ILO NOTES

International Labour Organization

FACING THE CRISIS IN EUROPE: REFLECTIONS ON THE CASE OF CHILE

I. CRISIS IN EUROPE AND ITS EFFECT ON CHILE

As a result of the European debt crisis, economic activity at a global level slowed throughout 2012. During the year, growth estimates for the different regions were successively revised down. This has also been the trend in Latin America, as shown in table 1.

Growth estimates for Chile have tended to converge around 5.0% for 2012 and 4.8% for 2013. The slowdown of the world economy has been affecting Chilean exports, while the dynamism of domestic demand sustained growth during 2012. Risk factors for 2013, apart from the European crisis, include US Congress difficulties in reaching an agreement on fiscal policy; a significant drop in the demand for raw materials by China, which could push down the price of copper; and a possible supply shock resulting in rising oil prices.[1]

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
Chile					
- Central Bank of Chile (IPOM, September)	-1.0	6.1	6.0	4.75 - 5.25	4.0 - 5.0
- Ministry of Finance (October)				5.0	4.8
- International Monetary Fund (IMF)				4.3a 5.0c	4.5a 4.4c
- Economic Commission for Latin America and the Caribbean (ECLAC)				4.9d 5.0e	4.8e

Source: Central Bank of Chile, ECLAC, IMF, and Ministry of Finance of Chile

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

As to the labour market, following a rise in the unemployment rate in 2009, this rate maintained a steady downward trend since 2010 and stabilized in 2012 around 6.4%. Although there are no signs of the open unemployment rate being impacted by the world economic slowdown, a decline in the creation of new jobs is starting to become visible.

1 Corbo, V. (2012) *El momento económico internacional y nacional* (Santiago, Centro de Estudios Públicos)

II. DIFFERENCES BETWEEN THE CURRENT SITUATION AND 2008 IN CHILE

After a -1% fall in GDP in 2009, the Chilean economy resumed growth in 2010 and 2011 with an average annual rate of 6%, and rates of approximately 5% are estimated for the present and coming year. Contrary to the past crisis, the prior recovery period showed substantive growth rates, but was short-lived.

Similar to what was observed during the 2008 crisis, inflationary expectations in Chile evolved downward during the year 2012 and are likely to settle around an annual 2.5%. This drop in inflationary pressure, however, does not imply a drop in the Central Bank Monetary Policy Rate in the short run. Notwithstanding the above, space exists for a less restrictive monetary policy in case of an eventual decline in economic growth.

In this scenario, it is also necessary to consider rises in the international price of grains (soybean, wheat, and maize) recorded in recent months. Drought in the USA and floods in Brazil are pushing up world food prices, which could reverse downward inflation trends.

To face the 2008 crisis, Chile deployed a set of countercyclical measures and programmes, in the order of 4 billion dollars, which diminished the impact of the crisis and contributed to fast economic recovery. As indicated above, since then, the period of recovery and growth has been brief, and today there are smaller margins for fiscal action.

The government budget for 2013 foresees a real 5% rise in expenditure, concluding reconstruction work after the damage caused by the 2010 earthquake and increasing its spending on education, which is to be financed through a recently passed tax reform. Upward trends in food prices and downward trends in the price of ores could have net adverse effects greater than foreseen on external accounts, thereby becoming a greater restriction for public policy activation.

The Central Bank of Chile reported [2] that until the middle of the present year, financial market conditions have been a factor bolstering consumer spending. This notwithstanding, in the case of consumer credit, supply restrictions have been observed, as well as a slight decline in nominal placements and a minor reduction in demand. Credit to the private sector, meanwhile, has shown sustained growth, with annual rates of 17.7% last June, similar to the rates observed in 2005-2006 and with cost reductions.

It is highly probably that in what remains of this year and the next, the increase in global credit and its components will adjust to a situation characterized by a scenario of less economic growth, as foreseen.

Although the 2008 crisis especially affected exporting sectors, it also had an impact on other sectors of the economy, with a consequent impact on employment. At present, although aggregate labour market indicators still do not record the effects of the economic slowdown, some specific sectors of activity are showing certain signs of tension. This is becoming visible in exporting sectors in a context of exchange appreciation, as well as in manufacturing, although construction continues to be dynamic. Heterogeneity in sectoral behaviour makes it necessary to closely monitor the situation in order to have a comprehensive and timely diagnosis for future decision-making.

III. POSSIBLE AREAS OF INTERVENTION

In an atmosphere of uncertainty, as indicated, it is useful to review available labour market policy instruments in the country, and assess their ability to respond on a timely basis in the case of a worsening economic situation. As shown during the 2008 financial crisis, most instruments are not for automatic implementation and, on the contrary, require relatively long implementation times. Review of available policies, and preparation of specific adjustments to make them more effective, is especially important in a context of relatively greater fiscal tightening.

a) Including the employment variable in the assessment of public works

During the international financial crisis, several countries increased their expenditure in public investment to partially offset the fall in private investment. In this respect it is advisable to systematically include the impact on employment of the portfolio of projects in execution and planning phases. This would, in case of a significant deterioration of activity, allow informed decisions as to whether the most capital-intensive projects could be postponed (or executed more slowly), on the basis of an evaluation of the costs of such a decision and a geographical mapping of new more job-intensive projects. Likewise, and considering the importance of acting in a timely manner, the necessary mechanisms should be established to minimize administrative times for the start-up of new projects.[3]

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.[4] Although the Chilean economy is growing and the prevailing macroeconomic situation is healthy, there are signs of incipient retraction of credit and higher costs. This situation especially penalizes small enterprises.

In this regard it is important to take into account the experience of the past crisis, when a set of measures was implemented to guarantee the rescheduling of loans to small enterprises, to increase the number of beneficiaries of entrepreneurship programmes and to improve the eligibility criteria of credit guarantee instruments for small-scale enterprises. At this time it is especially important to assess the effectiveness of these measures in order to identify which were the most suitable instruments that could be replicated –and improved- in case of a worsening economic scenario. The main idea here is to ensure that private sector development institutions play an active role in backing loans for this market segment. The ultimate objective is to enable smaller-sized enterprises to maintain liquidity, and not

2 Banco Central de Chile (2012) *Informe de política monetaria* (Santiago, Banco Central de Chile)

3 For a concrete case of implementation of this methodology, see ILO (2010) ILO Series *Obras públicas y generación de empleo* (Lima, ILO) providing details on what was done in Chile to face the financial crisis

4 See *Restricción de crédito bancario para consumo alcanza mayor nivel desde 2009* in La Tercera, 12 July 2012, p. 25, with reference to a quarterly survey by the Central Bank; and *Bancos toman mayores resguardos y disparan posición de liquidez en septiembre* in Diario Financiero, 9 October 2012, p. 4.

to aggravate the operating risks of enterprises that are otherwise healthy but facing a more restrictive economic context.

c) Work-sharing

During the last crisis, several countries implemented programmes to facilitate the retention of workers at enterprises undergoing difficulties, using work-sharing systems whereby the enterprise, the worker, and the State, through a subsidy, compensate part of the workers' reduced income.[5] In a context of economic slowdown and uncertainty, situations should be avoided in which enterprises facing specific difficulties would have to lay-off part of their labour force, thereby losing highly skilled staff.

In Chile a variation of a work-sharing programmes was applied temporarily, which involved a training component financed through an existing tax exemption scheme as well as a monetary component financed by employers and unemployment insurance. More recently, this type of response was one of the topics proposed by the main workers and employers organisations in the country, while the government made its own proposal.

International experience shows that the implementation of work-sharing schemes is more effective when certain design conditions are taken into account:

- It is preferable for programmes to be of permanent character, so that enterprises are familiar with their operational procedures and in order for the necessary administrative structures to be in place for appropriate and expeditious implementation.
- These systems should permit different types of reductions in working hours in accordance with the needs of the individual enterprise, though limits may be imposed on the maximum reduction rate, with subsidies adjusted accordingly.
- It is necessary to determine certain requirements for enterprises applying to the scheme, as well as a monitoring process in order to check that enterprises are in fact undergoing a temporary situation that justifies a partial reduction of their labour costs
- The parties should make specific and equitable contributions to overcome the difficult period. To promote a strengthening of industrial relations in Chile, incentives could be adopted in case applications by specific enterprises are supported by one or more labour unions
- While the programme is in effect, workers could take part in training programmes, without this being a necessary requirement for approval.

d) Improving protection against unemployment

Chile has an unemployment insurance scheme, which acts as an automatic stabilizer in the case of fluctuations in economic activity and employment, by sustaining consumer spending amongst the unemployed. Its efficacy, however, depends on the effective coverage, the size of the benefits, and the capacity to finance such benefits.

The Chilean unemployment benefit scheme underwent a substantial reform in 2009[6] and during the crisis access to its benefits was improved, coverage was extended and its countercyclical role was strengthened through additional benefits aside from those already established. Two additional payments were added in case the unemployment rate would exceed the trend of the previous four years, workers with fixed term contracts were included for benefits provided by the Solidarity Unemployment Fund (FCS - *Fondo de Cesantía Solidario*), and beneficiaries of the work-sharing mechanisms were included.

The following is proposed to strengthen the automatic stabilizer role of unemployment insurance and enhance the capacity of the economy to face recessive shocks:

- Reviewing of mechanism for activating and deactivating benefits and their duration, replacing past information as the benchmark with unemployment forecasts, to ensure a more opportune provision of benefits. The benefit application records of the system itself are a useful tool to construct early-warning indicators.
- Preparing the system to operate within the context of work-sharing programmes, putting in place the necessary procedures to generate benefits, calculate amounts and durations in accordance with the adjusted working hours.
- Assess the appropriateness of the benefits awarded and the limits of what should be charged to the FCS–since these are benefits with relatively low replacement rates, according to international experience, in order to improve the use of the system and support individuals' efforts to actively look for a new job.

e) Work training in tune with productive sector demand

Available data suggests that the skills training system in Chile requires improvements in order to provide appropriate coverage and relevant content in line with the competencies and knowledge required by the private sector. Three possible avenues to progress in this respect are:

- Ensuring the right connection with private sector needs

  International experience shows the usefulness of developing mechanisms to identify skills training needs and to design training responses and certification mechanism in line with training demands. These mechanisms could take the shape of tripartite councils in which the representatives of employers and workers address issues associated to the development of human resources in a specific sector, define occupational profiles, analyse training needs, and define programmes, among others. For example, in the case of Colombia these instances are called Mesas Sectoriales, in Argentina they are Consejos Sectoriales de Certificación de Competencias y Formación Profesional, in Brazil the SENAI has Comités Técnicos Sectoriales, and in Australia the Skills Councils play similar roles.

  It is also important to pay attention to training providers. A working approach on teacher training and the creation of incentives for scaling-up training supply in line with demand, would supplement the role of social actors, and would ensure a better return on investment in training.

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

6 See Velásquez, M. (2009) "Chile. El seguro de cesantía: Más protección en un contexto de crisis", *Serie OIT Notas sobre la Crisis* (Lima, ILO)

- Correcting deficits in the use and coverage of training

  With the support of social actors, it is necessary to establish training programmes that maximise the use of tax exemption schemes and other training modalities with public funds. This implies that access should not only be provided to employed workers, but also to the unemployed, redesigning access mechanisms and training options. It is necessary to review connections with the unemployment insurance scheme, as well as with the labour intermediation system, in order to increase the scope for unemployed workers not covered by unemployment insurance.

- Progress toward an integrated system of active and passive policies

  The national employment and training system (SENCE) provides the necessary conditions to develop a life-long training mechanism within the framework the National System for the Certification of Competencies (Chile Valora), through an evaluation and certification process that would enable workers to participate in a virtuous circle of updating and complementing their skills and competencies.

  In this area, the role of public employment services is also of key importance in the detection of training needs, especially in a context of low open unemployment, which may have a high structural component that merits this type of intervention all the more. This notwithstanding, measures should not be excluded to strengthen the operation of these services in the face of rising numbers of unemployed workers and the possible implementation of direct employment programmes.

  Finally, coordination between employment services and unemployment insurance should be strengthened to support job-seeking by the insured. The effective integration of these components is a weakness that could be overcome by using the e-employment pool (Bolsa Electrónica de Empleo), and by strengthening the in-the-field structure of Municipal Labour Intermediation Offices to broaden the reach of these services in more remote locations and cover more vulnerable potential beneficiaries.