

FACING THE CRISIS IN EUROPE: STRONGER LABOUR INSTITUTIONS IN LATIN AMERICA

I. THE 2008 CRISIS FOR LATIN AMERICA

The fall of Lehman Brothers in 2008 gave rise to a financial crisis at global level with an impact on international trade, causing an abrupt drop in the exchange of goods and services. The economies of Latin America were also affected as credit rationing occurred in the face of growing uncertainty and as demand for its main export products fell.

Since then, confidence in trade and the financial system was gradually restored and, on the basis of a sound fiscal situation and low debt levels, several countries of the region were able to adopt countercyclical measures to moderate the contraction of economic growth and attenuate the deterioration of people's wellbeing.¹ Furthermore, reactivation measures –mainly applied by China and other countries in Asia– prompted rapid reactivation of demand and prices for the main commodities exported by the region. The combination of countercyclical policies and the resumption of the region's external demand resulted in rapid recovery of growth with job creation since mid-2009.²

II. THE CRISIS IN EUROPE AND LATIN AMERICA IN 2012

Europe was only able to partially overcome the 2008-2010 financial crisis, and even those countries that resumed growth, did so at very low rates. As of early 2010, fragilities in the banking system in various countries, unsustainable levels of sovereign debt and deteriorating fiscal situations led to the European sovereign debt crisis.

In 2012, Europe and especially the Eurozone, still continues unable to find an avenue to resume the path of growth. According to recent estimates, the Eurozone will record -0.5% to -0.3% negative growth, after recording a -0.7% drop in the first semester of the current year, whereas the labour market continues to deteriorate, recording high levels of unemployment.³

The European crisis has had an impact on world economic performance, slowing growth, and estimates were successively revised down throughout 2012. USA will maintain its low but positive growth, the Chinese economy will slow and Japan will experience reduced growth. In this context, Latin American and Caribbean growth forecasts are lower than in past years, between 2.8% and 3.2% in 2012 and around 4% in 2013, as shown in Table 1.

1 ILO/World Bank (2012) *Inventory of policy responses to the financial and economic crisis, Joint synthesis report* (Washington D.C., World Bank)

2 This process was led by the countries of South America, whereas recovery lagged in Central America, Mexico and the Caribbean. See ILO (2009) "Políticas de empleo para enfrentar la crisis", in *Panorama Laboral 2009* (Lima, ILO) and Marinakis (2011) "Explaining Latin America's robust recovery from the crisis", in *The global crisis: Causes, responses and challenges. Essays from an ILO perspective* (Geneva, ILO)

3 See ILO-IILS (2012) *Eurozone job crisis: Trends and policy responses* (Geneva, ILO-IILS)

TABLE 1: 2012-2013 GDP trends and forecasts
(annual GDP percentage variations)

Institutions	2009	2010	2011	2012	2013
Latin America and the Caribbean^a	-1,6a	6,2a	4,5a		
International Monetary Fund (IMF)				3,7a 3,4b, 3,2c	4,1a 3,9c
Economic Commission for Latin America and the Caribbean (ECLAC)				3,7d 2,8e	4,1e

Source: ECLAC and IMF

- a) IMF (2012a) "World Economic Outlook: Growth Resuming, Dangers Remain. World Economic and Financial Surveys" (Washington D.C., IMF), April
- b) IMF (2012) World Economic Outlook Update (Washington D.C., IMF)
- c) IMF (2012) Regional Economic Outlook Update (Washington D.C., IMF)
- d) ECLAC (2012a) Informe macroeconómico de América Latina y el Caribe (Santiago, ECLAC)
- e) ECLAC (2012b) Estudio económico de América Latina y el Caribe. Las políticas ante las adversidades de la economía internacional (Santiago, ECLAC)

The described scenario foresees a moderate decline in the creation of jobs in the region, accompanied by lower quality of employment. This would drive a rise in the rates of open unemployment, which in many economies stand at historical lows.

III. DIFFERENCES BETWEEN THE CURRENT SITUATION AND 2008

Important differences exist between the current situation and the past crisis, which determine possible margins for action and the desirable direction of policies. The main differences are as follows:

The countries of the region resumed the path of growth after recording falls in 2009 and, in some cases in 2010, as in Venezuela (Bolivarian Republic of) and some Caribbean countries. Latin America and the Caribbean grew 6.2% in 2010, 4.5% in 2011, and for 2012 an increase of only 3.2% is foreseen. Hence, the period of growth has been relatively short and with growth rates lower than those registered in the period 2003-2008.

There are additional risk factors on top of those linked to the European crisis,⁴ such as the possibility of a significant drop in the demand for raw materials from China, that experienced a drop in its exports to Europe, difficulties in US Congress in reaching an agreement on fiscal policy, and a possible supply shock resulting in rising oil prices.

Inflationary pressures during 2012 followed a downward trend after the last quarter of 2011 in most countries of the region. Notwithstanding, this could turn around, since recent months have shown rises in international prices of grains (soybean, wheat and maize). Droughts in USA and floods in Brazil are pushing up world food prices (e.g. from 31 May to early August, the price of maize and soybean increased 47% and 26% respectively).

4 Countries that send a significant share of their exports to Europe, more than 13.1% on average, such as Argentina, Brazil, Chile, Costa Rica, Honduras, Peru, and Uruguay, would be most affected. Such effects would also depend on the type of export, since manufactured goods were especially affected during 2012, but not fuels, due to the rising price of oil and, above all, the intention by European countries to diversify their energy supply. See ECLAC (2012a) *op. cit.* and IDB (2012) *The World of Forking Paths: Latin America and the Caribbean Facing Global Economic Risks. Latin America and the Caribbean Macroeconomic Report* (IDB, Washington D.C.).

The abovementioned scenario imposes additional restrictions on having monetary policies that result in reductions to central bank benchmark interest rates.

To face the 2008 crisis, many countries of the region applied expansive fiscal policies that contributed to a faster economic recovery. However, as indicated earlier, the growth period since then has not been long enough to reconstruct sufficient margin for fiscal action. In early 2012 the IMF indicated that "fiscal accounts deteriorated by about 2% of GDP in almost 44% of developing nations. For this reason, developing countries have less fiscal space to respond before a new crisis".⁵ ECLAC reports little evidence of countries in Latin America strengthening their fiscal accounts in late 2011 and early 2012. In some countries, fiscal revenues grew during the first quarter 2012, but at a slower pace than in the past, and in others expenditure increased at a higher rate, especially in Argentina, Colombia, and Uruguay. Some countries passed tax reforms (Peru, Ecuador, El Salvador, Guatemala, and Chile) with a view to increase revenues, and other countries presented proposals (Costa Rica, Paraguay, and Colombia).⁶

Considering price forecasts for commodities (higher in the case of oil than food and metals), a significant rise is expected in the income of countries specializing in hydrocarbons, whereas for countries specializing in ores and agricultural products, revenues are expected to remain unchanged or slightly reduced. These trends, added to the heterogeneous performance of countries in terms of expenditure in the first months of the year, suggest a slight drop in annual fiscal results in comparison to 2011. Therefore, aside from the slowdown in the regional economy, a minor rise in the public debt to GDP ratio is expected in 2012.

Countries that in the face of falling exports in 2009 spurred increased domestic consumption, through policies favouring the use of credit by families, will probably see a limited ability to expand this approach in the current situation without risking increased indebtedness and, consequently, a rise in the default rate.

The 2008 crisis occurred simultaneously in all countries and, although it especially impacted export sectors, it also affected the rest of the economy and consequently employment. Although aggregate labour market indicators still do not record

5 IMF (2012a), *op. cit.*

6 ECLAC (2012a), *op. cit.*

the effects of the economic slowdown, certain sectors show tensions, such as different export sectors, manufacturing and real estate. This heterogeneous behaviour shows the need to closely monitor sectoral dynamics, in order to have a specific and timely diagnosis for future decision-making.

IV. REVIEW OF AVAILABLE POLICIES TO FACE AN UNFAVOURABLE SITUATION

The background information provided shows that the current situation differs from the situation preceding the 2008 crisis, mainly in terms of the smaller margins to implement policies to offset the effects of a less dynamic economic context. Although the scenario forecasted for 2012 speaks of a slowdown in the cycle of unemployment reduction in the region, this does not necessarily imply that the cycle would be reversed. Should such a scenario prevail, this could lead to tensions in specific sectors or in countries where internal imbalances could compromise growth.

In an atmosphere of uncertainty, it is useful to review the available array of labour market policy instruments, in order to prepare for timely responses in case of a worsening economic situation. During the 2008 financial crisis it became evident that most instruments are not for automatic deployment and require relatively long implementation times. However, the usefulness of this exercise is not limited to a potential crisis, since it also helps to identify and propose strategies to strengthen labour market institutions.

a) *Giving priority to public investment with more jobs*

During the international financial crisis, several countries increased expenditure in public investment to partially offset the drop in private investment. This measure continues to be relevant especially when projects with a high impact on employment are implemented in geographical areas experiencing increasing unemployment. In countries with a smaller fiscal margin it will be necessary to analyse the possibility of giving priority to projects in design stage with a greater employment component, over and above capital-intensive projects.

The ILO suggests assessing the employment impact of the portfolio of projects in planning and execution stages, with a view to postponing the more capital-intensive projects (or executing them more slowly) as well as having a geographical map of the most employment-intensive projects, with their implicit administrative execution times. This task should be carried out in collaboration with the Ministries of Public Works and Housing, together with a follow-up of activities and employment trends in the construction sector, with the greatest possible geographical disaggregation.⁷

b) *Credit and small enterprises*

In the face of uncertainty, and even more so in a context of crisis, the financial system tends to impose credit restrictions, thereby accentuating the economic cycle. Although the region is still growing, several countries are recording an incipient credit rationing and rising costs, which especially penalizes small enterprises.

⁷ See ILO (2010) "Obras públicas y generación de empleo", *Serie OIT Notas sobre la Crisis* (Lima, ILO)

In this situation it is important for State banks and private sector development agencies to play an active role in backing loans for this segment of enterprises. Recent experience shows the importance of implementing this type of measures, placing resources at the service of the banking system for this purpose. The ultimate objective is to enable smaller-sized enterprises to maintain liquidity, and not to aggravate the operating risks of enterprises that are otherwise healthy but facing a more restrictive economic context.

c) *Protecting employment and collective bargaining*

In times of economic slowdown and uncertainty, enterprises facing specific difficulties may resort to laying-off part of their labour force, even at the expense of losing highly-skilled staff. During the last crisis, several countries implemented programmes to facilitate the retention of workers at enterprises undergoing difficulties. Within the context of collective bargaining, work-sharing arrangements were made whereby the enterprise, the worker, and the State, through a partial subsidy, compensated workers' reduced income with the possibility of providing training at the workplace.⁸

These programmes proved useful in ensuring that enterprises undergoing difficulties did not lose their trained workers and could quickly recover their production capacity upon increased demand. Nevertheless, for its implementation to be effective, this instrument should be available when the first symptoms of a worsening labour market occur, since its aim is to anticipate possible lay-offs, and all stakeholders should know from beforehand how it operates, in order to facilitate bargaining between workers and employers for implementation in each case.

d) *Protecting against unemployment*

Some countries of the region have an unemployment insurance scheme, which acts as an automatic stabilizer in the case of fluctuations in economic activity and employment. It is of utmost importance to move ahead and adopt measures to extend the coverage of these schemes and ensure that persons who fulfil the eligibility criteria actually have quick access to its benefits. In countries that still do not have an unemployment insurance scheme, it would be opportune to evaluate the possibility of creating one.

Recent experience shows that some unemployment insurance schemes extended the duration of benefits to respond more effectively to increases in the duration of unemployment. It is recommendable to monitor the evolution of this indicator and assess the cost of this potential measure.

Unlike in developed countries, the unemployment insurance schemes in the region provide benefits only during a short period of time. Hence it is advisable to set a criteria that triggers an automatic extension of the benefit duration in certain defined circumstances, since ad hoc extensions run a greater risk of arriving late.⁹

⁸ For further details, see Messenger (2009) "Work sharing: A strategy to preserve jobs during the global job crisis", *Travail Policy Brief*, N° 1 (Geneva, ILO)

⁹ See discussions about this topic in OECD (2011) *Should benefit duration vary over the business cycle?* (OECD), pp. 68-71

e) Minimum wage policy

During the economic crisis, most countries in the region decided to apply moderate readjustments to their minimum wage, thereby protecting the purchasing power of lowest wages. Given that, in practice, the inflation rate fell in comparison to the previous year during the period in which these minimum wages were effective, real adjustments turned out to be positive, constituting a dynamizing factor for domestic markets.¹⁰

This is a policy option that can be used to the extent that inflationary pressures are low and in instances where it is deemed necessary to activate a moderately dynamizing factor of economic activity.

f) Training and labour intermediation policies

In a context as the one foreseen, professional training activities may acquire greater emphasis in order to improve the competencies of less qualified job seekers. This is particularly important for young people who, as their inclusion in the labour market is likely to be postponed, should have the opportunity to remain longer in the formal education system, preparing themselves better for a period with more job opportunities. So, rather than encouraging early and precarious inclusion in the labour market, countries could take this situation as an opportunity to increase schooling rates, especially in the technical training system.

Labour intermediation services should give priority to identifying businesses' labour requirements once the present period of reduced growth is overcome, forwarding this information to professional training institutions. Measures should also be introduced to strengthen their operation in the face of rising numbers of unemployed persons and the possible start-up of direct employment programmes. Finally, and in response to a more structural need, the connection between labour intermediation services and unemployment insurance should be strengthened in countries where such a scheme is operational.

g) Conditional transfers

During the 2008 crisis, transfer programmes implemented in a great number of countries in the region constituted an important cornerstone of public policies to provide a minimum income for their most vulnerable populations. Although these programmes primarily aim to correct structural problems, by promoting

education and avoiding school attrition, their increased coverage converted them into countercyclical instruments.

Of the 19 countries that implement transfer programmes in the region, 17 saw an increase in the number of beneficiaries and in the budget between 2011/2010 and 2008/2007.¹¹ Likewise, and partly reflecting these increases, expenditure in social security and aid increased in relation to GDP between 2010 and 2006/2007 in all 19 countries.¹²

Given that in the majority of cases these programmes already achieved the expected coverage, in case of a crisis it would not be advisable to further extend coverage. However, to the extent there is sufficient fiscal space, benefits could be adjusted to offset losses in purchasing power, which would have an equivalent impact on consumption.

h) Emergency employment programmes

Since the unemployment insurance schemes operational in the region are only able to cover part of the regions' workforce, it is necessary to implement emergency employment programmes in case of a significant rise in unemployment rates. Although the current labour market situation in the countries of the region does not pose an immediate need to prepare for these programmes, it is advisable to review the basic terms (benefit amounts, duration, selection of beneficiaries, and so on) to ensure their fast and timely implementation. In countries where these programmes operate at a lower scale, it is recommended to assess the terms and requirements for a possible extension, and on this basis estimate the cost for various scenarios.

i) Ensure monitoring of basic rights at work and encouraging social dialogue

It has been shown that social dialogue is a valuable tool for creating consensus and adopting measures, both at enterprise level as well as sectoral or national level. Dialogue has the potential to develop mechanisms to equitably share the costs as well as the benefits of growth and its fluctuations.

The ILO recommends a close monitoring of the compliance of labour standards, as well as the strengthening of social dialogue at national level, since its institutionalization can pave the way for national agreements, which serve as a framework for developing dialogue at sectoral or enterprise level.

10 See Marinakis, A. and Velásquez, M. (2010) Salarios en la crisis y en la recuperación, *Serie OIT Notas sobre la Crisis* (Lima, ILO)

11 Based on ECLAC, *Panorama Social 2011*, table 41 data (Santiago, ECLAC)

12 Analysis based on data from the *Conditional Transfer Programmes managed by ECLAC* at <http://dds.cepal.org/bdptc/>, July 2012