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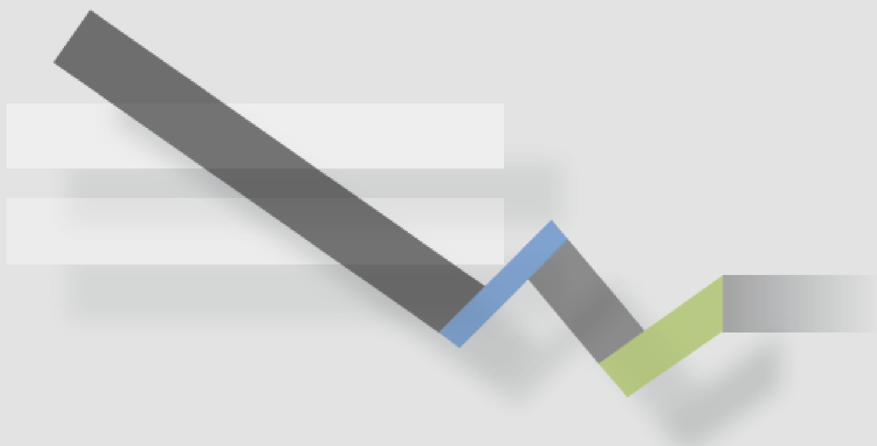
# World of Work Report 2011



## Making markets work for jobs

World of Work Report 2011

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## Who are the authors of World of Work Report 2011?

The report has been prepared by staff of the International Institute for Labour Studies and is published under the responsibility of its Director. Chapter authors are:

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# Editorial

**Raymond Torres**
*Director*
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### The economic slowdown may entail a double-dip in employment …

The next few months will be crucial for avoiding a dramatic downturn in employment and a further significant aggravation of social unrest. The world economy, which had started to recover from the global crisis, has entered a new phase of economic weakening. Economic growth in major advanced economies has come to a halt and some countries have re-entered recession, notably in Europe. Growth has also slowed down in large emerging and developing countries.

Based on past experience, it will take around six months for the ongoing economic weakening to impact labour markets. Indeed, in the immediate aftermath of the global crisis it was possible to delay or attenuate job losses to a certain extent, but this time the slowdown may have a much quicker and stronger impact on employment. After the collapse of Lehman Brothers in 2008, many viable enterprises expected a temporary slowdown in activity and so were inclined to retain workers. Now, three years into the crisis, the business environment has become more uncertain and the economic outlook continues to deteriorate. Job retention may therefore be less widespread.

Moreover, government job- and income-support programmes, which proved so successful in cushioning job losses and supporting job retention practices in firms at the start of the global crisis, may be scaled down as part of the fiscal austerity measures adopted in a growing number of countries. Lastly, and more fundamentally, while in 2008-2009 there was an attempt to coordinate policies, especially among G20 countries, there is evidence that countries are now acting in isolation. This is leading to more restrictive policies driven by competitiveness considerations, and job retention measures could fall victim to it.

The latest indicators suggest that the employment slowdown has already started to materialize (Chapter 1). This is the case in nearly two-thirds of advanced economies and half of the emerging and developing economies for which recent data are available. Meanwhile, young people continue to enter the labour market. As a result, approximately 80 million net new jobs will be needed over the next two years to restore pre-crisis employment rates (27 million in advanced economies and the remainder in emerging and developing countries). However, in light of the recent economic slowdown, the world economy is likely to create only about half of those much-needed jobs. And it is estimated that employment in advanced economies will not return to its pre-crisis levels until 2016, i.e. one year later than projected in the World of Work Report 2010.

### … exacerbating inequalities and social discontent …

As the recovery derails, social discontent is now becoming more widespread, according to a study carried out for the purposes of this Report (see special focus on social unrest in Chapter 1). In 40 per cent of the 119 countries for which estimates could be performed, the risk of social unrest has increased significantly since 2010. Similarly, 58 per cent of countries show an increase in the percentage of people who report a worsening of standards of living. And confidence in the ability of national governments to address the situation has weakened in half the countries.

The Report shows that the trends in social discontent are associated with both the employment developments and perceptions that the burden of the crisis is shared unevenly. Social discontent has increased in advanced economies, Middle-East and North Africa and, albeit to a much lesser extent, Asia. By contrast, it may have stabilized in Sub-Saharan Africa, and it has receded in Latin America.

### ... and further delaying economic recovery.

The worsening employment and social outlook, in turn, is affecting economic growth. In advanced economies, household consumption – a key engine of growth – is subdued as workers become more pessimistic about their employment and wage prospects. Indicators for the United States and several European countries suggest that workers expect stagnating or even falling wages. The uncertain demand outlook, combined with continued weaknesses in the financial system of advanced economies, is depressing investment in all countries, including in emerging and developing economies which rely primarily on exports for growth and job creation.

In short, there is a vicious cycle of a weaker economy affecting jobs and society, in turn depressing real investment and consumption, thus the economy and so on.

### This vicious circle can be broken by making markets work for jobs – not the other way around

Recent trends reflect the fact that not enough attention has been paid to jobs as a key driver of recovery. Countries have increasingly focused on appeasing financial markets. In particular, in advanced economies, the debate has often centred on fiscal austerity and how to help banks –without necessarily reforming the bank practices that led to the crisis, or providing a vision for how the real economy will recover. In some cases, this has been accompanied by measures that have been perceived as a threat to social protection and workers' rights. This will not boost growth and jobs.

Meanwhile, regulation of the financial system – the epicentre of the global crisis – remains inadequate. In advanced economies, the financial sector does not perform its normal intermediary role of providing credit to the real economy. And emerging economies have been affected by the massive inflows of volatile capital (Chapter 2).

In practice, this means that employment is regarded as second order vis-à-vis financial goals. Strikingly, while most countries now have fiscal consolidation plans, only one major advanced economy – the United States – has announced a national jobs plan. Elsewhere, employment policy is often examined with a fiscal lens.

It is urgent to shift gears. The window of opportunity for leveraging job creation and income generation is closing, as labour market exclusion is beginning to take hold and social discontent grows.

### This requires, first, ensuring a closer connection between wages and productivity, starting with surplus countries ...

It is time to reconsider "wage moderation" policies. Over the past two decades, the majority of countries have witnessed a decline in the share of income accruing to labour – meaning that real incomes of wage earners and self-employed workers have, on average, grown less than would have been justified by productivity gains. Nor has wage moderation translated into higher real investment: between 2000 and 2009 more than 83 per cent of countries experienced an increase in the share of profits in GDP, but those profits were used increasingly to pay dividends rather than invest (Chapter 2). And there is no clear evidence that wage moderation has boosted employment (Chapter 3).

In fact, wage moderation has contributed to exacerbating global imbalances which, along with financial system inefficiencies, have led to the crisis and its perpetuation. In advanced economies, stagnant wages created fertile ground for debt-led spending growth – which is clearly unsustainable. In some emerging and developing economies, wage moderation was an integral part of growth strategies based on exports to advanced economies – and this strategy too is unsustainable.

By ensuring a closer connection between wages and productivity, the global shortfall in demand would be addressed. In addition, such a balanced approach would make ease the pressures on budget-constrained governments to stimulate the economy. In many countries, profitability levels are such that allowing wages to grow in line with productivity would also support investment.

Obviously, the proposed policy would need to be adapted to country circumstances and can only be achieved through social dialogue, well-designed minimum wage instruments and collective bargaining, and renewed efforts to promote core labour standards. With this in mind, surplus economies like China, Germany, Japan and the Russian Federation have a strong competitive position, and therefore more space for such a policy than other countries. More balanced income developments in surplus countries would be in the interest of those countries while also supporting recovery in deficit countries, particularly those in the Euro-area which cannot rely on currency devaluation in order to recover lost competitiveness.

### ... second, supporting real investment notably through financial reform...

There will be no job recovery until credit to viable small firms is restored. In the EU, the net percentage of banks reporting a tightening of lending standards has remained positive throughout 2011, and when firms in the EU were asked about the most pressing problem they faced between September 2010 and February 2011, one-fifth of small firms reported lack of adequate access to finance. Targeted support could take the form credit guarantees, the deployment of mediators to review credit requests denied to small firms and providing liquidity directly to banks to finance operations of small enterprises. Such schemes already exist in countries like Brazil and Germany.

In developing countries, there is significant scope for increasing investment in rural and agricultural areas (Chapter 4). This requires targeted public investment, but also curbing financial speculation on food commodities in order to reduce the volatility of food prices. Food prices were twice as volatile during the period 2006-2010 than during the preceding five years. As a result, any increase in agricultural income is perceived by producers – especially small ones – as temporary. Producers thus lack the stable horizon needed to invest the agricultural-income gains, perpetuating food shortages and wasting decent work opportunities.

### ... third, maintaining and in some cases strengthening pro-employment programmes funded from a broader tax base ...

No country can develop with ever rising public debts and deficits. However, efforts to reduce public debt and deficits have disproportionately and counterproductively focused on labour market and social programmes. Indeed, cuts in these areas need to be carefully assessed in terms of both direct and indirect effects. For instance, cutting income support programmes may in the short-run lead to cost savings, but this can also lead to poverty and lower consumption with long-lasting effects on growth potential and individual well-being.

A pro-employment approach that centres on cost-effective measures will be instrumental in avoiding a further deterioration in employment. Carefully designed pro-employment programmes support demand while promoting a faster return to pre-crisis labour market conditions. Early support in crisis times pays off through reduced risk of labour market exclusion, as well as productivity gains. The positive employment effects due to more vibrant labour market matching compensates for any negative effects resulting from private sector crowding out. Increasing active labour market spending by only half a per cent of GDP would increase employment by between 0.2 per cent and 1.2 per cent in the medium-term, depending on the country (Chapter 6). Though these estimates provide broad orders of magnitude only, they underline that, if well-designed, spending on pro-employment programmes is consistent with fiscal objectives in the medium term.

Moreover, pro-employment programmes are not expensive to the public purse. If need be, new resources can be found to support much-needed spending. In this regard, the Report notes that there is scope for broadening tax bases, notably on property and certain financial transactions (Chapter 5). Such measures would enhance economic efficiency and help share the burden of adjustment more equitably, thereby also contributing to appease social tensions. The heterogeneous nature of the recovery makes it necessary, however, to apply the approach in the light of country-specific circumstances.

### ... and putting jobs back on top of the global agenda.

The responsibility for making markets work for jobs rests primarily with national governments. They have at their disposal a rich panoply of measures inspired by the ILO Global Jobs Pact – ranging from job-friendly social protection programmes, to well-designed minimum wages and employment regulations and productive social dialogue- which can be quickly mobilized in combination with job-friendly macroeconomic and financial settings. It is especially important to move quickly on this front in the Euro-area, where the signs of economic weakening are strongest.

There is also a critical role for international policy coordination. This task has become more difficult given the different cyclical positions of countries. However, the Report's findings suggest that a job recession in one region will, sooner or later, affect economic and social prospects in the other regions. Conversely, the interconnectedness of economies means that, if countries act in a coordinated way, any favourable effects on employment will be amplified. In this regard, the G20 has a special leadership role to play in keeping employment, along with fiscal and financial issues, high on the global policy agenda. Here too, time is of the essence.

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