in solidarity on a coordinated and comprehensive global response to the crisis and undertake actions aimed at, *inter alia*, restoring confidence and economic growth and creating full and productive employment and decent work for all...." [23] Later, the G-20 Summit in Pittsburgh in September 2009 decided to "put quality jobs at the heart of the recovery," and agreed on "the importance of building an employment-oriented framework for future economic growth."

There are several dimensions to re-integrating employment objectives into macroeconomic policies. These include **fiscal** and **monetary policies**, as well as supporting **sectoral policies** (targeting particular sectors of the economy, often referred to as "industrial policy"). Fiscal policies comprise both public revenues and expenditure as expressed in the government budget. Fiscal policy is typically the province of the ministry of finance or treasury, which thus tends to have ascendancy over other ministries, whether related to labour and social protection, health or the environment. Monetary policy includes policy on interest rates, exchange rates and money supply, and the regulation of the financial sector. Monetary policy is primarily the responsibility of the central bank, which is now most often an independent body, whose degree of democratic accountability to the public is often raised as a major concern with respect to meeting growth and employment goals.

THE FORGOTTEN LESSONS OF THE GREAT DEPRESSION

The prevailing doctrines of "sound" macroeconomic policies (sometimes referred to as "**orthodox**," "**neoliberal**" or "**Washington Consensus**" policies, which include objectives such as limited public intervention in the market, low or zero budget deficits, an exclusive focus of monetary policy on consumer price stability) have been seriously challenged in the wake of the global economic crisis. One of the most important lessons of the Great Depression was that markets are not self-correcting and that government intervention is required to ensure recovery ("**counter-cyclical**" measures). In the aftermath of the 1930s crisis, governments introduced policies that provided automatic stabilizers for aggregate demand and implemented context-specific policy frameworks to reduce economic instability and promote full employment (so-called "**Keynesian**" or "**heterodox**" policies).

Since the 1980s and 1990s, the confidence in the self-stabilizing nature of the market returned, even though it had been challenged with the increased frequency of crises in developing countries the 1990s, especially the East Asian crisis of 1997-98 (UN 2009). The global crisis triggered in September 2008 was different in that it originated in the more advanced

23. Paragraph 11 of the Outcome Document on the United Nations Conference on the World Financial and Economic Crisis and Its Impact on Development.

industrialized countries, and that even governments who were outright opposed to Keynesian-type policies had little choice but to implement them on a scale never witnessed in economic history.

STRENGTHENING THE EMPLOYMENT AND DECENT WORK CONTENT OF STIMULUS PACKAGES

However, the amounts spent on rescuing the financial sector ("bailouts") have far surpassed fiscal stimulus packages directed at the real economy.[24] The ILO has argued that fiscal stimulus packages should be much more focused on employment and social protection. Looking at some 40 stimulus packages announced and implemented by governments as of early 2009, the ILO concluded that on average, direct transfers to low-income households and employment measures constitute the two smallest components – at 9.2 percent and 1.8 percent respectively. Yet, the analysis found that *the greater the employment orientation of the measures, the stronger the stimulus for the real economy.* In particular, the multiplier effects of investments in employment-intensive areas, including infrastructure, is higher than with alternative measures such as tax cuts (ILO/IILS 2009).

In another survey undertaken for the G-20 Summit in Pittsburgh, the ILO finds that where decent work-related measures have been taken, they did make a difference, even though these only managed to limit some of the damage and much more ambitious measures are needed to reduce the time lag between economic recovery and employment recovery (ILO 2009b).

"PRO-CYCLICAL" IMF CONDITIONALITIES ?

A number of emerging market economies have been in a position to implement stimulus packages, but the majority of developing countries and some transition economies are confronted with major fiscal space constraints in trying to implement counter-cyclical measures. To receive emergency lending, many have little choice but to turn to the International Monetary Fund (IMF), whose lending capacity has been significantly strengthened as a result of the April 2009 G-20 London Summit decision to triple its resource base (from US$250 billion to US$750 billion). The IMF has announced that it has drawn lessons from the East Asian crisis, when its emergency lending was tied to **"pro-cyclical" policies** (such as fiscal tightening and higher interest rates) that led borrowing countries into even deeper crisis, causing massive job losses that could have been avoided. Its official position now is that coordinated countercyclical policies and large fiscal stimulus packages are the most effective means to compensate for the fall in aggregate demand (IMF 2009).

This new position is applied in some countries that received IMF lending through its new Flexible Credit Line, where the Fund permitted the easing of monetary and fiscal policies

24. The stimulus package in the United States of US$787 billion, while still smaller than the financial rescue package (which many estimate at above US$1 trillion) was proportionally much higher than in other developed countries. It has been argued that the much weaker automatic stabilizers (social protection systems) in the United States as compared with European countries may explain at least partly why a much higher stimulus package was deemed necessary. In addition, unlike the United States, Europe's Stability and Growth Pact places very strict limits on the amount of deficit spending allowed for Eurozone member countries. These strict criteria were broken in the face of the crisis by virtually all members, but it has been argued that they may have acted as a brake on the amount of deficit spending for the various national stimulus packages in the Eurozone.

to fight the recession (Columbia, Mexico and Poland). However, according to a number of UN and civil society sources, the same pro-cyclical stabilization and adjustment policies (reducing public spending, raising interest rates) are binding conditions for crisis-response IMF lending in a sizeable number of other countries in real need of emergency funds (see examples and references in Box 4.1). Nuria Molina of the European Network on Debt and Development (Eurodad) commented in this regard that:

> "Despite making commitments at the G-20 to follow the principles of the Global Jobs Pact concluded at the 2009 ILO Conference by implementing expansionary fiscal policies and the safeguarding and re-enforcement of social protection and decent work, rich countries who control the IMF are still allowing it to impose conditions leaving developing and transition country governments unable to follow these principles of recovery." [25]

BOX 4.1

SOME CRITICAL STUDIES OF IMF PRO-CYCLICAL CRISIS RESPONSE LENDING

Several studies by civil society organizations that have examined fiscal and monetary targets in recent IMF loan programmes find that the Fund has also continued to impose pro-cyclical macroeconomic tightening in almost all recent lending arrangements with developing countries (ActionAid and Bank Information Center 2008; CEPR 2009; TWN, 2009). For example, in the IMF programmes for São Tomé and Principe, and Senegal the target is to bring fiscal deficits down to below 3 percent of GDP, to be achieved through spending cuts where necessary. In Côte d'Ivoire and Ethiopia, the targets for 2009 are even more stringent, below 2 percent of GDP. In Côte d'Ivoire, Malawi and the Congo, the IMF programmes aim to reduce inflation to below 5 percent in the midst of the current crisis (Molina-Gallart 2009).

UNCTAD also documents similar findings. For example, Pakistan had to tighten both its fiscal and monetary policy, including drastically reducing its fiscal deficit from 7.4 percent of GDP in 2008 to 4.2 percent of GDP in 2009. In the stand-by agreement with Ukraine, approved in November 2008, the initial objective was to achieve a balanced budget, even though GDP was projected to fall by more than 10 percent in 2009 and gross public debt was very low. However, in May 2009, the IMF was obliged to accept a loosening of fiscal policy and allow a fiscal deficit of 4 percent of GDP in light of the continued weakening of economic activity, which could have been expected at the outset. Belarus, Georgia, Hungary, Latvia and Serbia have all signed IMF agreements that require very restrictive fiscal policies, which could exacerbate these countries' economic downturns (UNCTAD 2009).

Similarly, DESA notes that "despite pronounced intentions, many recent IMF country programmes contain pro-cyclical conditions that can unnecessarily exacerbate an economic downturn in a number of developing countries" (DESA 2010:99).

25. "Doing a Decent Job? A New Report on the IMF Shows a Leopard who Cannot Change its Spots." Joint press release by SOLIDAR and Eurodad, Brussels/Istanbul, 5 October 2009.

The ILO tripartite constituency took up these issues with IMF Managing Director Dominique Strauss-Khan at the March 2009 session of the ILO Governing Body. Workers' representatives expressed concern with the pro-cyclical policies that the IMF applied in a number of countries seeking financial assistance in the crisis. Mr. Strauss-Khan explained that his institution is in favour of a "global stimulus," which means promoting counter-cyclical stimulus packages "where possible" – that is in countries that are in a fiscal position to do so. For those countries that do not have their public finances in order, the IMF supports fiscal and monetary measures that must first and foremost reassure foreign investors so as to avoid massive withdrawal of external private funds. One important difference from the way the IMF handled the East Asian crisis, he added, is now the IMF insistence on social "safety nets" to protect the most vulnerable in the midst of adjustment. [26]

This would suggest that in such situations, the prevailing priority is to reassure foreign investors even if it is at the expense of domestic enterprises, workers and aggregate demand. This raises a number of questions : insofar as capital outflows are a problem, do policies such as interest rate hikes that worsen the recession ultimately reassure foreign investors, or *de facto* have the opposite effect ? Are these dilemmas linked to currency speculation (the trading of currencies to make profit) ? Are there other means to limit capital outflows in the midst of a crisis ? Could "**capital management techniques**" (combining prudential regulation and capital controls) play a role in taming capital movements that undermine employment and decent work objectives ?

Before addressing these questions, it would be useful to better understand the impact of widespread financial liberalization on growth, employment, income distribution and policy space.

IMPACTS OF FINANCIAL LIBERALIZATION

Many voices have argued that one of the most problematic dimensions of globalization has been the increasing unpredictability (volatility) of capital movements resulting from widespread financial liberalization around the world. This includes measures to free the cross-border movement of capital through **opening up the capital account**. In many developing countries, these policies were applied as part of the stabilization and adjustment policies which marked the 1980s and 1990s (UNCTAD 1998 ; NGLS 2000).

The major expected result from financial liberalization was that it would allow countries to achieve greater economic growth and stability through more efficient allocation of capital. What is the record ?

Impact on growth and employment : As explained in more detail in Chapter 5, a good measure of whether investments are supportive of job creation is whether investments are directed at increasing **productive capacities** (including investments in new equipments and infrastructure). However, the surge in international capital flows in the 1990s pursuant to financial liberalization did not bring the expected growth benefits : actual investment as a percentage of GDP into new infrastructure and productive capacity stagnated. Gross fixed

26. See broadcast : "IMF Managing-Director, Dominique Strauss-Kahn addresses ILO's Governing Body on responses to the current global financial and economic crisis," 23 March 2009 in Geneva, on : http ://www.ilo.org/global/About_the_ILO/Media_and_public_information/Broadcast_materials/B-rolls/lang--en/docName--WCMS_103998/index.htm.

capital formation (the most commonly used measure for physical investment) as a percentage of GDP was actually lower on average than in the 1980s and 1970s (Van Der Hoeven and Lübker 2007).

How can one explain the divergence between the speedy growth of capital flows and stagnating productive investments? Many have attributed this discrepancy to capital being allocated to intensified financial intermediation (that can generate very high profits without in itself producing value-added in the real economy); and the fact that much foreign direct investments (FDI) was spent on mergers and acquisitions (companies that merge or are taken over by other companies) rather than into new factories that would generate new jobs (UNCTAD 1998; UNCTAD 2004; Van Der Hoeven and Lübker 2007).

Impact on stability and employment: Worse, this period of financial liberalization was associated with a sharp rise in financial instability and the frequency of disastrous financial crises, especially in developing countries. As also evidenced in the current global crisis, *labour is disproportionately affected* by crises, not only in terms of mass unemployment, but through a permanent deterioration of wages – even when previous employment levels are recouped after the significant time period between economic recovery and job recovery (UNCTAD 1998; Van Der Hoeven and Lübker 2007).

Impact on inequality: A less talked about consequence of capital account liberalization is its contribution to *growing income inequality*. Several extensive cross-country studies have shown robust correlations between capital account openness and inequality, whether measured in terms of the Gini coefficient,[27] or income shares between labour and capital. The most telling measure is that in most cases, there is a consistent correlation between capital account liberalization and significant declines in the share of national income going to labour (wages) vis-à-vis capital. Falling labour shares is evidenced in both developed and developing countries and is persistent over time (studies cited and further developed in Kang-kook and Jayadev 2005).

These negative trends are in great part explained by the fact that the potential for greater mobility of capital reduces the bargaining power of even organized labour to claim a fair share of the benefits of growth. This new phenomenon suggests that, while a great deal of effort needs to go into restoring or extending basic workers rights of association and collective bargaining as part of worldwide efforts to reverse inequality, it may in itself not be enough.[28] These new asymmetries generated by financial globalization need to be factored into the broader decent work strategy.

Impact on policy space: Of equal concern is the impact of capital mobility (or the **threat of capital flight**) on the ability of national governments to introduce socially desirable policies (**policy space**). Heterodox economist Gerald Epstein (2005:6-7), for instance, noted that:

27. The Gini coefficient is a statistical measure for income inequality on a ratio from zero to one (the closer to one the higher the inequality).

28. A recent study in over 50 countries finds that trade unionism and collective bargaining is less effective than in the past at countering inequality. This may be accounted for by the greater role played by factors such as technological changes and the "inequality increasing effects" of greater shares of FDI in national income (Baccaro 2008).

> "[C]apital flight can be a powerful weapon against government policies that threaten the wealth or the prerogatives of the rich. In this role, capital flight has sometimes been called 'capital strike' evoking the idea that capital ... goes on strike against undesired taxation or regulatory policies.... What if the government simply wants to lower interest rates to achieve full employment and wealth holders flee? Is that capital flight or a harmless portfolio decision? What impact will such 'capital movements' have on the ability of governments to make economic policy?"

Another consequence of financial liberalization in developing countries is the significant *build-up of reserves* as a cushion against future crises. This intensifies the "*deflationary bias*" in the current global reserve system that is inconsistent with global full employment. This issue will be addressed in more detail in Chapter 7.

CAPITAL MANAGEMENT FOR EMPLOYMENT AND DECENT WORK

From a human rights perspective, governments have a **duty to protect** the right to work by preventing as much as possible financial instability and crises that lead to the unnecessary destruction of jobs and often permanent deterioration of average wages. They also have a **duty to fulfil** decent work-related human rights, notably through regulating finance in a manner that will maximize productive employment creation. "**Capital management techniques**" can play an essential role on both fronts. They include the flexible and dynamic use of two broad categories of policy options:

- **Capital controls** (managing the flows of capital in and out of the country) and
- **Prudential regulation** (of domestic financial institutions).

These two policy categories are often discussed separately, with prudential regulation being much more accepted in mainstream policy circles than capital controls. However, both sets of policies are needed to be effective and they are mutually reinforcing. They are needed first of all to put an end to the "*boom and bust*" policies of the last two decades, which have been a prime cause of growing socioeconomic insecurity, mass unemployment and income inequality (DESA 2008). They can promote financial stability through their ability to reduce currency flight, fragility and "*contagion risks*" involving the spread of financial crises from one country to another. For instance, capital controls can reduce capital inflows when these are driven by the short-termist "*herd behaviour*" of portfolio investors (that leads to a speculative boom), or limit a "*panic exit*" of capital when the boom turns to bust.

Likewise, when a potential speculative asset bubble is in the horizon, prudential regulation can raise the cost of investing in high risk assets by increasing the capital requirements attached to these assets. **Capital requirements** are the amount of reserves financial institutions have to set aside proportionally to their lending. The higher the reserves required to gamble on very risky speculative investments the less "**leverage**" the institutions have, so the less profitable it is to continue such investments (UNCTAD 1998; DESA 2008; Epstein, Grabel and Jomo 2005).

A key question is the approach taken to prudential financial regulation: should it be based on the principle that "*everything is allowed unless explicitly forbidden*" (the preferred approach in private financial circles)? Or should the guiding principle be that "*everything is forbidden unless explicitly approved*" (the approach used for example to prevent the market-

ing of toxic foods and medicines)? The latter approach is criticised its effects on slowing "financial innovation," but the question involves determining the economic and social usefulness of the many new financial products developed in recent years. The second approach limits the ability of financial innovation to always be ahead of regulators (to bypass regulation), especially if it is complemented with the principle of simplicity: *new financial products should be easy to understand in terms of their risks for the general public.*

The right of countries to use capital controls to complement enhanced and coordinated prudential regulation was a cross-cutting priority in the global civil society consultation that NGLS undertook in early 2009 for the Commission of Experts of the President of the UN General Assembly on Reforms of the International Financial and Monetary System – hereafter referred to as the "*Stiglitz Commission*." That "*governments should have the space to undertake capital account management techniques*" was a prominent feature in the final recommendations of the Stiglitz Commission (UN 2009:81; NGLS 2009a).

Although the mainstream policy thrust of the last two or three decades has been actively pursuing capital account liberalization, the IMF's founding Articles of Agreements actually permit its members to exercise capital controls as is necessary to regulate international capital movements (Article VI.3).[29] The international consensus reached at the June 2009 UN Conference on the world economic and financial crisis in this regard states that: "*Developing countries facing an acute and severe shortage of foreign reserves because of the fallout of the crisis…should not be denied the right to…, as a last resort, impose temporary capital restrictions…in order to help mitigate the adverse impacts of the crisis and stabilize macroeconomic developments.*"[30]

Box 4.2 provides an illustration of how capital controls were used by Malaysia to limit the effects of the 1997-98 East Asian financial crisis from spreading to the real economy and provide policy space for counter-cyclical measures.

Cross-country analysis suggests that capital management techniques can promote socially desirable types of investment and financing strategies (that are employment intensive, long-term, stable and sustainable) by rewarding investors and borrowers for engaging in them (the "duty to fulfil"). Conversely, they can be used to discourage less socially useful or socially harmful investments by increasing their cost or precluding them altogether (Epstein, Grabel and Jomo 2005).[31]

The global financial crisis has dramatically shifted political momentum in favour of re-regulating the financial sector. However, one major obstacle identified notably by civil society organizations and the Stiglitz Commission is the proliferation of trade and investment agreements that legally prevent governments from re-regulating the financial sector and introducing capital management techniques (see Chapter 6).

---

29. More recently, IMF Managing Director Dominique Strauss-Khan indicated that "there is no reason to believe that no kind of control is always the best kind of situation." "IMF refuses to rule out use of capital controls" in *Financial Times*, 2 November 2009.

30. Paragraph 15 of the Conference Outcome Document.

31. Capital management techniques work best over long periods in the presence of strong "fundamentals" – such as a low debt ratio, moderate inflation, sustainable current account and fiscal balances, consistent exchange rate policies, administrative capacity of the public sector to implement coherent policies, and a government able to maintain independence from narrow political interests and to maintain some control over the financial sector. But conversely, capital management techniques can also help enhance fundamentals, so the causation works both ways. Capital management can certainly enhance democracy by reducing the potential for speculators and external actors to exercise undue direct or indirect influence over domestic policy making (Epstein, Grabel and Jomo 2005).

BOX 4.2

CAPITAL CONTROLS TO STAVE OFF THE 1997-98 FINANCIAL CRISIS IN MALAYSIA

The goals of the capital controls that the Malaysian government introduced in 1998 in the wake of the East Asian financial crisis were to facilitate expansionary macroeconomic policy while defending the exchange rate, reduce capital flight, preserve foreign exchange reserves and avoid an IMF stabilization programme. These included: prohibition measures that stopped offshore speculation on the ringgit (the Malaysian national currency); prior official approval for the export of foreign currencies by Malaysian residents to obstruct speculative outward capital flows; requiring repatriation of export proceeds within six months from the time of export; and imposing a 12-month ban on the outflow of external portfolio capital.

While these measures are still regarded as controversial in parts of the financial community, the evidence suggests that the controls were well designed to limit foreign exchange outflows and speculation on the national currency, while not adversely affecting foreign direct investors. At the same time, the measures did provide breathing room for domestic monetary and financial policies and allowed for a much speedier recovery than would have been possible via the orthodox IMF route (Epstein, Grabel and Jomo 2005).

CENTRAL BANKS AS AGENTS OF EMPLOYMENT CREATION

The previous discussion gives credence to the proposition that central banks, in coordination with executive branches of government, should also be agents of employment creation. However, their primary focus has been on keeping a low rate of inflation (overall price stability). Economic growth and employment objectives, from this perspective, are seen as inappropriate direct targets of central bank policy. Employment and growth objectives are assumed to be met as a "by-product" of an inflation-focused approach to monetary policy that will create the macroeconomic stability needed to favour investment, growth and employment creation (Epstein 2007a).

A stable macroeconomic environment is an essential prerequisite for growth and employment.[32] However, even on this count, the problem is that many contemporary central banks, particularly of economically advanced countries, decided to focus only on one source of inflation: **consumer price inflation**. As the Stiglitz Commission pointed out, they chose to ignore **financial asset price inflation** (what John Maynard Keynes described as "*profit inflation*"), turning a blind eye to the systemic risks posed by financial innovations on risk and liquidity management in financial markets. "Thus while [consumer] price stability was achieved, central banks did not prevent, and may even have contributed to, the gravest financial turmoil since the Great Depression" (UN 2009:35).

32. As British economist John Maynard Keynes had warned only a couple of years before the terrible episodes of "hyperinflation" (commonly defined as 50 percent inflation a month or more) that hit Germany and other neighbouring countries in the early 1920s: "...There is no subtler, no surer means of overturning the existing basis of Society than to debauch the currency. The process engages all the hidden forces of economic law on the side of destruction..." (Keynes 1963 (1919):78).

Many central bankers claim that even if asset prices should be their concern (some say it is not), they do not have the instruments to deal with asset price inflation. Their argument is that they only have the instrument of raising interest rates, which could provoke a generalized recession in the process. But according to the Stiglitz Commission, central banks have many more refined instruments than the blunt use of interest rates. These include the above-mentioned asset-type-specific capital requirements and other regulatory instruments that can be used to go against the tide of speculative booms that are bound to end in bust. In addition, there needs to be much closer coordination between central banks that deal with trends in the overall economy (the macroeconomic level) and regulatory authorities that monitor individual financial institutions and instruments (the microeconomic level). As the recent crisis demonstrates, the collective impact on jobs and the economy of decisions taken by individual firms and the growth of particular types of financial products can be devastating (UN 2009).

The first challenge is thus to *include the control of these asset-based systemic risks among the core objectives of central banks* in order to live up to the duty to protect people's right to work against the risks of financial instability.

The second challenge (to meet the duty to fulfil the human right to work) is to return to the historical norm of *integrating growth and full employment as a core mission of central banks*, on a par with macroeconomic and price stability. The tendency may not be easy to reverse. In some countries, such as the United States, employment and growth are a core part of monetary policy. In other jurisdictions, such as the Eurozone under the purview of the European Central Bank (ECB), the explicit primary focus is price stability (inflation at below 2 percent). Likewise, a growing number of central banks in developing countries and transition economies have signed on (implicitly or explicitly) to "**inflation targeting**" in the low single-digits as their primary operating framework. This represents a sharp break from historical practice, not just in the developing world, but also in the now developed countries. In the post-World War II period, development and full employment was seen as crucial part of central banks' tasks (Epstein 2007a).

That central banks should be agents of employment creation immediately raises the question of the extent to which central banks should be immune from public oversight. Historic cases of hyperinflation (inflation at 50 percent a month or above) have given good reason to the argument that central banks should not be subject to short-term political expediency. Whether they should be independent institutions or under the direct control of elected governments is a matter of political debate.[33] But in either case, there should be formal and informal mechanisms to hold central bankers accountable to full employment goals (Stiglitz 2003; NGLS 2009a).

This implies greater policy dialogue on a number of fronts:

- Firstly, there should be a much more open and transparent public debate on what is often presented as the "trade-off" between full employment or higher wages and inflation.
- Secondly, it is important to better understand the macroeconomic policy options (heterodox policies) that could lead to more pro-employment growth.

33. This has become an overt political issue in some Eurozone member countries. For instance, in the run-up to the French presidential election in 2007, both the centre-right and centre-left main political parties had included a reform of the ECB statutes to include growth and employment as part of their election platform.

DO HIGHER WAGES AND FULL EMPLOYMENT ACCELERATE INFLATION ?

Annex I explains the history in economic theory on the trade-off (real or perceived) between inflation and full employment. This was taken to its extreme in the highly influential monetarist theory of the **Non-Accelerating Inflation Rate of Unemployment (NAIRU)**, which sets a level of unemployment below which inflation risks accelerating and eventually getting out of control. The basic argument is that any public intervention to promote full employment through fiscal or monetary expansion will not lead durably to more jobs but to higher levels of inflation. There would be "too much money chasing too few goods" as the common adage goes. At best, there is scope to influence "cyclical unemployment" (e.g. through stimulus measures in the face of a recession) when the full productive capacity of the economy at a given time is underutilized (UNCTAD 1995).

Although the validity and usefulness of NAIRU has been seriously challenged in academia, it is still widely used to assess and guide macroeconomic policy (UNCTAD 1995 ; Epstein 2007a). In the United States for example, a reduction in levels of open unemployment that fell below the assumed NAIRU in the latter part of the 1990s (the NAIRU was then fixed at around 6%) was invoked by the US Federal Reserve as a reason to hike up interest rates even in the absence of any signs of inflation rising (Stiglitz 2003). The same argument is applied to wages with a view to preventing a wage-led inflationary spiral. In 2007, for example, the President of the European Central Bank had openly threatened to raise interest rates if European workers' collective demands for wage increases were met.[34]

This particular brand of economic philosophy has not only sharply restricted macroeconomic policy : it has also been used to weaken social policy by arguing that if unemployment remains durably at a higher level after a recession is over, it is due to "*rigidities*" in the labour market. Policy remedies thus include deregulation of labour markets (especially the weakening of trade union rights) and cutting back on minimum wages and unemployment benefits where they exist. These are measures purported to improve the "*supply side*" response of the labour market to the needs of business. *The Economist* magazine actually prescribes these types of remedies as a way out of the current global jobs crisis :

> "Over the next couple of years, politicians will have to perform a difficult policy U-turn ; for, in the long term, they need flexible labour markets. That will mean abolishing job-subsidy programmes, taking away protected workers' privileges and making it easer for businesses to restructure by laying people off."[35]

Some measures to improve the "supply" of labour are essential and need more investment, such as providing re-training for unemployed people with the skills to match labour demand (known as "*active labour market policies*"). But other measures that prevent workers from organizing and bargaining collectively are not only counter-productive from a social justice perspective : as we have seen, they have negative macroeconomic consequences by repressing aggregate demand. Fundamental principles and rights at work are not an "economic distortion" but rather a means to help correct the uneven bargaining relations between workers and employers (Jenkins, Rodgers and Lee 2007).[36]

34. See for example "ECB warns of higher rates if pay levels rise" in *International Herald Tribune*, 2 February 2007.

35. *The Economist*, 14 March 2009, page 11.

36. A modest but important step in the right direction on this front has been the suspension in April 2009 of the "Employing Workers Indicator" (EWI) from the World Bank's highly influential *Doing Business Report*. >>>

To anchor the decent work agenda not just in social policy but also macroeconomic policy, it is essential to understand the conceptual flaws embodied in the NAIRU approach to economic growth. It assumes that the long-term full productive potential of an economy (called "**potential output**") is not influenced by demand, which is why demand-boosting measures are seen to only generate higher inflation in the long run. But this misses a key dimension: *the prospect of strong demand growth provides a powerful incentive for entrepreneurs to invest in expanding productive capacity (expanding potential output); while the prospect that demand will remain weak has the opposite effect*. As UNCTAD had already warned in 1995:

> "Restrictive macroeconomic policies can therefore be self-validating: if demand growth is checked too much on grounds that potential output is not sufficient to satisfy it, the growth of potential output will be held back" (UNCTAD 1995:173).

This then can lead to a vicious circle. Lower rates of investment in capital formation slow the rate of productive employment creation, which is responded to through more labour market flexibility that further depresses wages and further reduces incentives to invest in productive capacity and thus productive employment.[37]

The evidence on whether inflation targeting works at reducing inflation is at best mixed, and the record shows that economic growth and employment generation are rarely, if ever, the by-product of inflation-focused central bank policy. There is plenty of evidence that they can in fact create obstacles to more and better employment (Epstein 2007a; Heintz and Pollin 2008). To move away from this harmful one-size-fits-all approach in central bank policy, a more balanced and pluralistic debate on the monetary policy agenda is needed. Some initial questions could include:

- Is inflation in the lower single digits always appropriate if it disproportionately affects the prospects of employment growth?
- Could inflation targets be relaxed with a better understanding of what constitutes "moderate" inflation (that is good for growth and employment) which depending on national contexts could be much higher but remain below 10 percent or even 15 to 20 percent (Jomo 2007)?[38]
- Should policy makers better differentiate the sources of inflation, such as supply shocks (e.g. caused by commodity speculation on the world market), and oligopolistic rent-seeking practices, which tighter monetary policies do nothing to address?
- Could the dangers of a wage-led inflationary spiral only be valid if wage growth far exceeds productivity growth (ILO 2008a)?
- If so, should the policy agenda rather focus on avoiding further wage deflation and restoring average wage growth closer to productivity growth (including through regularly updated minimum wage legislation, strengthened social dialogue and collective bargaining, and better financial regulation, as called for in the Global Jobs Pact)?

>>> (The EWI essentially gave the best ratings to countries with the lowest level of workers' protection, and has been used by the World Bank and IMF to pressure developing countries to undertake labour market deregulation.)

37. As described in Annex I, the current Chief Economist at the IMF appointed in September 2008, Olivier Blanchard, suggests in his earlier writings that he also believes that expansionary macroeconomic policy can durably increase potential output, while restrictive policy has the opposite effect.

38. A key argument in favour of the low-digit inflation targets is that inflation hurts the poor more than the rich. This is certainly the case for high rates of inflation, but at more moderate levels, when the question is presented as a trade-off, opinion surveys suggest that unemployment rather than inflation is perceived as a bigger problem for those in the lower quintile of income distribution (Epstein 2007).

The global economic crisis has put the single-minded monetary policy focus on inflation on the back-burner. But with the colossal amounts of liquidity pumped into the global economy since late 2008, there is a real risk of a return to restrictive macroeconomic policies once global economic (but not employment) recovery appears to be on a sure footing. The following section explores a range of heterodox monetary instruments that support employment stability and growth. Some of these could be used, in tandem with other policies, to direct credit to employment-generating sectors and may even help protect employment growth from the risks of future macroeconomic policy contraction.

HETERODOX FINANCIAL AND MONETARY TOOLS TO SUPPORT EMPLOYMENT

The still limited but growing literature and research on employment-friendly macroeconomic policies shows that a range of options are available – from modest changes to inflation-targeting to a much broader change in the mandate of the central bank and a focus on "**employment targeting**" within a broader monetary, financial and fiscal policy framework. There is no "one-size-fits-all" (Epstein 2007b).

How would an employment targeting framework operate? The central bank and the government, working together on this, would estimate a feasible target range for employment growth, taking into account the rates that are consistent with moderate inflation. Based on the estimate of the relationship between its policy instruments and employment growth, the central bank would try to achieve its target. This would be part of connecting the target to "real" as opposed to just monetary aspects of the economy: employment, productive investment, the real exchange rate. The priority and the type of instrument used might vary from one context to another, but it would appear that **capital management techniques** discussed above would often play a critical role in the process.

One of the frequently mentioned policy strategies is the pursuit of a **stable and competitive real exchange rate (SCRER) policy** (the "real" exchange rate is the nominal exchange rate adjusted for inflation). Exchange rate policy can significantly affect employment outcomes. For example, an overvalued exchange rate can be a cause of mass unemployment, while exchange rate gyrations are a major source of job and livelihood insecurity. Achieving a stable real exchange rate that enables local firms to compete fairly with imports might involve confronting a challenge in conventional economic theory known as the "**macroeconomic policy trilemma.**" In a nutshell the theory argues that with an open capital account, it is not possible to maintain simultaneous control over both the exchange rate and the interest rate, two fundamental instruments in the pursuit of full employment. The use of capital management techniques is one way to overcome this challenge.

Important lessons can be learnt from the heterodox manner in which the Argentinean government and central bank managed Argentina's post-2001 crisis situation in this respect. The SCRER was part of an explicit policy that placed decent work at the heart of the recovery effort, which included employment targets in the country's national MDG framework (see Box 4.3). One of the lessons is that not all countries may be in a position to pursue a SCRER strategy, at least without more extensive capital controls (Akyuz 2008).[39] In the longer-term there is a strong case in favour of more fundamental international reforms to stave off currency speculation – see Chapter 7.

39. The SCRER does not necessarily work in all country situations. It works best in countries with a strong "tradable" sector (which comprise the export sector and domestic sectors that compete with imported goods).

BOX 4.3

SUPPORTING THE DECENT WORK AGENDA THROUGH UNORTHODOX EXCHANGE RATE POLICY : THE CASE OF ARGENTINA

The introduction of an SCRER policy was part of the post-2001 crisis government's strategy to integrate employment and decent work as cornerstone of a more coherent economic recovery and development strategy.

In the early 1990s, the government with support of the IMF instituted a "currency board regime" which essentially fixed an overvalued Argentinean peso to the US dollar, which meant that local enterprises were crushed by cheap foreign imports and monetary policy was entirely dependent on foreign reserves which got depleted due to a worsening trade balance. Although Argentina was viewed as the "best pupil" of the IMF and its currency board regime hailed as a model for other emerging markets to replicate, this unsustainable system created the conditions for the 2001 crisis, which led to a massive devaluation of the peso.

By mid-2003, the newly elected government decided to break from the policy conditions of the IMF and institutionalized a SCRER policy as part of its official strategy to support an employment-focused recovery. This meant trying to maintain a stable real exchange rate at a level that would allow local firms to regain ground in the local market (roughly 3 pesos to the dollar), while still maintain control of the money supply. To do this, the government and central bank cooperated to : (1) intervene on the foreign exchange market to counter the surge of short-term speculative capital inflows that would appreciate the currency ; and (2) remove resulting excess pesos by issuing interest-bearing central bank letters and notes (an operation known as "sterilization").

This policy was complemented by a range of other measures, including reserve requirements on short-term capital inflows, collective price agreements, social programmes for the unemployed (see Box 3.2 on the *Jefas* programme), extension of social security, investments in public works and periodic hikes in the minimum wage. The record showed that by the first quarter of 2006, the country had reached the highest employment rates since the early 1980s, while steep inequalities were narrowing and poverty levels going down.

These policies would not have been possible if the government had not been in a position to claim policy space by pushing ahead despite opposition from the IMF on a number of counts, notably intervention on the foreign exchange market. The government also built considerable fiscal space through successful agreement on reduction of dollar-denominated sovereign debt combined with taxes on high export earnings. In addition, Argentina experienced only moderate surges in capital inflows since its recovery, which partly explains the success of sterilization policies (Jenkins, Rodgers and Lee 2007 ; Damill, Frenkel and Maurizio 2007 ; Akyüz 2008).

Among other promising heterodox monetary instruments are ***credit allocation mechanisms***. These tools include asset based reserve requirements, loan guarantees, support for pooling and underwriting small loans, utilizing the discount window in support of employment generating investments:

- **Asset-based reserve requirements** are a system in which lending institutions are required to hold low- or zero-interest-yielding reserves as a proportion of their earning assets. In effect, banks earn less the higher the proportion of reserves they need to hold. We already briefly touched upon how higher capital requirements could help counter irresponsible risk taking by financial institutions. Here the same type of policy tool can be used (in reverse so-to-speak) to direct credit where it is most needed to promote employment or strategic economic sectors (such as agriculture, or renewable energy). By lowering reserve requirements on those preferred types of assets, the central bank or government creates incentives to hold these types of assets relative to less desirable assets. These could also build-in a gender lens by preferential lending for activities that employ more women.

- **Loan guarantees** are another possible instrument which could be attributed to banks that lend to cooperatives and small businesses that generate good employment opportunities. These can also support micro-credit institutions to reach out to micro- and small enterprises, or poor entrepreneurs in the informal economy.

- **Special discount windows** of central banks could play a similar function offering credit, guarantees, or discount facilities to institutions which are on-lending to firms and cooperatives that offer promising employment potential (Epstein 2007b).

These types of instruments could be introduced as part of crisis response, but kept in place even when counter-cyclical measures are not deemed necessary anymore. As noted above, this could help protect employment from the effects of a general credit crunch that would be triggered if policy were to solely rely on the blunt instrument of interest rate hikes (Jomo 2007).

It should be emphasized that some of the above-mentioned measures work better in countries with relatively well-developed financial systems. They played a key role in post-World War II reconstruction in Europe and were part of the economic apparatus that many developing countries used to support the actions of State development banks that helped finance between a fifth and half of all fixed capital investments in places like Mexico, Chile, South Korea, Brazil and Indonesia (Espstein 2007b; Pollin and Heintz 2008).

In low-income countries, the ability to direct private bank lending is more limited. Research on private banking in many parts of Sub-Saharan Africa shows that credit is effectively "rationed," with very large differences between deposit and lending rates (spreads). One of the reasons is that private banks hold excess liquidity and prefer holding short-term government securities rather than long-term credit needed for productive investments. They do not respond well to lowered reserve requirements.

A different instrument to achieve the same purpose is a **prescribed asset** policy, which represents a type of financial quota. Under such a policy, a certain fraction of a bank's (or other financial institution's) assets must be held as investments or loans that support a priority area of economic development. Prescribed assets are not new to African economies. For instance, in the past, banks were frequently required to hold a portion of their assets as loans to the agricultural sector (Heintz and Pollin 2008; UNCTAD 2006).

The research suggests the need to go beyond trying to influence commercial bank lending and revisit the role of public **development banks** as a means to channelling more resources to support employment-creating investments. These types of institutions and above-mentioned policy instruments have been rolled back in the last two decades on grounds that they were subject to corruption and political patronage, and were inefficient. While there is plenty of evidence of abuse, *it is important not to confuse the disease with the cure* – which for a long time was assumed to be the more efficient performance of deregulated private banking. But public (development) banks were originally instituted precisely to respond to the short-comings of private banks, which have now become so evident. The ILO notes that in the face of the post-crisis credit crunch in United States, State-owned banks have shown greater readiness to lend to businesses and consumers than their private-sector counterparts (ILO/IILS 2009). It is not just a developing country issue. The aforementioned NGLS global civil society consultation on crisis response revealed consistent calls to give a greater role to public banks, a point that was also emphasized in the Stiglitz Commission.

There is a vital need to ensure that governance structures of public financial institutions have greater capacity, transparency and accountability to handle heterodox financial and monetary tools. An important dimension here is to be clear about the objectives these tools are supposed to serve. This is the subject of the next chapter, focusing on poverty-reduction through expanding productive employment in developing and least-developed countries.

5. A DEVELOPMENT PARADIGM SHIFT : POVERTY REDUCTION THROUGH PRODUCTIVE EMPLOYMENT GROWTH

"The only way to reduce poverty in the LDCs without resort to international welfarism or international migration is through the development of productive capacities of the LDCs and the concomitant expansion of productive employment opportunities within them" (UNCTAD 2006).

This chapter is based heavily on the innovative work undertaken by UNCTAD[40] (drawing on research from other sources, including ILO, FAO, UNDP, UNIDO, UNRISD and DESA) to promote a paradigm shift in international and national strategies towards poverty eradication in least-developed countries (LDCs). Many of the lessons are valid for other developing countries that do not fall under the UN technical definition of an LDC.

The paradigm shift involves placing at the heart of policies the development of productive capacities in a way that expands productive employment opportunities to reduce poverty. It means shifting from an approach that targets social policy but takes a universally non-interventionist approach to the economy, to a more *targeted economic policy approach* (that supports both production and employment) and a progressively universal coverage of social policy. It means also a shift from a "trade-driven approach to development" to a "*development-driven approach to trade*."

Understanding this paradigm shift is essential for the donor community as well. Doubling or re-doubling of external development finance will not be effective if it continues to be linked to the wrong development model.

WHAT IS PRO-POOR GROWTH ?

The starting point is a better understanding of what we mean by "*pro-poor growth*." It means transcending two tendencies in analysing the causes of poverty. At one end of the spectrum, microeconomic analyses of the causes of poverty focus on characteristics of the poor (such as illiteracy, living in remote areas, working in subsistence agriculture, etc.) and directing policies to address these in a way that is divorced from the broader macroeconomic context. At the other extreme, linking diagnoses of poverty to the macro-context lead to simplistic and misleading assertions that "economic growth is good for the poor." In between, there are studies that try to show that growth is pro-poor if the income share of the poor increases, or accelerates. But empirical work on pro-poor growth shows that to

40. Unless otherwise stated, most of the analysis and evidence presented in this chapter are drawn from UNCTAD's *Least Developed Countries Report 2006,* which focused on developing productive capacities for productive employment.

get behind these vague statistical relationships, it is necessary *to start with the view that household living standards are primarily based on the generation and sustainability of jobs and livelihoods.*

The starting point of poverty analysis should be how people make a living, which in turn is determined by whether there is a virtuous circle of expanding both production and quality jobs (that is, expanding productive capacities *and* inclusive productive employment opportunities) – and whether the international economic system is supporting or undermining this process.

The decent work challenge in developing countries is not just unemployment. Most poor people work: in the absence of social security they simply cannot afford to be completely unemployed. The overwhelming majority of the active population in low-income countries is employed or self-employed in the informal economy, earning very low income without rights and protection. The basic cause of poverty is that *there are simply not enough productive employment opportunities in the formal sector for a growing labour force.*

Part of the challenge is to better utilize existing capacities: existing productive resources and entrepreneurial capabilities in low-income countries are typically underutilized, notably because of lack of demand and other structural weaknesses. But beyond that, the challenge is to set in motion a concerted effort to catalyse and sustain a virtuous circle in which the *further development of productive capacities and the growth of demand mutually reinforce each other*. This means investing not only in the more productive and dynamic sectors of the economy but also in building capabilities *in the sectors where the majority of population (and the poor) are working*. Without that, there can be high growth, but at best low-job-intensity growth, and certainly not pro-poor growth.

THE NEGLECTED IMPORTANCE OF LOCAL DEMAND

Productive capacities (which condition the scope for generating more productive employment) develop through the inter-related processes of:

- **capital accumulation** (investments not just to increase machinery and equipment, but also supporting economic and social infrastructure and human capital);
- **technological progress** (new technologies, know-how and innovation); and
- **structural change** (more productive synergies within and between sectors of the economy).

However, these processes will not occur automatically by themselves or continue in some mechanical fashion forever. As we have seen in the previous chapter, what mainstream economic policy frameworks have missed is the **essential role of demand**. Demand is firstly what determines whether productive capacities are fully utilized or not. But even more important, the expectation of whether or not demand will grow is what conditions profit expectations and hence decisions to invest to expand productive capacities.

Domestic demand makes the largest contribution to economic growth in most low-income countries, yet its growth is also very weak as it has been neglected. This contributes to holding back investments in productive capacities, which in turn limit the scope for productive employment opportunities that could raise domestic demand. In order to break this vicious cycle, a key challenge is to boost local demand in the sectors where its potential is the highest. In the majority of low-income countries, *trends in domestic demand are closely related to what happens within the agricultural sector*.

AGRICULTURAL GROWTH LINKAGES, EMPLOYMENT AND POVERTY REDUCTION

Historically, the majority of the poor in low-income countries have been employed in agriculture. However, decades of structural adjustment policies that rolled back investments in agriculture (which was further undermined by unilateral agricultural trade liberalization) have seriously contributed to weakening the capacity of agriculture to productively absorb a growing labour force. Other factors, such as limits to arable land and environmental degradation have also contributed to this trend. We might be at a tipping point where more people will be seeking work outside agriculture for the first time in the history of LDCs. Yet non-farm productive employment opportunities are also growing too slowly.

To reverse this trend, it is essential to *capitalize on the linkages between agriculture and the rest of the economy*. On the supply side, concerted efforts to raise agricultural productivity is particularly important for increasing domestic savings in very poor countries and also for ensuring food security through an adequate supply of locally-produced foodstuffs. But demand-side linkages that result from agricultural growth are also an important mechanism to stimulate the development of local manufacturing industries and local services. These inter-sectoral linkages can serve as a catalytic incentive for productive investment decisions, mobilization of latent entrepreneurial capabilities and to ensure that economic growth is more broad-based and inclusive.

Research on agricultural demand-led industrialization in countries at different levels of development has found that in low-income countries, every US$1 of expenditure by agriculture generates US$2.75 of induced demand for non-agricultural inputs and services, and 70 percent of this backward linkage effect is attributed to rural household demand for consumer goods and services. Research in Africa has also found that growth in household incomes that comes from increases in agricultural production and incomes (due to technological changes, better prices or lower input costs) is largely spent on farm and non-farm items that are locally-produced. Adding US$1 of new farm income potentially increases total income in the local economy – beyond the initial US$1 – by an additional US$1.88 in Burkina Faso, US$1.48 in Zambia and US$1.48 in Senegal.

Viet Nam's relative success in terms of growth and poverty reduction during the period 1993-1998 provides a good example of how investments in agriculture have positive growth spill-overs in other sectors. Broad-based increases in agricultural labour productivity increased earnings for the majority of the poor and stimulated domestic demand for non-agricultural goods that were also produced by the poor in small and medium-sized enterprises (SMEs). This in turn led to higher earning opportunities for agricultural goods and services thereby creating virtuous circle of growth and poverty reduction.

The same kinds of synergies can be observed while promoting labour-intensive infrastructure projects as part of local development programmes that simultaneously support neighbouring micro- and small enterprises by using local materials and maintenance, and rely less on foreign inputs.

An important part of the process is to ensure that gains in productivity serve both for reinvestments and to improve incomes of small farmers as well as agricultural and non-agricultural wage earners. This requires institutions that notably support income redistribution, rights to bargain for better wages or farm incomes that must be adapted to the special conditions of the informal economy.

RESOURCE MOBILIZATION AND STATE CAPACITIES

These examples of bottom-up employment-led growth strategies that complement investments in more dynamic sectors require sufficient finance and State capacities. According to UNCTAD, domestic gross savings rates in LDCs are currently too low to achieve the investment rates needed to make a significant impact on poverty reduction (albeit a significant proportion may be leaking out through capital flight). But the potential savings that could result from better utilizing underemployed labour and latent entrepreneurship through the types of initiatives mentioned above could be very significant.

A defining feature of the most successful East Asian developing economies has been their ability to raise their domestic savings ratios by increasing business savings (not simply household savings). After the initial stages of the development process, the engine for developing productive capacities was the creation of a strong "*investment-profit nexus*." Through this nexus, expected profits provided the incentive for investment ; and realized profits were both an outcome of investments and a source for further investment. This did not happen automatically. It required the use of the heterodox policy instruments described in the previous chapter ; and was backed in the early stages by equitable land distribution and very large amounts of foreign aid.

External finance can play an important catalytic role in kick-starting and supporting a virtuous cycle of domestic resource mobilization and investment. Low-income countries have been by and large left out of international capital markets. As for longer-term foreign direct investment (FDI), its effectiveness depends on whether domestic policies manage to integrate FDI into domestic development strategies. Empirical studies show that FDI displaces (or "crowds out") domestic investments at least as frequently as it promotes ("crowds in") domestic investments. The data on LDCs suggests that foreign investment has not brought strong positive linkages to generate higher levels of private domestic investment. FDI-dependent growth based on exports of oil, minerals, or manufactures produced in export processing zones (EPZs), has often led "*enclave economies*" with little employment generation outside these enclaves. Elaborating polices that can foster positive linkages between FDI and domestic private entrepreneurship is a major challenge.

Low-income countries have thus been relying heavily on official development assistance (ODA) as a source of external finance. However, the potential of ODA to expand their fiscal space has been reduced by a number of shortcomings including : unpredictability and volatility of aid which tends to be pro-cyclical ; lack of coordination of the aid system ; high transaction costs of multiple donors ; internal brain drain from the public sector to donor projects ; and a fiscal squeeze on current expenditures due to conditionality and increased debt service payments from aid loans.

As low-income country governments are improving their financial management capabilities, they have repeatedly called for a much greater proportion of ODA to be channelled directly into their national budget (**budget support**). This call was echoed in the conclusions of the first Development Cooperation Forum (DCF) of the United Nations Economic and Social Council (ECOSOC) in June 2008, which states that : "*Budget support should be increasingly*

41. Official summary of the ECOSOC Development Cooperation Forum 2008 : http ://www.un.org/ecosoc/newfunct/Summary_of_the_President.pdf.

used as a preferred modality for delivering development aid due to its positive effects on national ownership, disbursement speed and use of national systems." [41]

If ODA is to support national ownership of policies, it should mean that developing countries should have the *democratically-accountable* policy space to experiment with heterodox economic policies in support of expanding productive employment. This right is often denied by the donor community and IFIs on grounds that these policies do not work; but when provided with evidence that they can be successful if well managed, the argument shifts to saying that State capacities do not exist. Former UNRISD Director Thandika Mkandawire (2001) has identified a series of "impossibility theses" that are often put forward to argue that the State cannot play a developmental role in Africa.

Weak State capacities are sometimes the result of long periods of civil conflict, but they are also often the result of external conditionalities that imposed severe cutbacks on State administrative services since the 1980s. If State capacities are indeed still weak, this does not mean that the State is irrevocably incapable. Direct budget support is often denied because more progress is needed for good governance. But lack of financial resources is a key source of inadequate governance. *Good governance requires an adequately paid civil service* (UNCTAD 2006).

Governance-related conditionalities can also undermine the effectiveness of aid if they insist on the doctrine that "less government intervention is good to promote a better investment climate." In successful developing countries, a better investment climate meant something quite different: it entailed public action that recognized the diversity of enterprise-level capabilities and proactive efforts to upgrade them; it entailed a macroeconomic framework that was geared to promoting rapid capital accumulation by providing investment incentives. [42]

In addition to fiscal constraints and donor-led conditionalities, other policy space limitations are related to provisions in various multilateral and bilateral trade agreements (see next chapter), but also to what is known as the "balance-of-payments constraint."

THE BALANCE-OF-PAYMENTS CONSTRAINT (PART 1)

The conventional approach to the **balance-of-payments constraint** stipulates that no country can grow faster in the long run than the rate consistent with "balance-of-payments equilibrium" which implies that there should be a balance between the value of exports and the value of imports, unless higher import costs vis-à-vis export revenues (trade deficits) can be financed through sufficient capital inflows.

Each component of demand in the broad sense of the term has some degree of import content (whether private consumption, investment, government expenditure, exports and of course imports). This import content is essential for the continuation of ongoing economic activities and development, so countries need foreign exchange to pay for these imports.

42. As UNCTAD (2006:300) argues in this regard: "The government capacities required in order to formulate and implement a strategy to develop productive capacities and expand productive employment opportunities are no more exacting than those required for formulating and implementing a poverty reduction strategy [PRSP]. Indeed, there are probably more *working* models to turn to with regard to the former than the latter [emphasis added]."

Export earnings are usually the most important source of foreign exchange. But if the rate of growth of exports is not enough, countries are obliged to attract external capital to finance the difference between the value of imports and the foreign exchange provided by exports. If this does not happen, it is said that the components of demand have to be constrained in the long term in order for the balance of payments to be in equilibrium.

Growth in the LDCs has been constrained by their balance-of-payments position. Most have experienced current account deficits, which have been financed by capital flows and transfers. But when the latter are not sufficient or unreliably volatile, measures are taken to cut back on imports, which implies cutting back on demand generally, since all elements of demand have an import content. Constraints on the balance-of-payments can have several external sources, such as:

- declining terms of trade;
- externally-imposed unilateral trade liberalization (often letting in heavily subsidized imports);
- protectionism in rich countries; and
- misaligned currency values.

In the wake of the global economic crisis, these constraints have taken catastrophic proportions for the many developing countries that do not have sufficient foreign currency reserves to buffer the shocks of collapsing export revenues, migrant remittances and capital flight.

The balance-of-payments constraint is a perennial problem, but the conventional approach outlined above ignores its deeper roots. This constraint represents one of the most deficient and inequitable features of the current international financial architecture: it places the onus of adjustment on deficit countries with weak currencies. Chapter 7 examines some of the systemic remedies to this problem put forward in the wake of the global financial and economic crisis. Suffice it to mention here that past responses to the balance-of-payments constraint have often translated into "engineered recessions" ("stabilization programmes") to curb import demand; and an excessive focus on unsustainable "trade-led approaches to development."

A DEVELOPMENT-LED APPROACH TO TRADE

The global economic crisis has given more momentum to calls for a reorientation of development approaches that rely less on export-based demand and more on domestic consumption-led demand growth. The current imbalance focusing primarily on trade-led growth has a long history: UNCTAD has noted how free trade theory has come to dominate the understanding of development processes since the 1980s. This was reinforced in the 1990s through arguments to the effect that "fast and full integration with the world economy was the key to seizing the opportunities of globalization and minimizing the chances of being left behind." From this perspective, UNCTAD noted, "global integration began to replace national development as major policy objective of governments" (UNCTAD 2006:293).

The paradigm shift discussed in this chapter involves a different approach to trade. It means pursuing a strategy that does not simply focus on developing productive capacities in the more dynamic sectors with export potential (tradable sectors) but that also supports

productive capacities within non-tradable activities (products that are sold locally) and seeks dynamic linkages between the two. Especially in low-income countries, it is in the non-tradable sectors that the majority of the population (and the poor) tend to be employed. They represent a vast pool of underemployed labour and entrepreneurial potential and source of domestic demand for more balanced growth. Obviously, the strategy has to be complemented with regional trade linkages (essential for very small national economies) as a stepping stone or alternative to global integration.

Under this paradigm, the policy approach "…first focuses on production, and then from this perspective identifies how international trade can support capital accumulation, technological change, structural change, employment creation and poverty reduction. What matters is not to maximize trade, but to maximize the beneficial effects of trade" (UNCTAD 2006:293-294).

The next question is whether trade rules support or hinder this process.

6. TRADE RULES FOR DECENT WORK AND A FAIR GLOBALIZATION [43]

One of the most difficult dimensions (conceptually and politically) of the decent work and fair globalization agenda is the relationship between trade and labour. This chapter examines the proposal of a "**social clause**" in the WTO that would integrate core labour standards in multilateral trade rules and enforcement mechanisms. It then argues that the debate between trade and labour standards has to an extent diverted attention from another key dimension of the trade and labour nexus: the differential impact of trade on employment. Recent research shows that the impact of trade liberalization on labour markets is much more important than previously assumed. Does this mean primarily that policies should better support labour market adjustments to trade, or also that trade rules themselves should be made more consistent with the full and productive employment goals of developing countries?

THE TRADE AND LABOUR STANDARDS DEBATE

In the contemporary history of multilateral trade governance (namely, since the establishment of the WTO in 1995), the relationship between trade and aspects of the decent work agenda has until recently primarily focused on whether labour standards should be incorporated in trade rules. This approach has remained in an impasse since the 1996 WTO Conference in Singapore. The reason for the deadlock is two-fold. On the one hand, there is concern especially in the industrialized countries that differential labour standards (and levels of application) between trading partners can create competitive disadvantages for those economies with higher standards, insofar as they are well enforced. On the other hand, there is concern, principally among developing countries, that introduction of a labour standards-related social clause in the WTO could be misused for protectionist purposes.

Some have suggested that an important step towards a common understanding of the issue was achieved in the 2008 ILO Declaration on Social Justice for a Fair Globalization. In this tripartite consensus document, it is stated that: "*the violation of fundamental principles and rights at work cannot be invoked or otherwise used as a legitimate comparative advantage and that labour standards should not be used for protectionist trade purposes*" (Article I.A.(iv)). Beyond this agreement of principle, there remains some debate as to whether or not the WTO should have an active implementation role.[44] What is clear is that the *primacy of the ILO* in this domain remains uncontested. Especially in the wake of the crisis, the thrust of the discussion has refocused on the need to dramatically strengthen the capacity of the

43. This chapter draws heavily from the findings of a workshop on trade and employment organized by NGLS and the Friedrich Ebert Stiftung (FES) Foundation on 20 May 2009 in Geneva.

44. There are proposals to amend the WTO Agreement on Subsidies and Countervailing Measures to include labour standard abuses as comparable to a non-permissible export subsidy. >>>

ILO and counterpart national institutions to implement labour provisions (including the capacity to undertake comprehensive labour inspections) and continue promoting ratification of core labour conventions where this is not yet the case.

Labour standards are certainly increasingly referred to in regional and bilateral trade agreements. Their principal weakness lies in supervision, particularly in countries that have not ratified the relevant ILO Conventions (Doumbia-Henry and Gravel 2006). Moreover their effectiveness on promoting the decent work agenda cannot be treated in isolation from the broader impact of these trade agreements on employment, especially on the economically less competitive trading partner. This brings us to consider the other dimension of the relationship between trade and decent work, which so far has received much less attention in trade policy debates.

THE IMPACT OF TRADE LIBERALIZATION ON EMPLOYMENT

In discussing how to promote greater coherence between the multilateral trade and decent work agendas, ILO Director-General Juan Somavia has noted that a major mistake made by advocates of free trade has been to ignore the fact that intensified international competition increases the pace of both job creation and job destruction – and does so in very uneven ways within and between countries.[45] A pioneering joint study by the ILO and WTO secretariats has begun shedding new light on this issue. The study noted that the predictions of conventional trade theory that expanded trade will be equalizing no longer hold true. Instead, *there appears to be widespread tendency for wage and income inequality to increase in the wake of trade liberalization and related developments such as the increase in trade in services and intermediate goods, increased flows of FDI and outsourcing, and the diffusion of skill-biased technological change*. Also, adjustments to trade liberalization do not only affect import-competing sectors, but other sectors as well. So job insecurity is much more pervasive than previously assumed (ILO/WTO 2007).

As awareness is growing that the social dislocations caused by trade liberalization are much greater than assumed, much of the current policy discussions and research on trade and labour are increasingly focusing on *how labour markets can better adjust to trade reform* (in effect: adjust to trade liberalization). These concern national policies to deal with negative distributional effects, including through strengthened social protection and active labour market policies to help better match labour supply and demand, including through skills and retraining programmes.

The above measures are only beginning to receive the attention they deserve in mainstream economic and development policy discussions, as noted in Chapter 3. They are essential, irrespective of purely trade factors, as social dislocations are also the result of other causations such as technological change, obsolescence of demand for certain products and financial instability or crisis.

>>> (See for example speech delivered by James Howard, ITUC in: "What Future for Global Economic Governance? – Potential Role of the WTO," Report of the session at the WTO Public Forum 2008, jointly organized by Friedrich Ebert Stiftung / Evian Group / CUTS International, Geneva, 25 September 2008.)

45. Keynote address at an international conference on "Decent Work: A Key to Social Justice for a Fair Globalization," organized by the Norwegian government in cooperation with the *Financial Times* on "Decent Work: A Key to Social Justice for a Fair Globalization," 5 September 2008, Oslo.

However, the other side of the equation is equally important: namely, *how should trade policies and rules be adjusted to be made more consistent with the objective of full and productive employment*? This concern was already expressed by the ILO's World Commission on the Social Dimension of Globalization, which stated that in order to achieve fairer multilateral trade rules, one essential principle is that:

> "Trade liberalization should not be enthroned as an end in itself. It is but a means for achieving ultimate objectives such as high and sustainable growth, full employment and the reduction of poverty. As such, *trade policies should be framed with these ends in mind and be evaluated accordingly*" (ILO 2004a:82, emphasis added).

Frank and honest policy debate on this other side of the equation is much more difficult. In part, it is because trade liberalization has been enthroned as an end in itself. As noted in the previous chapter, unqualified free trade theory has deeply influenced development policy. Yet the lessons of rapid and across-the-board trade liberalization in Africa and Latin America since the 1980s suggest that there were many instances where this form of trade liberalization led to the destruction of existing industries, particularly of those that were at their early stages of development, entailing massive job losses without necessarily leading to the emergence of new ones. According to some estimates, total income losses for sub-Saharan Africa from trade liberalization amounted to US$270 billion over the past two decades – more than the total ODA received by the region (UNCTAD 2005; Akyüz 2008).

In contrast, the newly-industrialized economies in East Asia had taken a much more gradual and selective path to trade liberalization, as part of a long-term industrial policy, and only after they had reached a certain level of industrialization and development when firms were in a position to compete internationally. Paradoxically, free trade advocates used the East Asian economic success story as evidence to push for across-the-board liberalization in other developing countries as part of structural adjustment programmes (UNCTAD 2005).

BOX 6.1

NEW POLICY SPACE RESTRICTIONS UNDER THE WTO

The 1994 Uruguay Round agreements have significantly restricted the policy options now available to developing countries. Here are a few examples:

- The Agreement on Subsidies and Countervailing Measures (SCM) prohibits subsidies that are conditional on export performance and those that are contingent on the use of domestic rather than imported inputs. However, LDCs and countries with a per capita income of less than US$1,000 (so called Annex VII countries) are exempted until graduation from this category.
- The Agreement on Trade-Related Investment Measures (TRIMs) requires the elimination of a number of measures such as compelling or providing incentives for an investor to use
- The Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPs) has made development tools such as reverse engineering and imitation less feasible and raised the cost to developing countries of acquiring technology (ILO 2004a; Akyüz 2008).

POLICY SPACE IN TRADE RULES FOR NATIONAL DECENT WORK STRATEGIES

A key operational dimension to make global trade rules fair and equitable is to ensure that developing countries have enough **policy space** to tailor national measures to local conditions and needs, as part of the principle of special and differential treatment for developing countries. The ILO World Commission had noted that the new trade rules adopted with the founding of the WTO at the end of the Uruguay Round in 1994 now make the selective protection or strategic promotion of domestic enterprises vis-à-vis foreign competition much more difficult. Many of the development tools used by now developed countries and by successful East Asian economies are no longer allowed (see Box 6.1, page 45).

Policy space remains controversial and would benefit from a more systematic and explicit treatment from the angle of its contribution to the goal of decent work for all.

An important step towards a common understanding was multilateral consensus recognition of the concept of policy space achieved at the 11th United Nations Conference on Trade and Development (UNCTAD XI). It is now accepted that multilateral rules do impose constraints on policy space in developing countries (see Box 6.2). According to some analysts, the main limitation is that the consensus views policy space as a "trade-off" vis-à-vis the benefits of multilateral rules and disciplines, rather than treating policy space as a necessary and integral part of global rules. Does a trade-off mean that negative consequences can be expected as a result of opting out of multilateral disciplines if that is the only avenue to achieve needed policy space? Does this in effect mean "a choice between the bad and the worse?" In many respects, this limitation is reflected in the current approach to Special and Differential Treatment in the WTO where, at best, greater policy space and flexibility are treated as exceptions with longer time frames that have to be bargained for, rather than an integral part of global rules needed for these to be fair and equitable (Akyüz 2008).

Within a framework that supports open economies and open societies, it should be possible to examine existing agreements as well as the ones under negotiation to see whether greater policy space should be embedded within these to ensure they are compatible with

BOX 6.2

AGREED MULTILATERAL TEXT ON POLICY SPACE

"The increasing interdependence of national economies in a globalizing world and the emergence of rules-based regimes for international economic relations have meant that the space for national economic policy, that is, the scope for domestic policies, especially in the areas of trade, investment and industrial development, is now often framed by international disciplines, commitments and global market considerations. It is for each government to evaluate the trade-off between the benefits of accepting international rules and commitments and the constraints posed by the loss of policy space. It is particularly important for developing countries, bearing in mind development goals and objectives, that all countries take into account the need for appropriate balance between national policy space and international disciplines and commitments."

2004 UNCTAD XI São Paulo Consensus, para. 8

the goals of full and productive employment and decent work for all. Part of the challenge is to distinguish those provisions that genuinely have to do with avoiding harmful international trade practices from the ones that are unduly impinging on domestic economic policies linked to the progressive realization of the right to decent work.

Another important dimension would be to distinguish "protectionism" in the sense of "beggar-thy-neighbour" policies (e.g. tariff escalations of the type that brought down the international trading system in the 1930s) from the policy space needed for developing countries to promote productive employment as discussed in the previous chapter. This may involve the fine-tuning of tariff policies to protect vulnerable farmers from import surges and price drops for example, but these types of policies should not be simplistically equated to "protectionism." As far as crisis mitigation measures are concerned, the new consensus terminology used at the UN Conference on the world economic and financial crisis was developing countries' "right to use legitimate trade defense measures." [46]

Some of the main topics affecting the decent work agenda in the current Doha Round of multilateral trade negotiations relate to:

- Industrial tariff liberalization;
- A special safeguard mechanism to protect livelihoods and food security in developing countries; and
- Financial services liberalization.

Beyond that there is the proliferation of bilateral trade and investment treaties that go much beyond current obligations under the WTO. These issues are on the forefront of international civil society advocacy campaigns.

INDUSTRIAL TARIFF LIBERALIZATION (NAMA)

The Doha Round includes an agenda item that involves principally industrial tariff reductions. Referred to as Non-Agricultural Market Access (NAMA), it also deals with other non-agricultural items such as fisheries. The NAMA negotiations are problematic because (a) they could lead to significant job losses and very significant tariff revenue losses not recouped from other sources; and (b) they could narrow the remaining policy space for many developing countries to pursue industrialization strategies by removing the flexible use of tariffs between sectors and over time.

Strategic use of tariffs can mean applying very low tariffs at one point of time for imported inputs but higher tariffs on other final products for which the local economic base is not yet ready to compete internationally. History shows that developed countries and East Asian success stories made abundant strategic use of tariffs as part of their development strategy (Chang 2002). Currently, developing countries on average have much lower tariffs than developed countries had at a comparable stage of development. But many developing countries still have the potential to use tariffs flexibly because their current applied rates are much lower than the rate at which they already committed to in the WTO (the "bound rates"). That flexibility could be removed, both in terms of the actual level of tariffs and the ability to use different tariff levels for different sectors at different stages of development.

46. Paragraph 15 of the Conference Outcome Document.

The International Trade Union Confederation (ITUC) has undertaken a simulation using the range of tariff reduction coefficients currently proposed in the negotiations for five countries that would appear to have to undertake some of the most drastic tariff reductions. In some cases, the new bound rate would be significantly below the current applied rate, while in others the new bound rate is close to the applied rate, thus removing all future flexibilities to raise tariffs in support of industrialization. In the first cluster of cases, the amount of jobs directly at risk are significant (and a function of the degree of competitiveness of the local firms), but the indirect job losses might be much higher due to inter-sectoral linkages. ITUC highlights also the risk that affected developing countries could be locked in low-value added production paths that would hinder the potential to create more productive employment and decent jobs and move up the development ladder.[47]

In light of these concerns, would commitments to policy coherence not require that there should be a more systematic and comprehensive ex-ante employment impact assessment of various NAMA outcomes for all countries affected, to ensure that NAMA is not inconsistent with the multilateral commitment to full and productive employment?

A SPECIAL SAFEGUARD MECHANISM FOR AGRICULTURE

As discussed in the previous chapter, most developing countries have undertaken rapid liberalization of agriculture which has made small farmers very vulnerable to import surges and price drops. Import surges can have a devastating effect on livelihoods. For example, in Honduras, domestic rice production covered nearly 90 percent of consumption in 1991; but by 2003 imports had increased drastically and the share of domestic production in total consumption was down to less than 10 percent.[48] This is a widespread phenomenon.

A key proposal on the Doha Round agenda is the introduction of a **Special Safeguard Mechanism (SSM)** that would act as an insurance scheme against price depressions and import surges. That scheme would aim to isolate small producers in developing countries from these risks – so to protect livelihoods and jobs, reduce the uncertainty associated with agricultural production and ultimately, by reducing this risk, promote a more conducive environment for investments in agricultural productivity. The basic mechanism is that in cases of import surges or import price drops on specific agricultural products that would threaten livelihoods and food security, developing countries would have the right to raise the corresponding tariffs to a neutralizing level, even if that level is above the "bound rate" in the WTO.

It is a group of developing countries (the G-33) with support from civil society that have taken the lead on this proposal. As part of this effort, the International Centre on Trade and Sustainable Development (ICTSD) has undertaken case studies in some 20 countries, using different indicators associated with livelihood security, food security and rural development, as well as vulnerability to further trade liberalization, to determine which products need some kind of mechanism that can protect small producers from price depression and import surges. The set of products are fairly consistent across the country studies and often correspond to the ones that are the most subsidized in developed countries. From

47. Based on presentation by Esther Busser, Deputy Director of the ITUC Geneva Office, at the NGLS/FES workshop on trade and employment, 20 May 2009, Geneva.
48. Source: FAO cited by ICTSD at NGLS/FES workshop.

that perspective, the use of tariffs could partly be seen as a counterpart of the subsidies used by developed countries to protect their farmers from external shocks, but which developing countries cannot afford to match.[49]

Disagreements over the "trigger" mechanism that would allow initiation of the safeguard was widely reported as a major reason for the breakdown of WTO ministerial negotiations in July 2008. A major concern of civil society is the risk that the final compromise on modalities of application would render the mechanism ineffective in most cases. If that hurdle was overcome, there would also need to be infrastructure in place for the timely monitoring of import volumes and prices so that action can be taken before the damage is done. This is a major challenge, but some creative solutions are worth exploring. UNCTAD, for example, has developed a technical cooperation programme to modernize customs systems in developing countries that could be adapted for this purpose.[50]

It should also be noted that many grassroots small farmers' movements believe that the safeguard mechanism does not go far enough and is unlikely to be effective against the livelihood threats they face. They have for a long time called for a complete removal of agriculture from the WTO jurisdiction, some proposing that the governance of agricultural trade would be more fairly handled by other international bodies such as FAO.

FINANCIAL SERVICES LIBERALIZATION

The recent global economic crisis has brought home the importance of strong financial market regulatory regimes to preserve financial stability and by extension, employment growth and stability. The Stiglitz Commission notes that the WTO's General Agreement on Trade in Services (GATS) Financial Services Agreement provides the only significant regulatory regime for international financial services, but with insufficient regard for its consequences either for growth or stability. It notes with concern that its provisions, if enforced, would "impede countries from revising their regulatory structures in ways that would promote growth, equity, and stability" (UN 2009 :104).

Many civil society organizations have expressed similar concerns, especially with respect to restrictions on the ability of governments to limit the size of banks, introduce new regulations and ban risky activities.[51]

There does seem to be a disconnect between momentum for greater financial regulation and the thrust of these agreements, which the Stiglitz Commission argues were conceived and developed at the instigation of "special interests [that] often do not realize (or care

49. Based on presentation by Christophe Bellmann, Programme Director, ICTSD, "Addressing decent work concerns through trade agreements : The case of the special safeguard mechanism," at the 20 May 2009 NGLS/FES workshop.
50. UNCTAD has developed a computerized customs management system, the Automated System for Customs Data (ASYCUDA), which is already installed in more than 90 countries. Even if the system was not designed to support implementation of an SSM, the data systems in place could easily be used to monitor changes in product-specific import prices and volumes, provided customs data are centralized in a timely fashion, which UNCTAD experts say is technically feasible (Per. Com.).
51. The "prudential carve-out" provision on domestic regulation under the GATS Annex Article 2(a) would appear sufficiently ambiguous in its wording to be potentially self-nullifying. It states : "Where such [prudential] measures do not conform with the provisions of the Agreement, they shall not be used as a means of avoiding the Member's commitments or obligations under the Agreement" (Public Citizen 2009).

about) the vulnerabilities that these commitments impose on other aspects of their economy or the international economy" (UN 2009:103).

This WTO agreement on financial services so far mainly concerns developed countries. However, many developing countries have already signed or are in the process of signing financial deregulation provisions in a number of other bilateral and regional agreements which contain commitments that restrict the ability of countries to respond to the current crisis with appropriate regulatory and macroeconomic reforms (including the above mentioned capital management and heterodox monetary tools). "More broadly," the Stiglitz Commission insists, "all trade agreements need to be reviewed to ensure that they are consistent with the need for an inclusive and comprehensive international regulatory framework which is conducive to crisis prevention and management, counter-cyclical and prudential safeguards, development and inclusive finance" (UN 2009:104).

It is evident that these reviews are a necessary part of the intensified international cooperation called for in the Global Jobs Pact to "*build a stronger, more globally consistent supervisory and regulatory framework for the financial sector so that it serves the real economy, promotes sustainable enterprises, decent work and better protects the savings and pensions of people*." [52]

PROLIFERATION OF NORTH-SOUTH REGIONAL AND BILATERAL TRADE AGREEMENTS

The financial deregulation commitments in bilateral and regional trade agreements are part of a broader set of concerns voiced by civil society and other actors regarding the proliferation of North-South regional and bilateral deals that seem to have accelerated as developing countries have increased their bargaining capabilities within the WTO. Many of these agreements and those under negotiation also involve steeper tariff reductions and much tighter policy space restrictions notably with respect to investment and intellectual property rights. The ILO World Commission had expressed concern that despite possible market access gains, bilateral and regional agreements between countries of very different economic weight "*may result in unbalanced outcomes, such as more limited space for national development policies in lower income countries, or difficulties of economic adjustment that lead to job losses without resources to compensate those adversely affected*" (ILO 2004a:73).

Many civil society groups are thus calling on UN bodies to examine whether these trade agreements support or undermine efforts towards greater policy coherence at national, bilateral, regional and multilateral levels.

A GOVERNANCE VACUUM

Moreover, the international trading system is not only suffering from unfair rules, but also of an absence of rules in areas such as exchange rates (which can play the same function as trade tariffs) and commodity price speculation. These issues are linked to defects in financial governance but their effects on trade and employment are much more significant than modest movements in tariff rates and non-tariff barriers. In its submission to the

52. Paragraph 21.(1) of the Global Jobs Pact.

Stiglitz Commission, the International NGO Working Group on Trade-Finance Linkages noted in this regard:

> "The fast dissemination of the crisis shows that the fate of developing countries in the trading system does not lie so much in the achievement of enhanced market access as on meaningful reforms to the international financial architecture in which context such trade is conducted."[53]

53. See: http://www.un-ngls.org/cfr_article.php3?id_article=709.

7. SYSTEMIC REFORMS FOR FULL EMPLOYMENT AND DECENT WORK

Global responses to the economic crisis have given impetus for reform on long-standing systemic deficiencies in global economic governance. This final chapter briefly reviews some of these in terms of their direct and indirect bearing on progress toward full productive employment and decent work for all. These include international tax issues, a new international debt architecture, a new global reserve system and staving off currency speculation.

INTERNATIONAL TAX ISSUES

Where progress has been most significant is in the area of international taxation and tax cooperation. International resource transfers are an integral part of the strategies needed to finance the global social protection floor, public investments for productive employment and more generally the transition to low carbon development paths. However, the OECD-DAC is already warning that, due to the financial crisis, 2010 will be a "crunch year" for ODA.[54] Progressive taxation efforts on multiple fronts become all the more indispensable. The good news is that large fiscal deficits ensuing massive bank bailouts and stimulus packages in the rich countries have increased the political will to institute collective measures needed to combat tax evasion, tax competition and explore innovative financing mechanisms. There is still a long way to go, but some important developments are worth highlighting.

- The UN 2008 Doha Conference on Financing for Development decided to set in motion a process to consider strengthening the UN Committee of Experts on International Cooperation in Tax Matters – which the Stiglitz Commission subsequently proposed should be upgraded into an intergovernmental body to strengthen its ability to enhance international cooperation in this area, notably "*to ensure that all countries commit themselves to the voluntary automatic exchange of information that would help root out tax evasion and corruption and also the repatriation of illegal funds*" (UN 2009:83-84). In this regard, the global civil society consultation for the Stiglitz Commission highlighted among others things the need to end the practice of transnational corporations manipulating their accounts through distorted "transfer pricing" to show their profits where they are taxed least heavily, rather than where they are earned.

- The G-20 have stepped up pressure on tax havens and are exploring options on "how the financial sector could make a fair and substantial contribution toward paying for any burdens associated with government interventions to repair the banking system."[55]

54. Presentation of OECD-DAC of its new survey on future aid plans at the second meeting of the Inter-Agency Consultative Group on the Fourth UN Conference on LDCs held on 4 November 2009 in Geneva.
55. Paragraph 16 of the G-20 Leaders' Statement: The Pittsburgh Summit.

Some civil society activists have described this decision as a possible step towards establishing a **Financial Transaction Tax** (FTT) – a broader concept than a currency transaction tax (or "Tobin Tax") to encompass also taxes on other financial transactions such as in relation to bonds, equities and derivatives.[56]

• Soon after, the Leading Group on Innovative Financing for Development (regrouping nearly 60 countries from North and South as well as NGO observers) decided in October 2009 to set up a Task Force "to explore several options for financing development based on an assessment of the feasibility of an approach focused on international financial transactions." [57]

It is important to distinguish the introduction of new international taxes from measures to prevent a "race to the bottom" in terms of **tax competition** between countries to attract or retain footloose capital. The latter would eventually imply international agreements on, for example, what should be a minimum tax floor on FDI. The ILO World Commission suggested that regional initiatives to that effect among countries with comparable levels of development might be an important stepping stone in that direction (ILO 2004a).

A NEW INTERNATIONAL DEBT ARCHITECTURE

The debt crisis that hit developing countries in the early 1980s paved the way for structural adjustment policies that had a devastating and enduring impact on jobs and livelihoods. Just as their debt situation was finally improving in recent years, this new crisis – for which they had no role in causing – risks plunging many of developing countries into a new debt crisis.

The UN Conference on the world economic and financial crisis affirmed that "appropriate measures must be taken to mitigate the negative effects of the crisis on the indebtedness of developing States and to avoid a new debt crisis."[58] In this respect, *UNCTAD has called for a debt moratorium on all official debts to all low-income countries without exceptions, conditionalities or performance criteria* (UNCTAD 2009). The IMF has since decided to suspend interest payments on low-income country debt up to 2011. According to UNCTAD, this is a step in the right direction but is not sufficient, given that the suspension only covers interest payments rather than much larger repayments on principal; and the time-frame is too short in light of prospects of only slow recovery.[59] Many civil society organizations are concerned that emergency support to developing countries is in the form of loans rather than grants – and sometimes subject to pro-cyclical conditionality as discussed in Chapter 4. They have called for **unconditional debt cancellation** as part of crisis response measures that would not be drawn from existing and new ODA resources (NGLS 2009a).

Beyond that, many voices are calling for fundamental reform of the international debt architecture. Some of the ideas on the table were already developed in the aftermath of the 1997-98 East Asian crisis, but soon lost steam as developed countries dropped their support for meaningful financial architecture reform in the euphoric speculative boom that

---

56. Joint NGO letter to IMF Managing Director dated 11 November 2009 concerning: "Request for civil society participation in IMF study on how the financial sector can help pay for the bailouts."
57. See Declaration: http://www.leadinggroup.org/article465.html.
58. Paragraph 33 of the Conference Outcome Document.
59. Yuefen Li, UNCTAD (Per. Com.).

followed (UNCTAD 2001). This includes the proposal for a **fair and equitable debt workout mechanism** that would allow debtor countries in difficulty to declare a unilateral "standstill" on debt payments, with creditors having to abide by the terms for debt restructuring of an independent arbitration panel. More fundamentally, civil society groups are calling for a rethink of current debt sustainability criteria that would not be based on debt-to-export ratios, but on sustainable development criteria. One specific criterion that many groups have been advocating for some time would be the domestic resources needed to meet the MDGs (NGLS 2009a). What would the criteria imply if estimated domestic resources required would integrate the new MDG target of full and productive employment and decent work for all?

THE BALANCE-OF-PAYMENTS CONSTRAINT (PART 2)

Chapter 5 reviewed the conventional approach to the "balance-of-payments constraint" that places limits on what developing countries can achieve without facing a balance-of-payments crisis (which causes a chain reaction often leading to mass unemployment and deterioration of social conditions). This section examines an alternative approach that Professor Joseph Stiglitz presented at the ILO Global Employment Forum in November 2001 and which he referred to as the "**trade deficit trap**."

Professor Stiglitz argued that an essential dimension of international financial reform is related to the question of trade deficits. He said that in the current doctrine, "countries with large trade deficits are told to cut them back," but without comparable pressure on large surplus countries. If a country cannot boost its export earnings sufficiently to close its trade deficit, it depends on capital inflows to make up the difference. If these are not sufficiently forthcoming or the deficit is prolonged for too long, to avoid a crisis the country must sooner or later turn to the IMF for help, which one would expect would provide resources for expansionary policies to avoid cut backs on imports that would have negative spill-over effects on export-related jobs in other countries.

However, the IMF had not only abandoned its original mandate, Professor Stiglitz noted: it had taken up "the opposite banner," all too often providing funds to countries only on the condition that they engage in measures to reduce imports and reassure foreign investors. Since the raising import barriers is discouraged, there remain few options but to cut back effective demand through contractionary policies, despite their contribution to global slowdown and their predictable toll on job losses and cut backs in public services. "The sum of all trade surpluses minus deficits must add up to zero," he continued. If some countries insist on having large surpluses, other countries must have correspondingly large deficits. "*The deficits are like hot potatoes: as one country is forced to eliminate its deficit, it must show up somewhere else in the system. With a focus on trade deficits, no wonder then there is always an impending crisis somewhere in the world*" (NGLS 2002:5).

TOWARDS A NEW GLOBAL RESERVE SYSTEM?

The solution to this systemic impediment that Professor Stiglitz proposed at the ILO in 2001 was a cornerstone of the Stiglitz Commission recommendations and in the negotiations for the 2009 UN Conference on the world financial and economic crisis – the move towards a **new global reserve system**. The idea was originally proposed by John Maynard Keynes some eighty years ago in his 1930 *Treatise on Money*. Current discussions on the need for a

new global reserve system are usually linked to the systemic risks posed by global imbalances and the fragility of the US dollar as the world's *de facto* reserve currency. However, another angle to examine the same problem is the fact that ***the present global reserve system is incompatible with global full employment*** *and is inequitable*. The following sections explain why and what are some of the ideas on the table for reform at global and regional levels.

In making his proposal at the 1944 Bretton Woods Conference for an *International Clearing Union* with an international reserve currency named the "**bancor**," Keynes was concerned that the above-mentioned asymmetric adjustments between trade deficit and surplus countries would tend towards a ***deficiency of global aggregate demand*** (money is hoarded instead of spent in the surplus countries, while import demand is cut back in deficit countries). This asymmetry also implied a ***constraint on the policy space needed for policies in support of full employment***. Adjustments to these imbalances could be smoothed with the emission of this international reserve currency that would act as a buffer to compensate deficit countries for the gap created by foreign exchange reserves "hoarded" in countries that maintain structural surpluses. More equitable ("symmetric") disciplines were also envisaged for both deficit and surplus nations. This concern was never adequately addressed at Bretton Woods, which partly explains the above-mentioned "trade deficit trap."

The deflationary bias of the system has been compensated to some extent by the fact that the United States, as emitter of the world's global reserve currency, has been able to sustain large trade deficits for a long time. The United States is not only the "consumer of last resort," but also the "deficit of last resort." The problem of using a *national* currency as an *international* reserve currency was identified by Robert Triffin in the 1950s and has become known as the "**Triffin dilemma**" : dollar deficits necessary to increase global liquidity can erode confidence in the dollar as a reserve currency. There are other reserve currencies, but the dollar still remains the main choice for settling international payments. With confidence in the dollar eroding, holders of large dollar-denominated reserves have an incentive to diversify, but further diversification away from dollar holdings may precipitate a downfall of their remaining dollar assets. A disorderly collapse in the dollar's value could be the cause of yet another global financial crisis.

A move to a multiple currency reserve system based on multiple, competing reserve currencies, would not resolve the problems associated with the current system ; it would in fact add an extra layer of instability. Indeed, matters have been made much worse since the breakdown, in the 1970s, of the Bretton Woods system of fixed exchange rates tied to the gold convertibility of the dollar. The move to flexible exchange rates among the major currencies, combined with widespread relaxation of controls on capital movements, has dramatically increased global instability and the frequency of crises, as well as the inability to guarantee full employment.

Especially since the 1997-98 East Asian crisis, developing countries that could afford it have been accumulating very large foreign exchange reserves as a buffer against future crises and to create the policy space to respond if they occurred. This view was reinforced with the record of pro-cyclical policy conditions imposed by the IMF as the only "collective insurance" system at the global level. In addition, restrictions on the ability to use industrial policies to encourage nascent industries in emerging economies under recent WTO agreements may have led some countries to substitute exchange rate policies to effect similar outcomes, thus contributing to reserve accumulation (UN 2009).

As a result of these factors, reserve accumulations more than doubled in the decade after the East Asian crisis, rising from 5.6 percent of world GDP in 1997 to 11.7 percent in 2007. Reserve accumulation in the period 2003-2007 amounted to an annual average of US$777 billion, or 1.6 percent of GDP. When these reserves are "earned" through trade surpluses as opposed to being "borrowed" through foreign capital inflows, there is a deficit in global aggregate demand. Thus the system is incompatible with global full employment; but it is also highly inequitable: developing countries have been transferring resources (typically at very low interest rates) to the developed countries that issue the reserve currencies. That amount was estimated at US$3.7 trillion in 2007. *The difference between the lower lending rate and the higher interest rate that developing countries pay developed countries when they borrow from them represents a net transfer of resources from poorer to wealthier countries*. In proportion to GDP, the amount of reserves that developing countries have been holding is multiple times greater than developed countries: 26.4 percent for developing countries versus 4.8 percent for high-income OECD countries in 2007 (UN 2009).

HOW WOULD THE SYSTEM WORK?

Since the global economic crisis, Keynes' idea of a new global reserve system is back on the international agenda. It is now implicitly part of the follow-up to the UN Conference on the world economic and financial crisis (see below). Considerable discussion will be needed for the international community to decide the precise arrangements. According to the Stiglitz Commission, the basic idea would be the annual emission of an international currency that would be targeted to offset the increase in "non-borrowed" reserves – meaning to compensate for reductions in global purchasing power resulting from excessive reserve accumulation. The system of allocation could also have built-in incentives or penalties to discourage countries from maintaining large surpluses. It could build on the potential new source of global liquidity known as **Special Drawing Rights (SDRs)**[60] that was created in the 1960s. The potential of SDRs was never fulfilled (with only minimal emissions in 1970-72 and 1979-81). However, the recent approval by the IMF (as a result of a decision at the April 2009 London G-20 Summit) of a new emission of SDRs equivalent of US$250 billion constitutes an important breakthrough on which more fundamental reforms could evolve. In this regard, the UN Conference on the world financial and economic crisis agreed that:

> "The crisis has intensified calls by some States for reform of the current global reserve system to overcome its insufficiencies. We acknowledge the calls by many States for further study of the feasibility advisability of a more efficient system, including the possible function of SDRs in any such system and the complementary role played by various regional arrangements."[61]

A major stumbling block is inequitable allocation of SDRs, which is tied to a country's IMF quota (in turn derived from its weight in the global economy) rather than a country's need. Another problem is widespread scepticism about the IMF being in a position to administer the system, at least in the absence of fundamental governance reform. An alternative proposed by the Stiglitz Commission is to assign this role to a new institution such as a

60. SDRs are valued as the weighted average of the major currencies. In July 2009, the SDR basket contained the value of 0.632 US dollars, 0.410 euros, 0.0903 pounds sterling and 0.0543 yen (UNCTAD 2009).
61. Paragraph 36 of the Conference Outcome Document.

"Global Reserve Bank." The Stiglitz Commission outlines a variety of options on how the system could function. In its more sophisticated version, the system would allocate SDRs on the basis of "need" (which could be equated to estimated demand of reserves) in a counter-cyclical fashion. It could also enable to provide revenues to finance development and global public goods via multilateral development banks – an old idea already proposed by an UNCTAD panel of experts in the 1960s (UNCTAD 2009). The UN Conference recognized in this regard "*...the need for keeping under review the allocation of SDRs for development purposes*." [62]

According to the Stiglitz Commission, there are many reasons why major reserve currency countries, including the United States, would find it in their interest to join such a system. There are of course the benefits of a more stable global economy that can more readily operate at full employment. In the current system, the United States has the benefit of borrowing at low cost, but also suffers from its role in supplying global reserves. The demand for global reserves has led to increasing current account deficits in the United States that have had adverse effects on US export-related jobs : when dollars are held to meet demands for liquidity in surplus countries, there is no countervailing increase in demand for US goods. This necessitates the US maintaining persistent fiscal deficits, if it wishes to keep the economy at or near full employment. And the periodic need to correct these deficits requires contractionary monetary or fiscal policies that have adverse effects on the domestic US economy as well as the world economy (UN 2009). [63]

Besides strengthening political support for wider and more equitable use of SDRs, some analysts point to the need to build confidence in the use of SDRs as an accepted means of international payments – so as to bypass the need to convert SDRs in dollars or other hard currencies before making such payments. [64]

A "BOTTOM-UP" REGIONAL APPROACH ?

Given the complexities and political resistance involved, it may be difficult to achieve the transition through a global agreement from the outset. Civil society organizations have also expressed reservations of a global system built from the "top down" – where asymmetries between "hard" currency and "soft" currency countries could lead to an inequitable outcome. An alternative, also proposed by the Stiglitz Commission, would be a "bottom-up" approach through existing and new regional initiatives involving currency swap arrangements or even pooling of reserves that could enable the issuing of a new reserve asset (a "*regional SDR*") that could be used at regional or even global levels. [65]

62. Paragraph 35 of the Conference Outcome Document.

63. According to the Stiglitz Commission, the costs for the US far outweigh the benefits of the current system, especially now that major shareholders of dollar reserves are worried about the value of their reserves should the US adopt policies leading to a depreciation of the dollar. The only way to respond to these concerns would involve a loss of monetary autonomy for the US as it would have to take into consideration the effects of its monetary policy on the rest of the world and perceptions of these impacts (UN 2009).

64. See for example, Aldo Caliari "Can the G20 have it both ways ? Addressing global imbalances without reform of the world monetary system," Center of Concern : http ://www.coc.org/node/6441.

65. In Asia, for example, a high-level meeting of senior officials of finance ministries and central banks of the region held in Dhaka in July 2009 supported "regional arrangements that lessen reliance on traditional reserve currencies, such as multilateral systems for payments of trade transactions with domestic currency, complemented by regional units of account and clearing unions. These could eventually become the basis of regional currencies. Such arrangements would have the added value of increasing fiscal space – by relaxing pressure on hard currency reserves – >>>

Regional initiatives could become part and parcel of the global reserve system. Some have suggested that the reformed IMF should be a network of such regional reserve funds. Such a decentralized system would have the advantage of better solving problems with crises in the smaller countries at the regional level, in which they would also have a greater voice. One way to link regional and global arrangements would be to make contributions to regional arrangements one added factor in determining SDR allocations (UN 2009).

STAVING OFF CURRENCY SPECULATION FOR STABLE EMPLOYMENT

The move to a new global reserve system can help deal with chronic liquidity short falls and some of the asymmetries in the current system described in this volume. Together with the use of appropriate capital management techniques, it could increase the "armoury" available to national or regional authorities to combat (among other systemic risks) currency speculation, and the devastating toll that currency gyrations cause to enterprises and workers around the world. But would it be enough?

According to UNCTAD, the longer term solution would involve a multilateral agreement for managing exchange rates so that "real" exchange rates remain stable at a sustainable level. It is premised on the notion that, contrary to mainstream theory, currency markets have a tendency to "get the price wrong" through speculative arbitrage between interest rates that lead to "overshooting" and "undershooting" of currency values. So the task of managing exchange rates should be returned to governments, but there are limits to what individual monetary authorities can do on their own – thus the call for international cooperation. In the proposed system, the "nominal" exchange rate would be adjusted periodically using inflation differentials as the main guide (so the "real" exchange rate remains stable), and the value of each currency would be anchored to a new artificial currency – whether SDR or some other international unit of account. The difficulty would be in determining the initial purchasing parities of each currency, but then coordinated "symmetrical" interventions from member central banks (through essentially emissions of the appreciating currencies to buy up enough of the devaluating currency) would by and large defeat the arbitrage strategies of speculators. Again, regional initiatives might be the most realistic way forward. **Currency swap arrangements** are already part of regional agendas under construction in Latin America and Asia (UNCTAD 2009; NGLS 2009b).

It remains unclear whether such a system would necessarily involve a loss of monetary policy autonomy, as is the case for Eurozone member countries, although more policy space would be gained in other areas. In addition, by removing exchange rate tools, would there be intensified pressures on domestic labour markets to become more "competitive?" According to UNCTAD's current chief macro-economist, Heiner Flassbeck, the answer is yes: to avoid "**wage dumping**," the system would also need to include an agreement by member countries to take the necessary steps needed to ensure that average wages rise in line with productivity growth (NGLS 2009b).

>>> and boost intra-regional trade, thus help in mitigating the impact of trade-related shocks." (See paragraph. 33 of the Dhaka Outcome Document: http://www.coc.org/system/files/Outcome+Document.pdf.) Similar discussions are taking place in Latin America on a "New Regional Financial Architecture" built around three pillars: the Bank of the South (*Banco del Sur*); the Common Reserve Fund of the South (*Fondo Común de Reservas del Sur*); and a regional settlements clearing system based on a new currency unit called SUCRE (*Sistema de Compensación Regional de Pagos*). Source: Ecuadorian Technical Commission for a New Regional Financial Architecture (Per.Com.).

As we have seen throughout this volume, the need for decisive progress on **aligning wages with productivity growth** is an essential cross-cutting priority. Any rigid legally-binding agreement, if desirable, might be difficult to achieve, at least from the outset. But certainly, there would need to be much more public debate at national and international levels on what should be the panoply of policies and institutions required in different contexts to reach that goal (as we have seen some of them well beyond the remit of the ILO and labour institutions). Progress on that front alone could make a decisive difference in efforts to rebalance growth patterns and (together with other policies such as redistributive taxes) reverse systemic income inequalities associated with globalization.

8. CONCLUSIONS

1. A FRAMEWORK FOR ACCOUNTABILITY AND COHERENCE

The decent work and fair globalization agenda can become a powerful tool to raise standards of accountability in economic governance. It provides a means to assess the effectiveness of economic policies that goes well beyond conventional measures such as growth rates, export performance or low inflation. The litmus test is what national and international economic policies are doing in terms of supporting or undermining the goals of full and productive employment and decent work for all. This agenda can also help articulate a wide range of issues, from social protection to macroeconomic financial and trade reforms, into a coherent framework. For instance, investments in social protection systems lessen not just the social but also the economic impact of recessions. Conversely, the various capital management tools and alternative macroeconomic policies described in this volume can limit not just economic instability (and thus the burden on social protection systems) but also help redirect finance towards long-term investments in productive employment, including "*green jobs*" in sectors that can promote low-carbon development paths.

2. CONNECTING WITH NATIONAL POLITICAL PROCESSES

The decent work-fair globalization nexus also helps to better connect civil society campaigns with national political processes – where elections are won or lost over the question of jobs. This publication provides some tools to engage more effectively in such debates, in a manner that goes beyond conventional ideological cleavages regarding the respective roles of the State and market in creating full and productive employment. It outlines a range of alternative public policies that can help better align entrepreneurial decisions with social and environmental objectives. It also articulates the relationship between national political debates on employment and their international dimensions, including changes needed in global economic governance to make the economy not only fair, but compatible with global full employment.

3. DECENT WORK IS A "WIN-WIN" PROGRAMME FOR SOCIETY AND THE ECONOMY

The multi-stakeholder discussions held in preparation for this publication highlighted the "public goods" quality of the decent work agenda: from a macroeconomic perspective, all actors benefit from widespread progress on the decent work agenda – this means higher consumer demand and thus higher sales revenue which can lead to further investments in productive jobs, thus creating a virtual circle in which decent work promotion is the pivotal link.

However, the short-term, high return expectations of deregulated financial markets impose incentives that go in the opposite direction. As one participant with a background in financial services noted at an NGLS co-sponsored workshop, "the credit ratings of enterprises and countries are very often *inversely* related to progress on the decent work agenda –

where job layoffs by companies are rewarded, where progressive policies such as raising the minimum wage are often penalized." This publication suggests some avenues for new regulatory frameworks that can help reverse this trend.

4. THE MDGS AND THE DECENT WORK AGENDA

The years 2010-2015 provide a decisive opportunity to promote the decent work agenda as part of the overall development agenda of the UN. In 2010 the United Nations will review progress towards realizing the Millennium Development Goals (MDGs), including progress made in relation to the new MDG target on "full and productive employment and decent work for all" (added as a result of the 2005 MDG review). This publication suggests that the new target brings with it a much more comprehensive and incisive analytical framework to assess whether economic policies are helping or hindering progress towards the realization of the MDGs. It also shows the links with other important international processes, including follow-up to the proposals in the Global Jobs Pact and the recommendations of the Stiglitz Commission on financial and monetary reforms.

5. A HUMAN RIGHTS AGENDA FOR ECONOMIC REFORM

The different dimensions of decent work are firmly anchored in universal human rights. An implicit human rights proposal that runs throughout this volume is the extension of "affirmative action" into economic policy. Then UN High Commissioner for Human Rights Mary Robinson in 2002 had introduced this concept in relation to reforming global trade rules. She noted that "non-discrimination" under human rights law may require "affirmative action" to protect the weaker and more vulnerable players, as equal rules among very unequal players could result in the "institutionalization of discrimination" against the weakest. The implication was the need for more policy space for developing countries, discussed in Chapter 6.[66] This publication has shown how affirmative action could also be extended to other areas of economic policy, whether to support employment growth in smallholder agriculture, small and medium-sized enterprises, or socially and environmentally desirable projects that do not get backing from the market.

This publication has also provided concrete tools to determine whether economic policies measure up to the human rights principles of "progressive realization" and "non-retrogression" of decent work-related human rights. This applies to national policies (such as whether resources and institutions are aligned so as to maximize the promotion full productive employment and social protection for all), but also to "extra-territorial obligations" under human rights law. These imply duties to help fulfil human rights through international cooperation and to not impede the ability of other State parties to fulfil domestic human rights obligations (such as through inappropriate conditionalities, or unfair trade and investment agreements).

66. Report of the High Commissioner for Human Rights to the 2002 session of the UN Commission on Human Rights (E/CAN.4/2002/54). The concept of affirmative action in trade policy was also a center-piece recommendation in the 2004 Report of the World Commission on the Social Dimension of Globalization (ILO 2004).

Much more progress is needed in the realization of the "social and international order" in which the rights set forth in the Universal Declaration on Human Rights can be fully realized. This especially applies to reforms of the international financial architecture needed to make it more stable, equitable and compatible with full employment.

Heterodox economic policies can be used for good or ill, so all these efforts cannot be dissociated from civil and political rights to participation, transparency and accountability – at national and international levels.

6. "Deglobalization" or better "localization"?

Some actors have described the increasing calls for a shift from export-led growth towards greater reliance on domestic demand-led growth as equivalent to "deglobalization," which has been called for by many civil society organizations since the 1997-98 East Asian crisis. Others are concerned that "deglobalization" is a concept that goes too far, especially for very small economies that rely on exports to generate enough productive jobs. What is clear is that a "fair globalization" implies addressing the imbalance between the "global" and the "local" discussed in Chapter 2. It means giving more emphasis on the need for a successful "localization" that requires a framework of rules and policies much more conducive to generating more and better jobs in sectors that produce for the local market, where the majority of people and the poor are employed. This is important to address an essential dimension of the decent work and fair globalization agenda not covered in this volume: namely the issue of international migration. Much of the debate on migration has focused on the human rights of migrants, including their right to decent work, and countering the reactionary political backlash against intensified immigration in many parts of the developed world. But the other side of the migration debate needs to get much more visibility: how to generate enough productive employment opportunities in the areas where most people would choose to stay if given a chance at a decent job and livelihood?

7. Creating space for alternatives

The economic alternatives exposed in this publication are by and large inspired from the Keynesian tradition of correcting market failures and guiding (or "animating") entrepreneurial spirits and investment decisions towards desirable social goals. But there needs to be spaces to experiment with alternatives that go well beyond market-based incentives anchored on competition. Entrepreneurship based on the principles of cooperation and stewardship can also lead to quality productive employment. The NGLS global civil society consultation for the Stiglitz Commission revealed a range of alternatives, such as cooperatives, that need to be encouraged to flourish through a different set of financial rules and institutions than the ones that prevail today (NGLS 2009a).

This might include different mechanisms to support a "green jobs agenda for the South." Much of the competitive edge for green technologies and thus the creation of new green jobs will emanate from industrialized countries and large emerging economies. In tandem with the financial and technology transfers discussed in climate negotiations, the application of an alternative development paradigm based on expanding productive capacities for productive employment can help low-income countries build their own green jobs agenda. But there are limits to what even "guided" markets can achieve in other key areas for low-

income countries, such as employment creation aimed at restoring biodiversity and large-scale reforestation.

A core agenda for future policy dialogue will be what innovative financial mechanisms and institutions can do to support decent work opportunities for promoting global and local public goods – whether related to climate change adaptation and mitigation, or local environmental and community rejuvenation. Most of these require something very different from market-based mechanisms.

The importance of generating publicly-financed employment is all the more important when the pace of capital accumulation in the private sector is not strong enough to generate enough employment, or overcome possible trade-offs between productivity growth and employment growth. Innovative taxes and the more sophisticated proposals for a new global and regional reserve system represent some of the promising avenues outlined in this publication to take this agenda forward.

references

ACTIONAID, Bank Information Center and European Network on Debt and Development. 2008. *Quick Fixes or Real Solutions? World Bank and IMF responses to the global food and fuel crises*, Brussels.

AKYÜZ, Yilmaz. 2006. "From Liberalization to Investment and Jobs: Lost in Translation." *Working Paper* No. 74. Policy Integration Department, International Labour Office, Geneva.

AKYÜZ, Yilmaz. 2008. "Global Rules and Markets: Constraints over Policy Autonomy in Developing Countries." *Working Paper* No 87. Policy Integration Department, International Labour Office, Geneva.

BACCARO, Lucio. 2008. "Labour, Globalization and Inequality: Are Trade Unions Still Redistributive." *Discussion Paper* (DP/192/2008). International Institute for Labour Studies, International Labour Organization, Geneva.

BALAKRISHNANA, Radhika, Diane Elson and Raj Patel. 2009. *Rethinking Macro Economic Strategies from a Human Rights Perspective*. Marymount Manhattan College, New York.

CENTRE FOR ENVIRONMENT CONCERNS. 2009. *Delivering NREGS: Challenges and Opportunities, A Practitioner's Experiences*. Centre for Environment Concerns, Hyderabad.

CEPR. 2009. "Empowering the IMF: should Reform be a Requirement for Increasing the Fund's Resources?" Center for Economic Policy and Research, Washington D.C.

CHANG, Ha-Joon. 2002. *Kicking Away the Ladder*. Anthem Press, London.

CHEN, Shaohua and Martin RAVALLION. 2008. "The Developing World is Poorer than We Thought, But No Less Successful in the Fight against Poverty." *World Bank Policy Research Working Paper* 4703. August 2008, Washington D.C.

DAMILL, Mario, Roberto FRENKEL and Roxana MAURIZIO. 2007. "Macroeconomic policy changes in Argentina at the turn of the century." In NOVICK et al (2007) *Research Series 114*. International Institute for Labour Studies, International Labour Organization, Geneva.

DESA. 2010. *World Economic Situation and Prospects 2010*. United Nations Department of Economic and Social Affairs, New York.

DESA. 2008. *World Economic and Social Survey 2008: Overcoming Economic Insecurity*. United Nations Department of Economic and Social Affairs, New York.

DOUMBIA-HENRY, Cleopatra and Eric GRAVEL. 2006. "Free trade agreements and labour rights: recent developments." In *International Labour Review*, Vol. 145, No. 3. International Labour Organization, Geneva.

Drache, Daniel. 1997. “The Short But Amazingly Significant Life of the ITO, Free Trade and Full Employment: Friends or Foes Forever?” York University, Toronto.

Elson, Diane. 2007. “Macroeconomic Policy, Employment, Unemployment and Gender Equality.” In Ocampo, José Antonio and Jomo K.S. (2007) *Towards Full and Decent Employment*. Zed Books: London & New York, Orient Longman: Hyderabad, Third World Network: Penang (published in association with the United Nations).

Epstein, Gerald. 2007a. “Central Banks as Agents of Employment Creation.” In Ocampo, José Antonio and Jomo K.S. (2007) Towards Full and Decent Employment. Zed Books: London & New York, Orient Longman: Hyderabad, Third World Network: Penang (published in association with the United Nations).

Epstein, Gerald. 2007b. “Central banks, inflation targeting and employment creation.” *Economic and Labour Market Papers* (2007/2). International Labour Office, Geneva.

Galbraith, James. 2009. “Financial and Monetary Issues As the Crisis Unfolds.” *Public Policy Brief* No.103. The Levy Economics Institute of Bard College, Blithewood.

Heintz, James and Robert Pollin. 2008. *Targeting Employment Expansion, Economic Growth and Development in Sub-Saharan Africa: Outlines of an Alternative Economic Programme for the Region*. United Nations Economic Commission for Africa, Addis Ababa.

Ilo/Iils. 2009. *The Financial and Economic Crisis: A Decent Work Response*. International Labour Office, International Institute for Labour Studies, Geneva.

Ilo. 2004a. *A Fair Globalization: Creating Opportunities for All*, Report of the World Commission on the Social Dimension of Globalization. International Labour Organization, Geneva.

Ilo. 2004b. *Economic Security for a Better World*. Programme on Socio-economic Security, International Labour Office, Geneva.

Ilo. 2008a. “Decent Work for Sustainable Development in the Era of Globalization: Statement to UNCTAD XII, Accra, 21-25 April 2008.” International Labour Organization, Geneva.

Ilo. 2008b. “Can low-income countries afford basic social security?” *Social Security Policy Briefings*, Paper 3. International Labour Office, Geneva.

Ilo. 2008c. “Report of the ILO Forum on Decent Work for a Fair Globalization, Lisbon, Portugal, 31 October-2 November 2007.” International Labour Office, Geneva.

Ilo. 2009a. “Report of the Committee of the Whole on Crisis Response,” Provisional Record 19, International Labour Conference, 98th Session. International Labour Office, Geneva.

ilo. 2009b. “Protecting people, promoting jobs: A survey of country employment and social protection policy responses to the global economic crisis: An ILO report to the G20 Leaders’ Summit, Pittsburgh, 24-25 September 2009.” International Labour Office, Geneva.

ILO. 2009c. "From crisis response to recovery, jobs and sustainable growth." Statement by ILO Director-General to the International Monetary and Finance Committee and Development Committee, 4-5 October 2009, Istanbul.

ILO. 2010. *Global Employment Trends*: January 2010. International Labour Office, Geneva.

ILO/WTO. 2007. *Trade and Employment: Challenges for Policy Research*, a joint ILO/WTO Secretariat study prepared by Jansen, Marion and Eddy Lee, Geneva.

IMF. 2009. *World Economic Outlook 2009*. International Monetary Fund, Washington D.C.

JENKINS, Hamish, Gerry RODGERS and Eddy LEE. 2007. "The quest for a fair globalization three years on: Assessing the impact of the World Commission on the Social Dimension of Globalization." *Discussion Paper* (DP/175/2007). International Institute for Labour Studies, International Labour Organization, Geneva.

JOMO K.S. 2007. "Towards Full Employment and Decent Work: An Introduction." In OCAMPO, José Antonio and JOMO K.S. (2007) *Towards Full and Decent Employment*. Zed Books: London & New York, Orient Longman: Hyderabad, Third World Network: Penang (published in association with the United Nations).

LEE, Kang-kook, and Arjun JAYADEV. 2005. "Capital Account Liberalization, Growth and the Labor Share of Income: Reviewing and Extending the Cross-country Evidence." In EPSTEIN, Gerald (ed.) *Capital Flight and Capital Controls in Developing Countries*. Edward Elgar Press, Northampton.

KEYNES, John Maynard. 1963. "Inflation and Deflation" (originally published in 1919). In *Essays in Persuasion*. W.W. Norton & Company, New York.

MCPHERSON, Malcom. 1999. "Seignorage in Highly Indebted Developing Countries." *Development Discussion Paper* No. 969. Harvard Institute for International Development, Harvard University, Cambridge.

MKANDAWIRE, Thandika. 2001. "Thinking About Developmental States in Africa." In *Cambridge Journal of Economics* 25:289-313, Cambridge.

MOLINA-GALLART, Nuria. 2009. *Bail-out or blow-out? IMF policy advice and conditions for low-income countries at a time of crisis*. European Network on Debt and Development, Brussels.

NGLS. 2000. "UNCTAD X Addresses Crisis of Global Economic Governance." *NGLS Roundup* 54, May 2000. United Nations Non-Governmental Liaison Service, Geneva.

NGLS. 2002. "ILO Employment Forum: A Global Agenda for Employment." *NGLS Roundup* 84, January 2002. United Nations Non-Governmental Liaison Service, Geneva.

NGLS. 2009a. *Civil Society Consultation on the Work of the President of the UN General Assembly's Commission of Experts on Reforms of the International Monetary and Financial System*. United Nations Non-Governmental Liaison Service, Geneva.

NGLS. 2009b. "UNCTAD proposes new multilateral regime to stave off currency speculation: Interview with Mr. Heiner Flassbeck, Director of UNCTAD's Division on Globalization and Development Strategies." In *Go Between 118,* Dec.08-Jan.09. United Nations Non-Governmental Liaison Service, Geneva.

NOVICK, Marta, Carlos TOMADA, Mario DAMILL, Roberto FRENKEL and Roxana MAURIZIO. 2007. "In the wake of the crisis: Argentina's new economic and labour policy directions and their impact." *Research Series 114*. International Institute for Labour Studies, International Labour Organization, Geneva.

PRASAD, Naren. 2008. "Policies for redistribution: The use of taxes and social transfers." *Discussion Paper* (DP/194/2008). International Institute for Labour Studies, International Labour Organization, Geneva.

PROVE, Peter. 2009. "The Basic Income Grant (BIG) Pilot Project in Namibia." Presentation to United Nations Human Rights Council Social Forum, 1 September 2009. Lutheran World Federation, Geneva.

PUBLIC CITIZEN. 2009. "No Meaningful Safeguards for Prudential Measures in World Trade Organization's Financial Services Deregulation Agreements." Special Pittsburgh G-20 Report. Public Citizen, Washington D.C.

STIGLITZ, Joseph. 2003. *The Roaring Nineties: Why We're Paying the Price for the Greediest Decade in History*. Penguin, London.

TWN. 2009. "The IMF's Financial Crisis Loans: No Change in Conditionalities." Third World Network, Penang.

UN. 2009. *Report of the Commission of Experts of the President of the United Nations General Assembly on Reforms of the International Monetary and Financial System*. United Nations, New York.

UNCTAD. 1995. *Trade and Development Report, 1995*. United Nations Conference on Trade and Development, Geneva.

UNCTAD. 1997. *Trade and Development Report, 1997*: *Globalization, Distribution and Growth*. United Nations Conference on Trade and Development, Geneva.

UNCTAD. 1998. *Trade and Development Report, 1998: Financial Instability; Growth in Africa*. United Nations Conference on Trade and Development, Geneva.

UNCTAD. 2001. *Trade and Development Report, 2001: Global Trends and Prospects, Financial Architecture*. United Nations Conference on Trade and Development, Geneva.

UNCTAD. 2004. *World Investment Report 2004*. United Nations Conference on Trade and Development, Geneva.

UNCTAD. 2005. "Trade Liberalization and Economic Reform in Developing Countries: Structural Change or De-Industrialization?" *Discussion Paper* No 179. United Nations Conference on Trade and Development, Geneva.

UNCTAD. 2006. *The Least Developed Countries Report 2006: Developing Productive Capacities*. United Nations Conference on Trade and Development, Geneva.

UNCTAD. 2009. *Trade and Development Report, 2009: Responding to the global crisis; Climate change mitigation and development*. United Nations Conference on Trade and Development, Geneva.

Van der Hoeven, Rolph and Malte Lübker. 2007. "Financial Openness and Employment: The Need for Coherent International and National Policies." In Ocampo, José Antonio and Jomo K.S. (2007) *Towards Full and Decent Employment*. Zed Books: London & New York, Orient Longman: Hyderabad, Third World Network: Penang (published in association with the United Nations).

World bank. 2010. *Global Economic Prospects 2010: Crisis, Finance and Growth*. World Bank, Washington D.C.

Wray, Randall. 2007. "The Employer of Last Resort Programme: Could it work for developing countries?" Economic and Labour Market Papers (2007/5). International Labour Office, Geneva.

ANNEX I

Competing Theories on Wages and Full Employment : An Overview *

ABSTRACT

The following presents a brief overview of various theories on the determination of wages, and on the relationship between wages, unemployment, and inflation. The initial portions dealing with standard theories on the subject are largely based on two commonly used macroeconomics textbooks, "Macroeconomics" by Olivier Blanchard and "Principles of Macroeconomics" by N. Gregory Mankiw. Mankiw depicts the labour market using a supply and demand model, while Blanchard's explanation involves wage setting and price setting relationships. Both of these theoretical interpretations reach nearly identical conclusions on the causes of unemployment, its relationship to inflation, and on policy recommendations. The latter sections draw on alternative schools of thought that question the orthodox theory that has guided economic policies with respect to the labour market in the last two or three decades.

ORTHODOX APPROACHES TO WAGE PRICE DETERMINATION

To explain the determination of the nominal wage level (the figure that appears on a pay check without taking into account its "real" purchasing power, relative to changing prices for goods and services), Blanchard begins with the idea that wages are determined first and foremost by two factors : the expected price level in the economy, and the unemployment level.[i] If the unemployment level is higher, then workers have less leverage to demand higher wages from firms. A different way of expressing this is that wages are determined by the supply (people who want to work) and demand (firms who want to hire people) for labour ; unemployment means that the supply of labour exceeds the demand for it. For those who believe in the ultimate efficiency of market, if there is unemployment, and no outside interference, the level of wages should decrease, causing firms to hire more workers until the excess unemployment no longer exists.

The price level is important because if workers expect a rise in prices, commonly referred to as inflation, then they will demand higher wages. The "real wage," measured by the amount of goods that a worker can buy rather than the nominal wage that he or she receives, is what will be most important to the workers. Some economists also add a third

* This paper was prepared by Joshua P. Greenstein, Research Assistant and pursuing a PhD at the New School for Social Research, New York City.

element determining wages, which includes such factors as the presence of unions or other collective bargaining apparatus, unemployment insurance and minimum wage laws, all of which would be expected to raise the wage level.[ii] Another important factor in determining wages is the average productivity of workers. Productivity refers to the amount of value, such as units of a certain good, produced per worker. If, for example, a new technology allows the same amount of workers to produce more of a certain good, this will also affect wages. Mainstream theory states that, as workers' productivity rises, wages should increase in "real" terms. Firms will be able to produce more goods while paying the same wages, and so price level should fall while nominal wages remain the same.[iii]

WAGES, INFLATION, AND "NATURAL" UNEMPLOYMENT

If wages are largely influenced by unemployment and real or expected changes in price level, a major area of inquiry in economics has been how these three factors interact. Probably the most famous explanation of this relationship is known as the "Phillips curve," named after the economist who first introduced the idea in the late 1950s. Phillips showed a negative correlation between unemployment and inflation in the United Kingdom. This means that in years with low unemployment, there was high inflation, in years with high unemployment, there was low inflation. A few years later, Paul Samuelson and Robert Solow published an article showing the same relationship in the United States.[iv] This is one of the most important theories in crafting monetary policy-the idea that there is a trade-off between inflation and unemployment. Both standard labour market models offer closely related explanations for this phenomenon. One is through aggregate demand, the total demand for goods and services in an economy. An increase in aggregate demand (people want to buy more goods and services) should raise the price level in an economy, at least in the short term. Further, increased demand mean firms need to produce more goods and services, which means they need to hire more workers, which decreases unemployment.[v] If the supply, the number of workers is the same, then wages will rise. The wage setting price setting model explanation is known as the "wage price spiral."[vi] In this explanation, rather than beginning with aggregate demand, the focus is on unemployment and wages first, and on the effect on supply. A lower level of unemployment leads to a higher nominal wage (less leverage for firms, more for workers). Because the higher wage increases firm s' costs, they raise prices to maintain their profit level. The higher price level then leads the workers to once again demand higher wages, and the cycle becomes self perpetuating.[vii]

The original Phillips curve relationship began to be questioned, however, by the late 1960s, most prominently by two neoclassical economists, Milton Friedman and Edmund Phelps. Friedman and Phelps argued that inflation was caused only by the money supply, and could not affect employment in the long term.[viii] The explanation for this involved introducing an important factor into the relationship between inflation and employment: expectations. Friedman's argument was, that if inflation was continuous, the wage and price setters in the economy would become accustomed to it, and eventually wages would rise equally with inflation every year.[ix] There would be a return to the original level of output, and unemployment, referred to as the "natural" level. The "natural rate of employment" was determined by the labour market, competition, and other structural elements. It could not be affected by monetary factors.[x] In other words, the relationship described in the original Phillips curve would no longer work – inflation would not result in less unemployment in the long term, only higher prices.

This argument has serious policy implications – many Keynesian economists argue for looser monetary policy (low interest rates and the injection of more money into the economy) as an action against high unemployment or economic recessions. If Phelps and Friedman were correct, this would result in at best a temporary surge in output and employment, before returning to the same exact level. It was essentially an argument against using monetary policy to combat unemployment.

POLICY IMPLICATIONS OF RIGID WAGE AND EFFICIENT MARKET THEORIES

The belief that the market for labour will efficiently adjust to changes in price, levels of employment, or other economic fluctuations, has major policy implications. The explanation of unemployment related to this theory, that wages are too rigid, do not adjust quickly enough to these factors, also comes with its own set of policy recommendations. For those who believe these theories to be flawed, the policies implied may actually do more harm than good. For example, standard economic theory argues that having a minimum wage can create unemployment. The government intervention creates a "price floor" that does not allow wages to adjust as efficiently. Even if there is unemployment, wages are not allowed to get low enough for firms to have an incentive to hire more people.[xi] This is actually very similar to the rigid wage explanation of unemployment, but here the rigidity comes from government edict. Another commonly targeted creator of "market inefficiencies" in the labour market is workers' unions, for similar reasons. If unions raise the wages for unionized firms or sectors above the equilibrium (market determined) wage, the argument goes, that firm or sector will higher less workers as a result. Those who already have jobs will get higher pay, put others will be unemployed, or move to non-unionized sectors, where the increased supply of labour will lower wages.[xii] In this view, by interfering with the market's efficient allocation of labour and setting of wages, unions benefit a small group at the expense of others.

The focus on wage rigidity as the source of employment fluctuation is closely connected with the school of "Keynesian" economic thought sometimes referred to as the "neoclassical synthesis." Shortly after the publication of Keynes's major work, The General Theory of Employment, Interest, and Money, (in 1936), economist John Hicks created an "interpretation" of Keynesian theory known as the IS-LM model, a graphical representation of the goods and financial market. Paul Samuelson further developed and popularized an explanation of Keynes's theory based on IS-LM and an incorporation of classical economics. For theorists of this school, the problem of unemployment lies almost exclusively in wage rigidity. This belief has led to a similar set of recommendations as those who support efficient market labour theories. As Nobel Prize winning economist Joseph Stiglitz explained in 2009, "if rigid wages are the reason the economy is not working …what is the solution? Get rid of the rigid wages, and let labour markets be more 'flexible'." Stiglitz goes on to argue that this theory has been "the basis of a whole set of doctrines undermining job protections and labour rights."[xiii]

AN ALTERNATIVE APPROACH : AGGREGATE DEMAND, NOT SO-RIGID WAGES, AND DEFLATION

There are, however, many economists of the Keynesian tradition who argue that the neoclassical synthesis is a misapplication of Keynes's theories. For example, Hyman Minsky once wrote that as Keynes's theory "was transformed into quite simple doctrines to guide

public policy, much of what Keynes wrote was ignored."[xiv] Joan Robinson of Cambridge famously described the neoclassical synthesis as "bastard Keynesianism."[xv] The school of thought sometimes referred to as "Post-Keynesian" places aggregate demand, or effective demand, at the centre of economic theory, and often uses shifts in demand to explain employment fluctuations. Economists of alternate Keynesian traditions also argue that wages are actually not rigid, or at least not always, and especially not during times of economic fluctuations or extreme economic downturns. Further, there are also theoretical refutations to the "neutrality of money" theory, the idea that monetary policy cannot have long term effects on employment.

Joseph Stiglitz, for example, is a leading proponent of the view that wages may be too flexible during economic crises, and he uses evidence from recent (and some not so recent) events to support it. For example, he notes that wages fell by one third during the US Great Depression.[xvi] He has also used the example of the East Asian crisis in the 1990s, in which there were huge levels of unemployment, and huge declines in the price and wage level.[xvii] Stiglitz has further argued that employment may, in fact, react slowly to changes in the economy. For example, because of the costs of hiring and training new workers, firms may hesitate to lay off workers during the initial phases of downturns. They may instead want to try to "ride out" a brief period of low or negative profits so that they still have the workers they want when the recovery begins. This is known as "labour hoarding."[xviii] Conversely, if firms have laid people off during a crisis, when recovery begins, they may take other steps before hiring again, such as increasing the hours of workers they have retained.[xix] It is for reasons such as these that unemployment is sometimes referred to as a "lagging indicator" – its changes follow behind changes in the overall economy.

The larger claim by supporters of these alternate Keynesian theories, however, is that unemployment and low wages can be caused, especially at times of crisis, by insufficient aggregate demand. What this means is, when people's income falls, they will begin to buy less goods and services. This causes a spiral, much like a reverse of the previously mentioned wage-price inflation spiral, in which less goods and services are sold, causing prices to lower further, resulting in another increase in unemployment and decrease in wages. The argument from some economists is that in times of crisis, like the Great Depression, Japan in the 1990s, or perhaps today, wages can be too flexible, leading to this vicious cycle.[xx] Stiglitz has stated that the policy recommendations of those who focus on wage rigidity as the problem may have in fact exacerbated this problem by focusing too much on wage flexibility at the expense of other priorities.[xxi]

Some Post-Keynesian economists theorize that demand is central in determining unemployment and output level even in non-crisis moments. This theory seeks to refute the idea that a lowering of nominal wages will automatically reduce unemployment to its "natural" level. Involuntary unemployment, unemployment that cannot be solved simply by reducing wages, can exist in both the short and the long run.[xxii] Post-Keynesian economist Paul Davidson has argued that even if unemployment forces down nominal wages, employers would not have a motivation to hire more workers without an increase in effective demand providing a reason for them to increase output.[xxiii] In this view, keeping nominal wages low could actually increase unemployment. If wages do not rise with inflation, a rise in the price level leads to a decline in the real wage, which reduces demand and therefore reduces output.[xxiv] Therefore, any policy that aims directly and solely at keeping nominal wages low, and therefore lowering real wages, will not lower involuntary unemployment.[xxv] To supporters of this theory, it is a "truer" interpretation of Keynes's theory. Economist Lance Taylor argues that Keynes was "adamant" in his insistence that a reduc-

tion in nominal wages would not raise employment.[xxvi]

While the above theory is controversial, there is generally some acceptance among economists of all stripes that some policies addressing falls in aggregate demand are necessary. These are generally known as "automatic stabilizers." (The term "automatic" refers to the fact that they are already built into the system and don't need specific political action at the time of the crisis to take effect.) One example of an automatic stabilizer is taxes, especially if there is a progressive tax code. As income falls, consumers pay less in taxes, leaving them more money to spend, and hopefully mitigating their decrease in consumption. Another example of an automatic stabilizer is unemployment pay. When workers lose their jobs, they will receive unemployment payments, and so their consumption decreases by less than if they had no income. The theory is that this will result in a smaller decrease in aggregate demand than if the unemployed had no income at all, and so will help to lessen the cyclical effect of unemployment. One of the arguments put forth by Stiglitz and others who highlight aggregate demand is that the decades of following the policy recommendations related to market efficiency and rigid wages has resulted in a weakening of these automatic stabilizers, too much emphasis on flexibility and not enough on job security, all of which has combined to make the system less able to withstand crisis. [xxvii]

There are also theoretical counterarguments to the rejection by standard theory of the use of monetary policy for full employment. For example, Olivier Blanchard (currently chief economist at the IMF and author of one of the main texts used for this annex) has suggested that monetary policy can have an effect on long-term prospects of an economy, and that this is in fact what has happened in the last thirty years in economically developed countries.[xxviii] This theory can be partially explained by "hysteresis' – the idea that an increase in the actual rate of employment for a long enough time would lead to an increase in the natural rate. This change in the natural rate can be caused by changes in labour institutions, by workers giving up their job searches, or by workers losing skills through disuse and ceasing to acquire new skills. Because of this phenomenon, Blanchard has argued that monetary policy's effect on unemployment can eventually change the structural ("natural") unemployment rate, and the natural rate of output. [xxix] Long term high interest rates can also have a depressing effect on capital accumulation (for example, the building of new factories or investment in new infrastructure) and a negative effect on long run supply through this mechanism. The real interest rate is the cost of investment, the cost of capital. The size of the capital stock in turn affects the demand for labour, and the overall output. High interest rates over long periods can lead to lower output and higher unemployment in this manner. [xxx]

---

i Blanchard, Olivier. *Macroeconomics*. Upper Saddle River, NJ: Prentice Hall, 2006, pg. 126.
ii Blanchard, Olivier. *Macroeconomics*. Upper Saddle River, NJ: Prentice Hall, 2006, pg. 127.
iii Blanchard, Olivier. *Macroeconomics*. Upper Saddle River, NJ: Prentice Hall, 2006, pg. 274.
iv Mankiw, N. Gregory. *Principles of Macroeconomics*. Mason, OH: Thomson Higher Education, 2007, pg. 498.
v Mankiw, N. Gregory. *Principles of Macroeconomics*. Mason, OH: Thomson Higher Education, 2007, pg. 500.
vi Blanchard, Olivier. *Macroeconomics*. Upper Saddle River, NJ: Prentice Hall, 2006, pg. 168.
vii Blanchard, Olivier. *Macroeconomics*. Upper Saddle River, NJ: Prentice Hall, 2006, pg. 168.
viii Mankiw, N. Gregory. *Principles of Macroeconomics*. Mason, OH: Thomson Higher Edu-cation, 2007, pg. 501-2.
ix See, for example: Friedman, Milton. "Nobel Lecture: Inflation and Unemployment." *The Journal of Political Economy* Vol. 85, No. 3. (1977), pg. 456.
x Friedman, Milton. "Nobel Lecture: Inflation and Unemployment." *The Journal of Political Economy* Vol. 85, No. 3. (1977), pg. 458.
xi Mankiw, N. Gregory. *Principles of Macroeconomics*. Mason, OH: Thomson Higher Education, 2007, pg. 121.
xii Mankiw, N. Gregory. *Principles of Macroeconomics*. Mason, OH: Thomson Higher Education, 2007, pg. 325.
xiii Stiglitz, Joseph. "The global crisis, social protection, and jobs." *International Labour Review Vol*. 148, No. 1-2 (2009), pg. 9.
xiv Minsky, Hyman P. "The Legacy of Keynes." *The Journal of Economic Education* Vol. 16, No. 1 (1985) pg. 6.
xv Taylor, Lance. *Reconstructing Macroeconomics*. Cambridge, Massachusetts: Harvard University Press, 2004, pg. 132.
xvi Stiglitz, Joseph. "The global crisis, social protection, and jobs." *International Labour Review* Vol. 148, No. 1-2 (2009), pg. 10.
xvii Stiglitz, Joseph E. "Toward a General Theory of Wage and Price Rigidities and Economic Fluctuations." *The American Economic Review* Vol. 89, No. 2 (1999), pg. 75.
xviii Stiglitz, Joseph E. "Toward a General Theory of Wage and Price Rigidities and Economic Fluctuations." *The American Economic Review* Vol. 89, No. 2 (1999), pg. 76.
xix Stiglitz, Joseph E. "Toward a General Theory of Wage and Price Rigidities and Economic Fluctuations." *The American Economic Review* Vol. 89, No. 2 (1999), pg. 76.
xx Stiglitz, Joseph. "The global crisis, social protection, and jobs." *International Labour Review* Vol. 148, No. 1-2 (2009), pg. 10.
xxi Stiglitz, Joseph. "The global crisis, social protection, and jobs." *International Labour Review* Vol. 148, No. 1-2 (2009), pg. 10.
xxii Davidson, Paul. "Post Keynesian Employment Analysis and the Macroeconomics of OECD Unemployment." *The Economic Journal* Vol. 108, No. 448 (1998), pg. 825.
xxiii Davidson, Paul. "Post Keynesian Employment Analysis and the Macroeconomics of OECD Unemployment." *The Economic Journal* Vol. 108, No. 448 (1998), pg. 825.
xxiv Taylor, Lance. *Reconstructing Macroeconomics.* Cambridge, Massachusetts: Harvard University Press, 2004, pg. 131.
xxv Davidson, Paul. "Post Keynesian Employment Analysis and the Macroeconomics of OECD Unemployment." *The Economic Journal Vol*. 108, No. 448 (1998), pg. 826.
xxvi Taylor, Lance. *Reconstructing Macroeconomics*. Cambridge, Massachusetts: Harvard University Press, 2004, pg. 132.
xxvii Stiglitz, Joseph. "The global crisis, social protection, and jobs." *International Labour Review* Vol. 148, No. 1-2 (2009), pg. 11.

xxviii Blanchard, Olivier. Monetary Policy and Unemployment. Remarks at the Conference "Monetary policy and the labor market. A conference in honor of James Tobin." New School University, November 2002.
xxix Blanchard, Olivier. Monetary Policy and Unemployment. Remarks at the Conference "Monetary policy and the labor market. A conference in honor of James Tobin." New School University, November 2002.
xxx Blanchard, Olivier. Monetary Policy and Unemployment. Remarks at the Conference "Monetary policy and the labor market. A conference in honor of James Tobin." New School University, November 2002.

UNITED NATIONS NON-GOVERNMENTAL LIAISON SERVICE (NGLS)

The United Nations Non-Governmental Liaison Service (NGLS), established in 1975, is a jointly financed inter-agency programme of the UN system. NGLS promotes constructive relations between the United Nations and civil society, including through dynamic partnerships to foster greater coherence around cross-cutting and emerging issues on the UN's agenda and by facilitating meaningful civil society engagement in UN processes.

Drawing on its inter-agency nature and UN system-wide perspective, NGLS provides strategic information, analysis and support to a wide range of constituencies, using its unique convening and networking capacity to strengthen multi-stakeholder dialogue and alliance-building on core UN issues. NGLS programme activities deal with the full UN agenda on economic and social development, human rights, environment, peace and security and operate across the entire UN system of agencies, programmes, funds and departments concerned with these issues. NGLS works with national and regional NGOs from developing and industrialized countries and international NGOs.

The information produced by NGLS – both in published form and electronically – combines public information on UN and NGO events and issues, practical "how to" guides to the UN system for NGOs, and substantive analysis of issues on the international agenda. All NGLS publications are available on its website (www.un-ngls.org).

In 2009, the work of NGLS was supported by:
- United Nations Department for Economic and Social Affairs (UN/DESA)
- United Nations Conference on Trade and Development (UNCTAD)
- International Fund for Agricultural Development (IFAD)
- International Labour Office (ILO)
- Joint United Nations Programme on HIV/AIDS (UNAIDS)
- United Nations Children's Fund (UNICEF)
- United Nations Development Fund for Women (UNIFEM)
- United Nations Development Programme (UNDP)
- United Nations Educational, Scientific and Cultural Organization (UNESCO)
- United Nations Human Settlements Programme (UN-HABITAT)
- United Nations Industrial Development Organization (UNIDO)
- United Nations Population Fund (UNFPA)
- World Food Programme (WFP)
- World Health Organization (WHO)

NGLS also receives financial support for its activities from the Governments of Canada, France, the Netherlands, Norway, Sweden and Switzerland.

For further information:
NGLS Geneva
Palais des Nations
CH-1211 Geneva 10 Switzerland
Telephone: +41-22/917 2076
Fax: +41-22/917 0432
E-mail: ngls@unctad.org

NGLS New York
Room DC1-1106
United Nations, New York NY 10017, USA
Telephone: +1-212/963 3125
Fax: +1-212/963 8712
E-mail: ngls@un.org

"A fair globalization requires greater convergence of economic and social policies around the goal of decent and productive work for all. New policy thinking and strong advocacy are critical.

"This NGLS guide is extremely timely. It challenges much of the conventional thinking that guided policy making over the past three decades and which the crisis has shown to be profoundly flawed. Furthermore, it collects a broad set of proposals for alternative approaches to macroeconomic, financial, trade and employment and social protection policies that place the drive for decent work at their heart.

"As such it is a unique resource for civil society organizations, social movements and all those who campaign for economic and social justice."

Juan Somavia, Director-General of the International Labour Organization (ILO)

"In the last few years, there has been an increasing level of support for policy coherence to achieve a fair globalization, full and productive employment and decent work for all. To get global consensus on these core objectives has been a major achievement. But implementing the policy implications that derive from these commitments would require nothing short of a major overhaul in the way economic policies have been formulated in the last two or three decades. The global economic crisis provides an opportunity for a dramatic change of course, but in the face of pressures for a return to 'business as usual' we need to broaden political support around this alternative agenda.

"This NGLS guide to policy dialogue provides many thought-provoking suggestions for alternative economic strategies at national and international levels to realign macro-economic, financial and trade policies so as to meet the imperatives of full and decent employment. I strongly recommend that all interested in the decent work agenda find the time to read and consider its proposals."

Guy Ryder, General Secretary of the International Trade Union Confederation (ITUC)