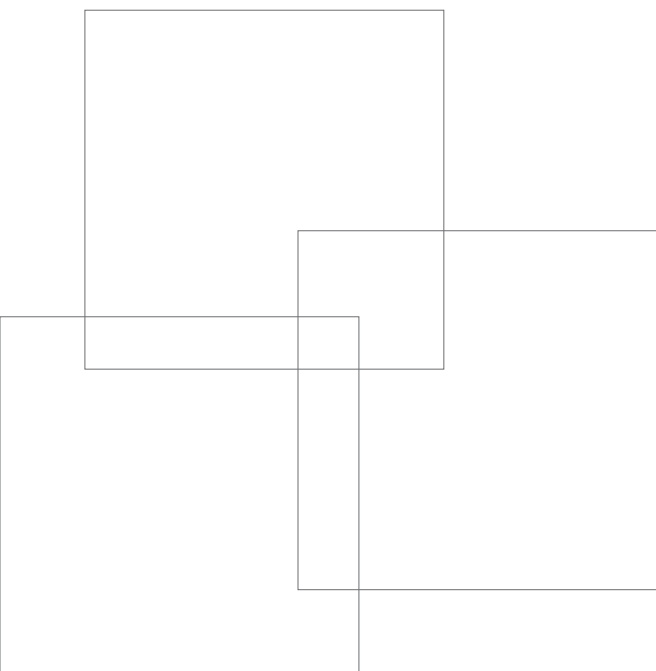




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Geneva



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National employment policies: A guide for workers' organisations

Labour institutions, social
protection and employment

Labour institutions, social protection and employment



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Quick overview

Labour institutions are the rules, practices and policies that guide the labour market. Their purpose is to improve social justice for workers by protecting freedom of association and collective bargaining. They also mandate standards for working conditions, many of which are internationally agreed upon.

When it comes to job creation, the most important levers are a country's macroeconomic conditions and industrial structure. Labour institutions matter most when it comes to employment quality.

The view that countries, particularly developing countries, cannot afford laws and policies to protect workers has unfortunately dominated policy debates. It is based on the supply and demand framework of conventional labour market theory. This theoretical model does not take into account unequal power in bargaining or a country's social norms, which may artificially keep down the quality of jobs.

We focus here on two important labour institutions - employment protection legislation and minimum wages. We look at the theoretical arguments for and against them and at what the research says. We also look at the linkages between employment and social security systems, such as pension plans and unemployment benefits.

Employment protection legislation

Research evidence confirms that employment protection legislation, such as hiring and firing rules, leads to more stable employment by reducing turnover. Dismissal rates are higher among workers not covered by employment protection legislation. The evidence that employment protection legislation decreases overall employment levels is quite weak and inconclusive.

Minimum wages

Research on the minimum wage suggests that this labour institution can create winners as well as potential losers among workers. Minimum wage effects depend on the degree of enforcement and compliance with the legislation, the share of workers covered by minimum wage legislation, the degree of competition in the labour market and minimum wage structures.

The crucial factor is the way minimum wages are set. To ensure that they increase the standard of living for workers and their families, at least five conditions have to be met (ILO, 2008):

- Keep the design of minimum wage systems relatively simple and easy to understand. Overly complex systems tend to be the least effective.

- Take into account both the needs of workers and economic factors.
- Extend legal coverage to a majority of workers, including those who are most vulnerable to exploitation.
- Set up a well-functioning mechanism to enforce compliance.
- Consult fully with representative organisations of employers and workers. Involving the informal economy is also important, especially in developing countries.

Social protection

Social protection is a country's system of benefits for people and families when they are poor, sick, disabled, out of work, elderly or young and dependent on others. The benefits may be provided through the state's social security system, through private insurance, through personal savings, through various social customs and relief organizations, or through some combination of these sources.

Our key message is that employment policies and social protection policies are closely linked. They must be connected in policy design in order to frame solutions grounded in long-term, sustainable, employment-centred growth.

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7.1. What are labour institutions?

Labour institutions “comprise rules, practices and policies – whether formal or informal, written or unwritten – all of which affect how the labour market works. They are as explicit and long-standing as certain labour laws that we have come to consider as universal rights, but also span the scope of informal practices that reflect the views of society, as well as short-term policies that fade and resurge depending on the policy mood” (Berg and Kucera, 2008, p. 11).



Here is a list of the dominant labour institutions that condition our working lives, both within and outside of the labour market (Berg & Kucera 2008, abridgement of Rodgers, 1994).

- Employment contracts
- The mechanisms for controlling and regulating employment contracts
- The organization and representation of labour: trade unions, or trade or craft associations
- The organization and representation of employers: employers' organisations and business associations
- The dominant procedures for job search and rules for access to jobs of different types
- The methods by which wages are paid
- The process of wage fixing or setting
- Training and skill institutions
- The organization of jobs within the firm
- The structure of ownership and control over production
- The social and state regulation of self-employment
- Social security and income guarantee systems
- The conventional standard of life–aspirations about consumption, leisure, savings and work
- The organization of labour supply, both within and outside the household.

All countries, regardless of their level of economic development, have labour institutions. Countries differ in the degree to which formal laws regulate the labour market, and whether these laws are applied in practice.

Many labour laws arise as a response to undesirable practices in what were once informally regulated labour markets. For example, discrimination, based on gender, race or social origin, is commonly found in labour markets throughout the world. Countries

that have decided to fight discrimination have enacted laws and policies to counter it and to change social norms.

The laws and policies that a nation pursues both influence, and are influenced by, the conventions and recommendations adopted by the International Labour Conference and the technical cooperation and advocacy work done by the International Labour Office.

7.2. Do labour institutions help or hinder the market?

When unemployment insurance was first adopted in Europe in the early part of the 20th century, it was seen as a response to the destitution brought about by job loss. Legal statutes on maximum hours, minimum wages, and health and safety regulations were adopted with the purpose of improving working conditions and the standard of living of workers. And laws protecting freedom of association and **collective bargaining** were adopted to remedy the bargaining power advantage employers have over workers. The emergence of labour law and the institutions it created were seen as one of the great triumphs of modern times.

Today, these same institutions – now widely adopted in many parts of the developing world – are considered by many to be a cause of unemployment and informality. The belief is that regulating things like hiring, firing and working hours has hampered investment, causing the poor to suffer more than they already do.

The standard model of labour supply and demand

This change in thinking is mainly explained by the pre-eminence of one economic theory: the standard economic model of labour supply and demand. This model argues that as wages rise, labour costs go up, and thus a firm hires fewer workers. This theory leads to the conclusion that policy makers would be wise to remove labour institutions because they are 'artificial' impediments to a competitive labour market.

At the level of an individual firm, the standard model seems logical. The influence of the model can be seen in Southern Europe, where governments have been forced to lower wages in an attempt to improve competitiveness and lower unemployment. However, this **policy** strategy has not worked. In most countries, there are fewer jobs than there are workers available, regardless of whether or not the labour market is highly regulated. With a stagnant economy and falling demand for goods and services, businesses do not hire additional workers, no matter how cheap labour has become. What seems logical at the individual level falls apart at the broader social level.

There are other inconsistencies between the standard model and the world we live in. Some firms and industries pay more than others, even if the jobs done at those firms are the same. And it is doubtful that the huge salaries of corporate executives are the outcome of limited supply and high demand.

Despite its weaknesses, the standard economic model of labour supply and demand continues to dictate economic policy making. It poses a challenge for trade unions and governments who are interested in redirecting **macroeconomic policy** towards employment promotion.

Are there other economic theories that better explain what we see around us?

Alan Manning, an economics professor at the London School of Economics, argues that employers have wide scope to set wages and thus the labour market is not purely competitive (Manning, 2003). According to Manning, there are frictions in the labour market that give employers market power, allowing them to set wages. To begin with, workers often have little information about alternative employment opportunities. Workers are also understandably hesitant to leave a job to search for a better one. If they are unemployed, they may not have the financial ability to hold out for a better opportunity. Mobility is another factor – it is not always possible for workers to move for a better job. Job search is also affected by family care responsibilities. These can limit the number of hours that workers can dedicate to paid work as well as how far they can go to search for new jobs.

Manning's model captures some aspects of the labour market, but probably not all. Sydney and Beatrice Webb, writing over a century ago in the classic book *Industrial Democracy*, based their analysis on the competitive model, but argued that the outcomes are inefficient both for workers and society (Webb and Webb, 1902). This inefficiency called for regulation.

They explained how workers' desperation resulted in wages too low to cover the social costs of labour. The Webbs argued that wages must be sufficient to maintain the worker and the workers' family, and that wages that are below this subsistence level entailed a social cost. Society bore these costs through social programmes to support the poor. In the absence of public assistance, impoverishment took a negative toll upon society in the form of crime, disease, and social unrest.

The Webbs argued for minimum wage policies that would avoid the spread of what they termed "parasitic industries". They acknowledged that, although some businesses would not be able to survive if forced to pay higher wages, the new wage floor would ultimately benefit society by "stopping the degradation" and "contributing to industrial efficiency" (op. cit., p. 767).

How do we know if labour institutions are accomplishing their goals?

It is difficult for economists to measure the performance of labour institutions, because there are so many variables involved. For instance, many labour institutions and policy interventions could combine to increase women's participation in the labour market. We may need more jobs that allow part-time work with pro-rated wages comparable to full-time work. We may also need policies to provide childcare and early childhood education. School hours affect a family's ability to participate in the labour market, so education policies may need to be harmonized with labour market policies. Tax policy should be designed to not unduly punish part-time workers. There may also be a need for effectively enforced anti-discrimination laws. Measuring the combined effects of all of these interventions is difficult.



Two important labour institutions – **employment protection legislation** and minimum wages – illustrate this point well. We discuss them next: the theory behind them, and the arguments for and against them.

7.3. Employment protection legislation



Employment protection legislation is a labour institution aimed at increasing job security. Almost every country has at least basic employment protection legislation in place. Well-known examples are hiring and firing rules or restrictions on the use of temporary workers.

For example, most countries worldwide oblige employers to compensate dismissed or fired workers with severance pay. The amount usually depends on the number of years worked for the company and the salary. Another example is the rule that firms have to give advance notice in case of dismissal. Another is the requirement to discuss decisions on dismissals for economic reasons with workers' representatives (Muller, 2011).

There are some exemptions from these rules. In some countries, dismissal legislation is not binding for small enterprises. In Germany, for instance, firms with fewer than ten employees do not fall under its Protection Against Dismissal Act.

Key messages of the International Labour Organization's guidance on firing rules

The ILO has set out guidance on firing employees in its Termination of Employment Convention, (No. 158) (ILO, 1982).

To whom do these rules apply?

- To all branches of economic activity and to all workers with some exceptions, such as those on temporary contracts or those serving a period of probation.

What are the rules?

- The employment of a worker shall not be terminated unless there is a valid reason connected with the capacity or conduct of the worker or based on the operational requirements of the enterprise.
- A worker whose employment is to be terminated shall be entitled to a reasonable period of notice or compensation in lieu thereof, unless he or she is guilty of serious misconduct.
- When the employer contemplates terminations for economic, technological, structural or similar reasons affecting a specified number of the workforce, the employer shall notify the workers' representatives and the appropriate authority (such as the ministry of labour) as early as possible.
- A worker whose employment has been terminated shall be entitled, in accordance with national law and practice, to a severance allowance and/or benefits from unemployment insurance or other forms of social security.
- A worker who considers that his or her employment has been unjustifiably terminated shall be entitled to appeal against that termination to an impartial body (such as a court). If the impartial body comes to the conclusion that the termination is unjustified, it can declare the termination invalid and order reinstatement and/or payment of adequate compensation.

The effects of employment protection legislation: What theory tells us

Employment protection legislation influences employer's and employee's decisions in various ways that affect labour costs, employment and productivity. (Cazes, 2013).

Arguments in favour of employment protection legislation

Some theorists argue that employment protection legislation increases **labour productivity**. Overall, it leads to a more stable and secure employment relationship, improving economic performance. Since rules like severance pay schemes make dismissals more costly, employment protection legislation gives an incentive to employers to invest more in their workforce by offering retraining and skills upgrading. For employees, job security will encourage work commitment and willingness to adapt to technological changes. In this view, employment protection legislation prevents 'low road' or 'race to the bottom' competitive strategies between enterprises. It forces them to compete on the basis of quality and innovation rather than low labour costs.

Employment protection legislation also increases protection for vulnerable groups. Regulations concerning pregnancy and maternity leave and seniority rules for older workers are examples of this protection.

Employment protection legislation can act as a stabilizer in case of economic downturns. Since employment protection legislation increases the costs for firms to dismiss workers, they might be more likely to keep them employed, even during times of recession. It ensures that clear rules and administrative procedures increase security for workers in the case of dismissals for economic or operational reasons. For example, in some countries firms are obliged to internally redeploy workers, if possible, when their positions are abolished.

Employment protection legislation also equalizes the costs of redundancies between society and individual firms. For example, if companies are required to finance further training for dismissed workers to facilitate their reemployment, these costs do not fall on publicly financed job centres.

Arguments against employment protection legislation

Other theorists argue that employment protection legislation reduces regular employment. For example, when firms have to give advance notice of dismissal for economic reasons, they must keep paying salaries to redundant workers for a certain period of time. Some theoretical models suggest that these regulations make employers reluctant to create regular jobs. Instead, they might use **informal employment** or temporary contracts, to which employment protection legislation usually does not apply.

Some argue that employment protection legislation hinders the free flow of workers between enterprises and slows the adjustment of the workforce in economically bad times. Over time, with development and technical progress, less productive jobs are destroyed and more productive ones are created. Regulations such as severance payments make it costly for companies to dismiss workers, causing inefficiencies and delaying productivity growth (Martin and Scarpetta 2011).

Employment protection legislation might also lead to inequalities by increasing the gap between 'insiders' and 'outsiders'. People in jobs with high security through employment protection legislation (the insiders) will be advantaged compared to those in unprotected jobs (the outsiders). However, the existence of outsiders can itself be a consequence of a failure to regulate. Instead of using precarious work as a temporary way to deal with an increase in activity, employers may be using it as an ongoing strategy to avoid labour regulation.



What does research tell us about the effects of employment protection legislation?

Research results in individual countries (single-country studies) may not apply to other countries. That is because of differences in the nature and extent of employment protection, economic conditions and labour market characteristics. Cross-country studies try to address this problem by using data from several countries. The challenge with these studies is to find comparable data for a broad range of countries. Some international organisations have developed summary indicators to assess the "strictness" of employment protection legislation in various countries and rank them accordingly.

Stable employment

Research evidence confirms that employment protection legislation leads to more stable employment by reducing turnover. For example, after a 1990 reform in Italy increased firing restrictions for small firms, research showed that turnover rates decreased in the companies affected (Kugler and Pica, 2008, pp. 78-95). Cross-country studies support this finding. A study using a sample of 16 industrial and emerging economies found strong evidence that stringent hiring and firing regulations tend to reduce turnover (Haltiwanger et al., 2010).

The authors of another cross-country study argue that when firms have less flexibility to adjust their labour force, it can impede productivity growth. However, they acknowledge that workers benefit from this form of regulation (Lafontaine and Sivadasan, 2009).

Employment levels

The evidence that employment protection legislation decreases employment levels is quite weak and inconclusive. However, there is widespread agreement that such regulation increases the gap between 'insiders' and 'outsiders'. For example, a study of the different impacts on permanent and temporary workers in Spain found that dismissal rates are higher among workers not covered by employment protection legislation (Boeri and Jimeno, 2005, pp. 2057-2077).

Impact on youth

The impact of employment protection legislation on youth unemployment is also inconclusive. Some studies conclude that strict employment laws hinder labour market access for younger workers (Botero et al., 2004). Others find no effect whatsoever (Noelke, 2011).

Size of enterprises

In some countries, studies show that employment protection legislation reduces firm size. In Italy, regulation is much stricter for firms with more than 15 employees. A 2003 study shows that companies with a size slightly below this threshold are reluctant to grow compared to much smaller or bigger firms, so as not to cross the line of 15 employees (Garibaldi et al., 2003).

Interpreting the research

It is important for trade unionists to look at studies like these with a critical and informed eye. Often there are weaknesses in the methodology used to carry out the research or interpret its results. Most research assumes that employment protection legislation will have an impact on economic outcomes without considering that there might also be an effect going in the other direction. For example, it may be that countries in economic recession, with low employment creation, tend to protect existing jobs through stricter employment protection legislation. It may be economic conditions leading to employment protection legislation, and not the other way around.

Look carefully at how researchers have chosen the indicators they use in their studies. In cross-country studies, summary indicators are often used to measure things like the "strictness" of employment protection legislation. These indicators are composed of many sub-indicators (for instance, several different hiring and firing rules). The research may not be telling us enough about the impact of these various sub-indicators.

Another frequent research limitation is not taking into consideration the degree to which employment protection legislation is actually enforced.

7.4. Minimum wages

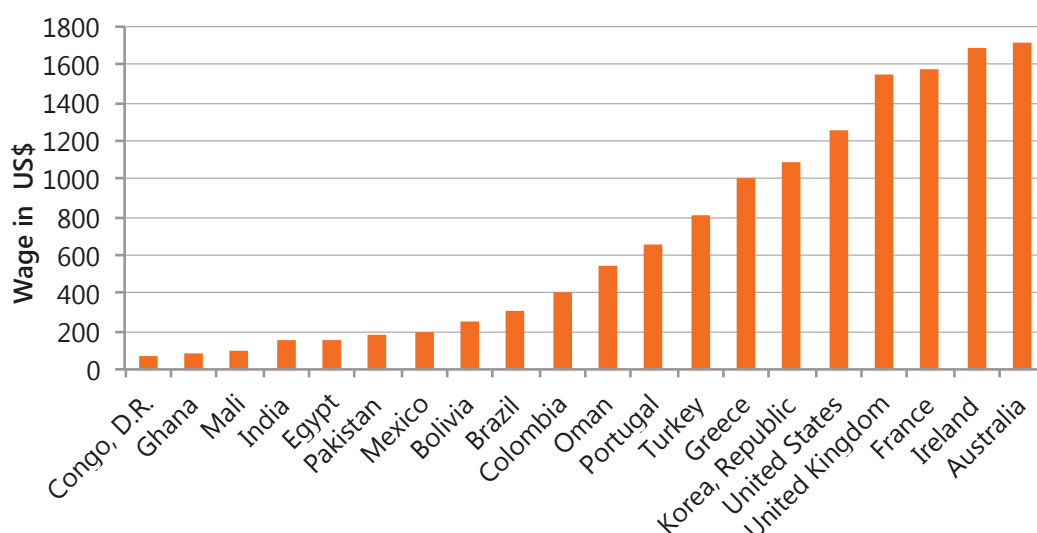
First introduced in New Zealand in 1894, the movement for minimum wages gained momentum in the context of sweatshop labour in the early 20th century. Today, over 90 per cent of countries worldwide have some kind of minimum wage law (ILO, 2013a).

The main objective of the minimum wage as a labour institution is to improve workers' welfare and to strengthen their bargaining power (Saget, 2001). Minimum wages mostly impact the lower end of the wage spectrum by setting a wage floor.

Minimum wages are established through complex fixing processes involving consultations between government representatives, workers' representatives and employers. They are often based upon arguments about how minimum wages affect labour market outcomes. Macroeconomic conditions, such as **inflation** or economic growth, also influence these discussions.

Rates, eligibility requirements and the frequency of adjustment differ drastically over time and among countries. For example, many countries have minimum wages only for specific sectors. Some have lower rates for some groups, such as youth. Figure 1 gives a sample of minimum wages around the world.

Figure 1. Minimum wages around the world, 2011, Purchasing Power Parity exchange rate (US\$)



Source: ILO, 2012

Notes: Pakistan data refer to the minimum wage for unskilled workers. United Kingdom data refer to the adult minimum wage. Oman data refer to minimum wages for Omanis in the private sector. (Migrant workers were not surveyed.)

Key messages of the International Labour Organization's guidance on setting minimum wages

The ILO Minimum Wage Fixing Convention, 1970 (No. 131) has been ratified by 116 states (ILO, 1970). It outlines key elements to consider in determining the minimum wage level.

Article 3

The elements to be taken into consideration in determining the level of minimum wages shall, so far as possible and appropriate in relation to national practice and conditions, include--

- The needs of workers and their families, taking into account the general level of wages in the country, the cost of living, social security benefits, and the relative living standards of other social groups
- Economic factors, including the requirements of economic development, levels of productivity and the desirability of attaining and maintaining a high level of employment.

Article 4

- Each member that ratifies this convention shall create or maintain procedures adapted to national conditions whereby minimum wages for covered groups of wage earners can be fixed and adjusted from time to time.
- In establishing, using and changing such procedures, provision shall be made for full consultation with representatives of the employers and workers concerned.

The effects of minimum wages: What theory tells us

Theories about minimum wages are highly dependent on the underlying labour market model.

Arguments against minimum wages

Those who oppose minimum wages often argue that minimum wages increase unemployment and push workers into the **informal sector**. The assumption is that firms – particularly smaller firms – can no longer afford to hire the same number of workers, because of the requirement to pay higher wages.

This argument is based upon a competitive labour market model, which assumes that workers have unlimited access to employment options and employers have unlimited access to hiring options. So employers have no incentive to offer more than the barest minimum wage that workers will accept. As a result, the theory predicts, the introduction of a minimum wage above that level will force employers to reduce employment (Fox, 2006).



Another argument is that minimum wages reduce the profit of business owners, and force them to look for alternatives such as new, labour-saving technologies. Or, in the case of bigger companies, employers may outsource production to countries that have no, or a lower minimum wage (Neumark and Wascher, 2007).

A third argument against minimum wages is that they prevent firms from reducing wage costs during economic downturns. This generates economic inefficiencies. For example, the inability to reduce wages below the minimum wage might force businesses to increase the price of their goods and services. The poor who purchase those goods and services will suffer more than the 'better-offs'. (Berg and Kucera, 2008).

Arguments in favour of minimum wages

Theorists who support minimum wages do not accept the theory that there is a perfectly competitive job market, where workers are free to move from job to job to maximize their income and job quality. These theorists believe that minimum wages are crucial to protect workers and ensure a decent standard of living for them and their families.

In the real-life labour market, when there are more workers willing to work than jobs available, vulnerable workers are easily underpaid. There are no head-hunters scouting for low-wage workers. Their families often rely solely on their earnings – that is true for 46% of families of affected workers (Fox, 2006). They are not likely to leave their jobs, even if wages are too low.

Another argument in favour of minimum wages is that they improve productivity. With minimum wages in place, it becomes in the employer's interest to invest in the workforce with training and to comply with safety and health standards.

Many of the first labour standards in the United States, in the early part of the 20th century, were directed against sweatshops. At the time, factories operated under piece-rate systems and there were no health and safety standards. Cramped workplaces affected workers' productivity, but this had little impact on employers because of the piece-rate system. The institution of minimum wages and health and safety regulations, as well as minimum age requirements, altered the incentives for employers. It became in their interest to upgrade production processes and make technological improvements. In the process, sweatshops largely disappeared in the U.S. (Berg and Kucera, 2008).

Keynesian economic theorists argue that, although minimum wages may create disincentives for employers, they can nevertheless increase employment by stimulating consumption. Low-paid workers are more likely to spend rather than save their wages.

Minimum wages can also drive up the average wage, leading to further positive impacts on consumption and employment. In developing countries, the minimum wage is often used as a reference point for other worker benefits. This is the so-called "lighthouse effect". If the minimum wage is set at a level that is meaningful for the **informal economy**, it may drive up informal sector wages (Gindling and Terrell, 2007a; Cazes, 2013, p. 207).

Finally, from a governments' point of view, minimum wage schemes are desirable because they decrease the costs of social welfare programs. By increasing the incomes of the poorest, minimum wages raise their incentives to join the workforce instead of remaining recipients of social welfare (Kallem, 2004).

In some countries, social protection benefits are tied to the minimum wage, as in most of Latin America.

If the minimum wage rises, so will pension, disability and unemployment insurance benefits. In Brazil for instance, there are 2.6 million people on disability/poor/elderly benefits and another nine million who receive the non-contributory minimum pension for agricultural workers.

The fiscal impact of an increase of the minimum wage can thus be extensive. In such countries, governments might resist increasing the minimum wage to avoid increasing the cost of social protection.

What does research tell us about the effects of minimum wages?

There is no global minimum wage, and results found for one country do not necessarily apply to others. It is often hard to find comparable data. This makes it hard for researchers to look at the effects of the minimum wage.

Minimum wage studies often differentiate between developed and developing countries. This is because, in developing countries, the informal sector often makes up half of the labour market.

Effects on developing countries

More and more studies are looking at the effects of minimum wages in developing countries on three outcomes:

- wages and employment in the formal sector
- wages and employment in the informal sector
- poverty reduction.

Several studies show that the minimum wage can help to protect the purchasing power of low-paid workers. In Costa Rica and Honduras, an increase in the minimum wage caused increases in the average wage in the formal sector (Gindling and Terrell, 2007a). However, there is also evidence that the positive effects of the minimum wage are strongly connected to compliance. In Honduras, for instance, only bigger companies could and have complied with the minimum wage (Gindling and Terrell, 2007b).

Although compliance is important, it is not the only factor that has an impact. Several studies show that the way the minimum wage is fixed also plays a significant role. In Columbia, a country with a relatively high minimum wage rate, it has improved the earnings of families in the middle and upper part of the income distribution, but not those on the bottom (Arango and Pachón, 2003). It is crucial to set the minimum wage in a way that minimizes job losses and non-compliance, while protecting the income of low-paid workers.

If set correctly, the minimum wage can have a positive impact on wages and formal sector employment. Brazil is a prime example. Although the minimum wage in Brazil nearly doubled from 2000 (R\$ 266) to 2010 (R\$ 510), formalization of the workforce increased. Several studies find that between 2000 and 2008, 66 per cent of the decline in income inequality was due to the increase in the minimum wage. Part of this decline was because social protection benefits levels in Brazil are tied to the minimum wage (Berg, 2010; Saboia, 2007).

One study in the Cambodian textile sector – one of the only industries covered by minimum wage in Cambodia – finds that remittances sent by women workers to the countryside have increased since the introduction of the minimum wage. This has benefited the rural poor (Saget, 2004, pp. 111-116).

Effects on developed countries

Some studies in developed countries find no evidence that minimum wages lead to job losses. On the contrary, one of these studies found that in New Jersey's fast-food industry, the introduction of a higher minimum wage increased employment (Card and Kruger, 1995).

Another research initiative in Oregon yielded a similar result, showing that Oregon had faster job growth than 41 other U.S. states and that low-wage employers added jobs at a faster rate after the implementation of a higher minimum wage (Oregon Center for Public Policy, 2005).

Research in Massachusetts, Florida and Hawaii found that there is no correlation between unemployment and the minimum wage. They found that the effects of the minimum wage depend on things like the degree of enforcement and the structure of the minimum wage (McLynch, 2004; Fox, 2006).

Nevertheless, some studies find that minimum wages have a small negative impact on employment, especially for young workers (Neumark and Wascher, 2007). However, evidence shows that higher wage levels outweigh these negative side effects (Fox, 2006).

The role of trade unions in setting minimum wages

What is a realistic way to set the minimum wage? It is generally agreed that wages should reflect the productivity of the economy. If wages increase faster than productivity, they will eventually produce inflation, and that penalizes wage earners. The minimum wage should reflect both overall productivity gains and the inflation rate. This ensures that the lowest-paid workers share in the increased well-being and do not see their earnings eaten away by price increases. Also, any minimum wage-setting exercise must reflect national circumstances and priorities.

To ensure that minimum wages protect workers and increase the standard of living for them and their families, at least four conditions have to be met when fixing or adjusting the minimum wage level (ILO, 2008):

1. Keep the design of the minimum wage system, whether it is a national rate or a set of rates for different sectors and occupations, relatively simple and easy to understand. Overly complex systems tend to be the least effective.
2. Take into account both the needs of workers and economic factors.
3. Extend legal coverage to the majority of workers, including those most vulnerable to exploitation, such as domestic workers.
4. Set up a well-functioning mechanism to enforce compliance.

The minimum wage-setting process should involve full consultations with representative organisations of employers and workers, as well as independent people representing the general interests of the country. It is also important to involve the informal economy in the determination of the minimum wage, especially in developing countries. The International Labour Organization's Minimum Wage Fixing Convention (No. 131) provides good guidance on how and what to address in the minimum wage fixing process (ILO, 1970).

One of the main challenges for trade unions in developing countries is to refrain from using national negotiations about minimum wages as a forum to achieve higher wages for their own constituencies. If they do this, they run the risk of undermining the minimum wage setting process. They may end up with no consensus, or with a minimum wage that does not represent a realistic threshold to protect the most vulnerable in the workforce (Saget, 2008, pp. 25–42).



7.5. Employment and social protection



Social protection is a country's system of benefits for people and their families when they are poor, sick, disabled, out of work, elderly or young and dependent on others. The benefits may be provided by the state's social security system, through private insurance, through personal savings, through various social customs and relief organizations, or through some combination of these sources (United Nations Research Institute for Social Development, 2012).

Social security and welfare systems arose in higher-income countries, where they have always been linked to a person's status as a citizen and participation in the labour market. Through employment, people, firms and governments paid into insurance schemes such as workplace injury insurance, unemployment insurance, sickness, maternity and health insurance, old-age, disability and survivors' pensions. Through taxes, workers and firms paid for protections such as social assistance for the poor, health care and education.

Organized labour and collective action helped to establish these social security schemes. They were made possible by the gradual expansion of formal wage employment and universal labour regulations. These social security systems can only be sustained through high levels of formal employment.

The 'de-linking' of social protection and employment

In Booklet 5, we discussed the shift in macroeconomic policy that has been occurring since the 1980s, with its emphasis on market forces, free trade rules, and the need to minimize interference with market mechanisms. This policy perspective sees social protection more as an after-thought an ambulance racing to address some of the worst social fallouts of free market policies.



In the drive to improve efficiency when resources are scarce, there has been a growing emphasis on policies that target certain categories of people who are in greater need. Targeted social policies usually identify the vulnerable to be those presumed unable to work – children, the disabled and the elderly, for example. The presumption is that labour markets provide sufficient support for those able to work. Social protections are separated from labour market status and employment outcomes.

Poverty reduction strategies are one example of the disconnect between employment and social protection. These are strategies that poor countries develop with external partners such as the International Monetary Fund and the World Bank. They describe the macroeconomic, structural and social policies and programs that a country will pursue over several years to promote growth and reduce poverty. Often these strategies are driven by economic policies that emphasise economic growth rather than employment. The view is that, after the conditions for growth have been secured, social policies could direct a portion of the resources generated to provide social services (such as education and health care) and limited assistance to vulnerable populations excluded from the benefits of growth (the so-called 'trickle-down effect').

The de-linking of employment and social protection can also be seen in emerging forms of social protection in developing countries. Conditional cash transfer programmes, for example, are not directly linked to job status. These programmes cannot adequately replace income from wages and the robust infrastructure of social services and benefits, such as pensions, that have traditionally been linked to employment (UNRISD, 2012).

The linkages between social policy and employment have also been weakened by emerging trends in labour markets. Those with full employment and full social security coverage constitute a shrinking share of the total workforce in many countries. In high-income countries, growth of **precarious employment** arrangements has meant new gaps in employment-based social protections. Advances in technology and communications have dispersed job opportunities around the globe. While good for productivity and profits, global integration has unleashed competitive pressures to reduce labour costs. Workers have not always been able to reap the benefits of higher productivity through improved wages and more robust social protection.

Bargaining power has been shifting in favour of employers, while labour organisations have lost ground. This has made it difficult to sustain collective action in support of social protection. With international sourcing, capital has an exit strategy if the costs of social protection are seen as too burdensome.





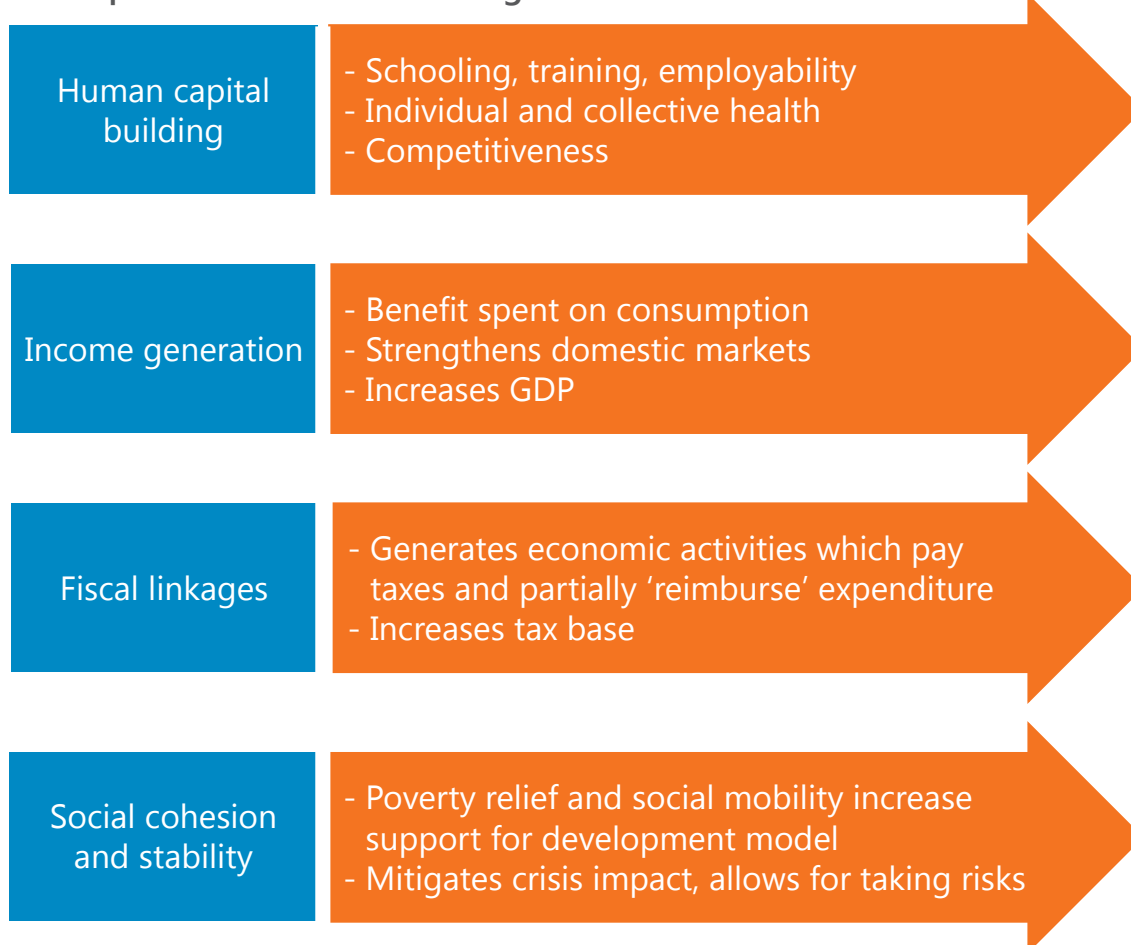
Why we need to strengthen the connection between employment and social protection

Employment and social protection policies must stay connected in policy design in order to frame solutions grounded in long-term, sustainable, employment-centred growth. There is ample evidence that social protection systems benefit the economy and labour market. They provide income for consumption to the unemployed, the disabled, the elderly and other vulnerable groups. They stabilize consumption during recessions, supporting enterprises until the next growth cycle. Social protections such as health care and occupational safety increase people's labour productivity. And social services themselves generate substantial employment, especially among women. These effects of social protection on employment are called linkages.

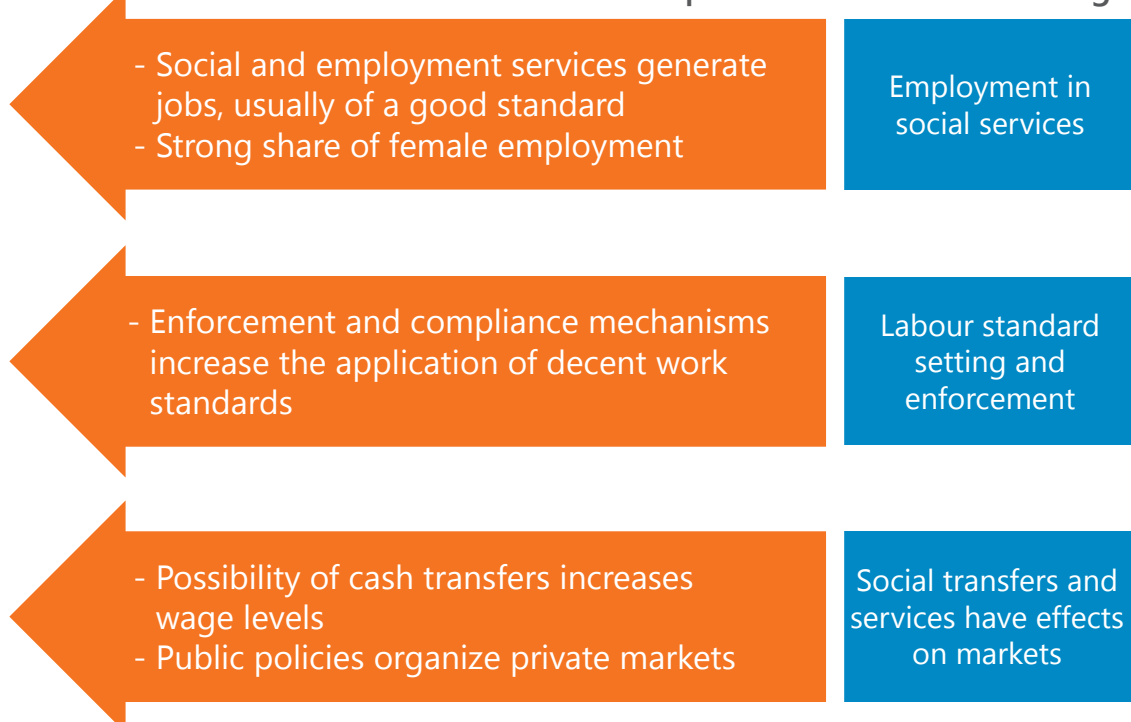
Backward and forward linkages between employment and social protection

Here are some **backward and forward linkages** found in an International Labour Organization study of social protection and employment in Burkina Faso, Cambodia and Honduras (ILO, 2013). These linkages show that employment strengthens the prospects for growth and social protection and vice versa.

Social protection's forward linkages

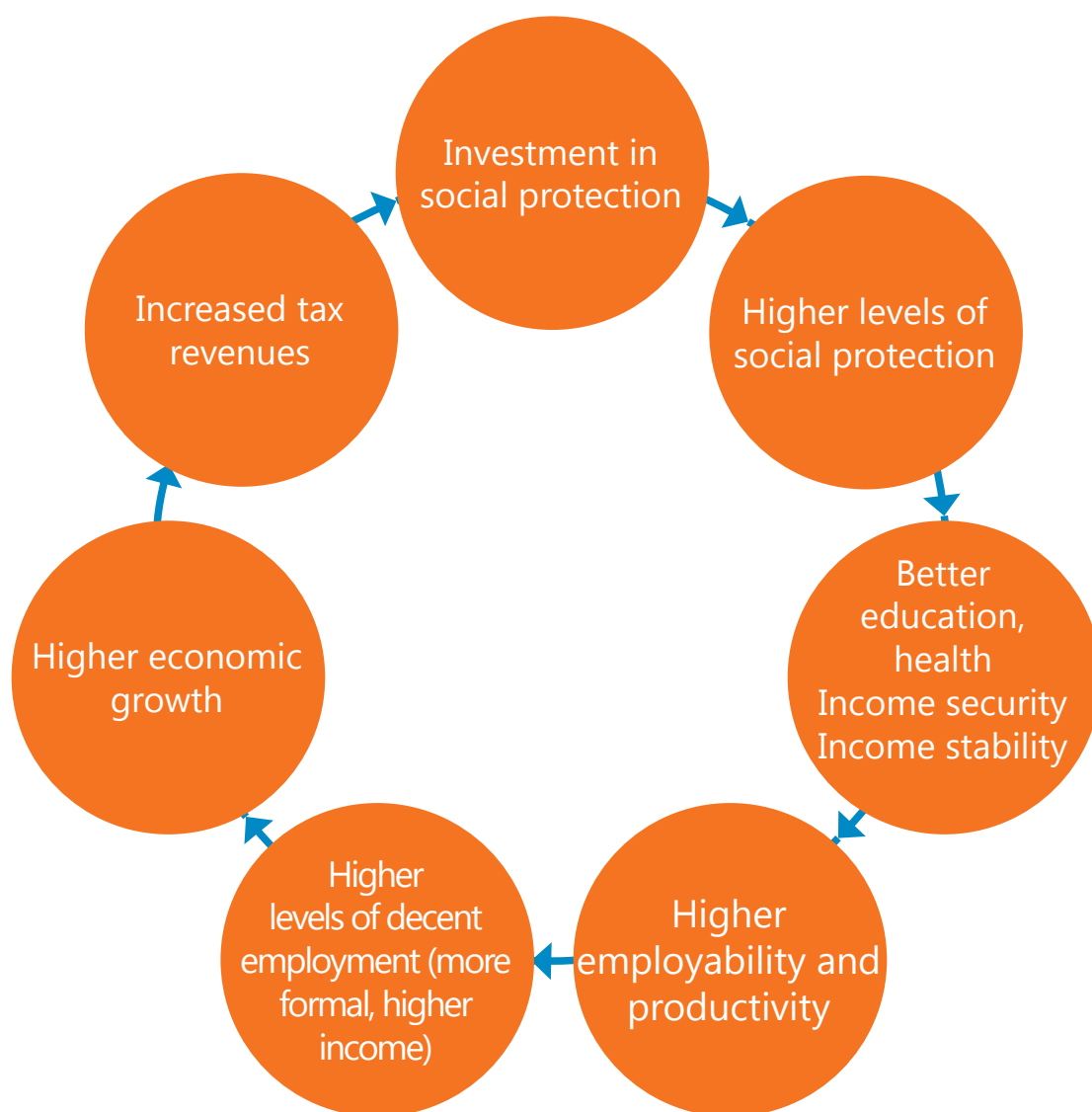


Social protection's backward linkages



Bachelet's "virtuous circle"

The Bachelet Report, named after the president of the ILO Social Protection Floor Advisory Group, links social protection investments with better health, education, services, stability and income security (ILO, 2011). These things generate more productivity and **employability**. They are the prerequisites for a higher level of formal employment and a larger tax base. These in turn allow for more expenditure on social protection and employment policies. This is the "virtuous circle":



However, to make sure that the virtuous circle fulfils its promises, a number of conditions are required. Social, employment and development policies will only result in more protection and employment if they are properly designed and operated. The strength of the circle diminishes if the goods and services demanded by social policy beneficiaries and newly employed persons are not available.

If the policies are ill-targeted and the benefits are captured by non-target groups, it will cause further income concentration and fail to alleviate poverty and social cohesion.

Another condition for the success of the virtuous circle is a successful fight against tax evasion. Without this, the additional employment and economic activity will not create the fiscal space for sustainable policies.

CASE STUDIES



India and Latin America

In India, expenditure on social protection over the period from 1973 to 1999 had a positive impact on economic development. Social security policies boosted the productive capacities of the poor, increased incomes and promoted employment (Justino, 2007, pp. 367–382).

Argentina, Brazil and Uruguay have shown that it is possible for a high level of economic growth and formal employment creation to proceed stepwise with the development of an encompassing social protection model. This, in turn, feeds back into economic growth by strengthening the domestic market (Berg, 2010).



What is a social protection floor?



Social protection floors are nationally-defined sets of basic social security guarantees aimed at preventing or alleviating poverty, vulnerability and social exclusion. These guarantees should ensure at a minimum that, over the life cycle, all in need have access to essential health care and basic income security. They should have the following four social security guarantees:

- access to essential health care, including maternity care
- basic income security for children, providing access to nutrition, education, care and any other necessary goods and services
- basic income security for people who are unable to earn sufficient income because of sickness, unemployment, maternity and disability
- basic income security for older persons.

The International Labour Organization adopted a Social Security Strategy at its 2011 and 2012 International Labour Conference. The newly adopted international labour standard Social Protection Floors (Recommendation, 2012) aims at re-establishing the link between economic, employment and social protection policies. It is a very strong call for policy coherence and coordination. The strategy emphasizes the need to move from informal to formal employment and to support universal rights to social security.

What are the policy implications of reconnecting employment and social protection?

States need revenue-harnessing systems, such as taxes, to sustain social protection. Taxation systems need high levels of employment to generate the needed taxes and social security contributions. They should avoid macroeconomic policies that dampen employment creation.

States may need new forms of labour market regulation to redress the structural inequities, such as labour market exclusion and low pay in sectors where workers do not have bargaining power.

A successful social protection floor is one that has strong links with employment policies. By investing in human capital, the social protection floor contributes to “a settled and productive work force”. At the level of macroeconomic policy, a successful social protection floor can also act as a stabilizer during times of recession, providing a basic income to stimulating demand for goods and services (UNRISD, 2012).

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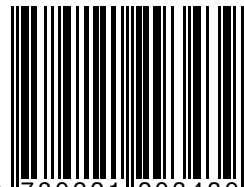
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