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LABOUR MARKETS, INSTITUTIONS AND INEQUALITY

Building Just Societies in the 21st Century



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1. Labour market institutions: the building blocks of just societies

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1.1 INTRODUCTION

Equitable societies with large middle classes are not the natural outcome of market forces. Equity, rather, is created by society, by the institutions – the laws, policies and practices – that govern the society, its economy and, in particular, its labour market. Building just societies means designing institutions that support the creation of quality jobs with decent wages and working conditions, as well as enacting policies to support those who cannot work or who are unable to find work.

This book argues that the lack of, or erosion of certain institutions that govern the labour market has contributed to rising inequality in many countries across the world, jeopardizing individual as well as societal well-being. Thus, if a country wants to improve equity it will need to strengthen its labour market institutions. The book employs a broad definition of labour market institutions that includes the more familiar institutions that regulate the workplace – collective bargaining, minimum wages, the type of employment contract, and working time regulations – as well as those institutions that redistribute income, including pensions, income support for the unemployed and the poor, as well as public social services. Because work is by far the most important source of household income among non-retired households, the book also considers full employment policies in its analysis. A commitment to full employment implies not treating employment as a residual outcome of economic growth, but designing and implementing policies that make job creation an explicit goal.

As the book is concerned with overall equity in a society, it considers not just wage and income inequality, but also inequality between groups. When labour markets are well regulated, when there are encompassing welfare states and when public social services are offered broadly to the population, there is greater equality between groups – as well as greater overall equality in wage and household income. Thus, achieving inclusiveness and equity requires constructing institutions that support people both

in and out of the labour market. Too often, debates on labour market institutions have pitted workers against each other – as the privileges of ‘insiders’ gained at the expense of the ‘outsiders’ – resulting in calls to deregulate the labour market in the false hope of achieving greater equity. But the dismantling of labour protections and the retrenchment of social policies only leads to greater inequality, in society as a whole and between groups.

Institutions do not work independently, but are part of overarching systems that govern the labour market and the economy. Thus, in societies where wages are decent and more equitable, there is less need for redistribution through taxes and transfers. Moreover, social policies are not ex post interventions, but are part of these larger systems as they can influence access to the labour market as well as wage levels. For this reason, the policy focus on ‘equality of opportunity’ risks being short-sighted, unless there are policies that are also directed at ‘equality of outcomes’. Indeed, where income is distributed more evenly, there is greater inter-generational mobility (Corak, 2013; Piketty, 2014). As the former Finnish president and 2008 Nobel Peace Prize laureate, Martti Ahtisaari, quipped, ‘to live the American dream, you have to go to Sweden’ (*Le Temps*, 2013).

Since its founding in 1919, the International Labour Organization (ILO) has sought to help its member States build just societies by adopting conventions and recommendations that govern the labour market. These international labour standards help shape national labour laws and policies and provide guidance on improving labour market governance. They address issues of employment, working conditions and social policies, but also freedom of association and collective bargaining, tripartite consultation and labour inspection. For this reason, many of the chapters in the book relate the policies discussed to the relevant international standards.

This introductory chapter sets forth the rationale for a new policy effort based on labour market institutions that can help build (or re-build) equitable societies. The rest of the book is divided into four parts. Part I on macroeconomic policies, development and inequality begins with an analysis of the relationship between economic development and income inequality and the role of political forces in shaping the distribution of income. This is followed by a chapter on the need for macroeconomic policies to promote full employment. Part II addresses some of the labour market institutions that affect income from work, including chapters on unions and collective bargaining, minimum wages, and the regulation of employment contracts (temporary and part-time work). Part III analyses social transfers and income redistribution and their contribution to fostering greater equality, including the design of tax and transfer policies, pensions, income support for the unemployed and the poor and public

social services. Part IV addresses how labour market institutions affect the inequality of women, migrants and youth.

1.2 IN MOST REGIONS OF THE WORLD INEQUALITY HAS BEEN INCREASING

Since the 1980s, there has been an increase in income inequality in most regions of the world, including most industrialized as well as many developing countries. The growing income gaps have affected both the functional distribution – the distribution of the national income between profits and wages – as well as the personal income distribution, which is the distribution of income among households or individuals. Personal income distribution includes income from work (including self-employment), from investments, but also from private and public transfers, including remittances, as well as social security and social assistance transfers.

Most discussions of increased income inequality have been divorced from trends in the labour share, reflecting a bias in the economics professions towards the study of individual labour market earnings. This bias is due, in part, to the influence of human capital theory, which emphasizes how a person's education, experience and characteristics affect their earnings, but also as a result of the widespread availability of micro-datasets that have allowed researchers to estimate these returns, disassociated from larger movements in the macroeconomy. But workers' well-being is dictated by their relative gains from national economic growth, or how the growth in output is shared between capital and labour. When overall productivity growth surpasses total wage growth, then labour shares fall (and vice versa). Falling wage shares translate into the personal distribution as stagnant or slow average wage growth. And, to the extent that highly skilled workers command earnings that are tied to profits or are more favoured relative to low-skilled workers, then there will be divergences in the personal income distribution.

In the decades following World War II, both capital and labour benefited from the rise in national income, and in some instances, labour's share increased in proportion as employment growth and wage gains led to rising wage shares in many countries. But beginning in the 1980s, in many countries of the world, the trend reversed and the share of national income accruing to capital began to widen, with profits commanding a greater share. Numerous reports from international organizations (IMF, 2007; ILO, 2008, 2010; ILS, 2011; OECD, 2011; UNCTAD, 2012) have documented this divergence for industrialized countries and some developing countries. The ILO (2013a) found, for example, that the labour

share declined from 75 per cent of national income in the mid-1970s to 65 per cent in the years before the financial crisis for 16 advanced economies, calculated as a simple average. For developing countries, the picture has been more mixed. In Asia, the wage share declined by roughly 20 percentage points between 1994 and 2007; in China, between 2000 and 2007 the wage share fell by 10 percentage points, despite significant average wage increases (IILS, 2011). In Brazil, labour's share in the national income dropped by five percentage points during the difficult decade of the 1990s, but then recovered in the 2000s (IPEA, 2010).

The growing divide between profit shares and wage shares has, in many countries, been driven by a disconnect between productivity growth and wage growth. Between 1999 and 2011, average labour productivity growth outpaced average wage growth by a two-to-one ratio in 36 developed countries for which there were data (ILO, 2013a). But these trends have not been uniform across workers. Workers in less-skilled and semi-skilled occupations have had little, if any, real wage growth, whereas the wages of highly skilled workers and particularly those whose earnings are in the top 1 per cent of the income distribution have gained the most (ILO/IILS, 2011). Moreover, the concentration of wealth among the top 1 per cent of the income distribution has intensified in many industrialized countries, and will likely continue to do so unless significant reforms are implemented (Piketty, 2014). The trends in income concentration have been coupled with a retrenchment of the welfare state in many advanced economies. According to the OECD (2011), of 27 countries for which it has data, the growth of incomes in the bottom decile exceeded that of the national average in only eight countries¹ between the mid-1980s and the late 2000s, whereas the growth in incomes of the top decile exceeded the national average in 18 countries.

Figure 1.1 is a map of changes in household income inequality between the early 1990s and late 2000s.² In most industrialized countries – Canada, the United States, most of Europe and Australia and New Zealand – inequality, as measured by the Gini coefficient, increased. Inequality also increased in Asia, including India and China, and parts of Africa, particularly Southern Africa. In Latin America, inequality increased slightly in a few countries in the region, but fell in most of the region. Inequality also fell in a handful of African countries. Nevertheless, Latin America remains the most unequal region of the world, slightly below Southern Africa.

The increase in inequality in developing countries has not always been a concern of policy-makers, many of whom have subscribed to the view that rising inequality is part of the development process. The structural transformation of shifting production and workers from low-productivity agriculture to high-productivity manufacturing was believed to go hand in hand with widening urban–rural wage differentials, which would only cease



Notes:

The measure used is the comparison of Gini coefficients for the first year between 1990 and 1995 for which data is available and the last year between 2005 and 2010 for which data is available.

Due to data constraints for African countries, we employed a less strict definition and used data for the following countries and years: Burkina Faso: 1994 and 2003; Cameroon: 1990 and 2002; Central African Republic: 1992 and 2003; Gambia: 1992 and 2003; Ivory Coast: 1990 and 2002; Mauritania: 1990 and 2000; Mozambique: 1996 and 2005; Nigeria: 1990 and 2004; United Republic of Tanzania: 1990 and 2001.

Source: Standardized World Income Inequality Database (SWIID).

Figure 1.1 Changes in income inequality, early 1990s vs late 2000s

when the pool of surplus labour was exhausted and structural transformation completed (Lewis, 1954; Kuznets, 1955). The widening of inequality would be followed by a narrowing of the distribution as incomes reached a higher level, resulting in Kuznets's inverted-U curve. But as Sangheon Lee and Megan Gerecke (Chapter 2 of this volume) remind us, Kuznets 'never intended to offer an immutable law of inequality and development' (p. 41); nonetheless, the curve has been interpreted as a 'natural law' of inequality with little role given for policy interventions. Furthermore, as Lee and Gerecke point out, Kuznets argued that inequality would narrow as a result of growing political pressure from lower-income groups, facilitated by the spread of democracy. Thus, the distribution of income – whether it will narrow or continue to expand – is largely determined by political power and its influence on shaping distributive and redistributive policies (Chapter 2). Financialization, globalization and technological change have, however, eroded the bargaining power of the lower-income classes at the workplace as well as their ability to mobilize collectively for political change, affecting the distribution of income in many parts of the world.

Thus, we see, for example, that in the United States, the growth in real after-tax income between 1979 and 2007 was 278 per cent for the top 1 per cent of the income distribution, whereas for the bottom quintile it rose by a mere 18 per cent, and by just 35 per cent for the middle quintile.³ The increase in top incomes was facilitated by the 1987 tax reform that lowered income tax rates for high earners as well as capital income, whereas the weakening of collective bargaining and low value of the minimum wage, along with the retrenchment in the welfare state, explain the stagnant income growth of the poorer classes.

Overall, income inequality has increased in Europe, though the experience among countries has been mixed as a result of country-specific tax policies, the extent that labour institutions support workers at the bottom of the income distribution, and the relative strength of the welfare state. Germany has seen an important rise in inequality, mainly due to a decline in earnings of those at the bottom of the wage distribution. There has been a divergence between productivity and wage growth, with labour productivity increasing by 23 per cent in the 1990s and 2000s, whereas real average monthly wage growth was flat, and even declined in the 2000s. The rise of 'mini-jobs' partly explains these trends, though on an hourly basis the same pattern holds (productivity growth of 12.8 per cent and wage growth of 0.4 per cent) (ILO, 2013a). In the Nordic countries, incomes of highly skilled workers have increased, but a strong welfare state has propped up incomes of the bottom deciles, thereby avoiding a polarization in incomes. In Sweden, however, inequality did increase – although it still remains low – as a result of widening gaps in market income and declines in redistribution. France had only a slight increase in inequality in the 2000s, which is attributable to the expansion of self-employment income (OECD, 2011). Wages of the lower-income groups continue to be supported by the minimum wage and extension mechanisms of collective bargaining.

Asia, which was known for its rapid growth with low levels of inequality during the 1980s and 1990s, has, in the first decades of the 21st century, given way to a pattern of exclusive growth. This is true of the more advanced economies of Japan and the Republic of Korea, where inequality has widened since the late 1990s, but is also the case with new giants such as China, Indonesia and India (ADB, 2012). Throughout the region, employment growth has been tepid and many of the jobs that have been created have been of poor quality. Informal self-employment has continued to expand and waged employment has been characterized by growing precarization and limited social protection coverage (ILO, 2010). Moreover, both China and India have witnessed speculative booms in real estate coupled with rising incomes in the banking, finance and information technology sectors (Galbraith, 2012). As a result, there has been both a

decrease in the share of national income going to wages, as well as widening dispersion of income among workers.

Latin America, despite having the dubious distinction of being the most unequal region in the world, reduced inequality in the 2000s. The decline stems from a compression in wage earnings, with government transfers playing a supportive secondary role. The compression in incomes is partly due to an increase in education and the return to skills as López-Calva and Lustig (2010) suggest, but it is also the result of the creation of formal jobs – which shifted workers from the more unequal self-employment jobs to waged employment – as well as from a strengthening of labour market institutions, particularly increases in the real value of the minimum wage, but also a strengthening of collective bargaining, especially in Uruguay, Brazil and Argentina. Indeed, in Argentina, Brazil, Mexico and Uruguay, reduced inequality in labour incomes accounted for over 60 per cent of the fall in inequality, most of which occurred amongst registered wage earners (formal workers). Public cash transfers were important – particularly in Chile and Mexico where they contributed over 25 per cent to the reduction in inequality – but the main driver was the reduction in inequality in labour income. In Mexico, where informal employment is particularly large, most of the declines in inequality were amongst unregistered waged workers; self-employed earnings contributed to inequality (Keifman and Maurizio, 2012).

In Africa, the picture has been mixed. There are some countries, such as Ethiopia, with very low levels of recorded inequality, reflecting in part the low levels of income per capita, and other countries, such as South Africa, which boasts the highest income inequality in the world. South Africa had made some headway in lowering inequality at the end of the 1990s, but this was reversed in the 2000s as wage dispersion increased to the benefit of the largely white workers at the top of the wage distribution; wages at the bottom have been negatively affected by the rise of contract work. However, two cash transfer programmes have helped to alleviate poverty in the bottom deciles, which remain affected by high rates of unemployment (Bhorat et al., 2013). In Kenya, the relatively successful economic performance of the 2000s did not translate into labour force gains, as contract work and informal work proliferated, leading to a greater dispersion of income (Wambagu and Kabubo-Mariara, 2013).

Although the causes for rising income inequality differ among countries, the weakening of labour market institutions has played either a leading or supporting role in bringing about these trends in many parts of the world. In Latin America, these institutions figured prominently in helping to redress the large inequalities that exist in the region. Still, for the greater part of the last three decades, labour market institutions have

come under attack, blamed for the less than stellar economic and labour market performance experienced in many parts of the world.

1.3 THE DEBATE ON LABOUR MARKET INSTITUTIONS

The weakening of labour market institutions in many parts of the industrialized and developing world over the past several decades is often attributed to globalization. The widespread integration of financial and goods markets that began in the 1980s, coupled with improvements in information technology, the rise of democratization, and overall improvements in literacy and education throughout many parts of the world, facilitated shifts in production to countries that had formerly been excluded from the world economy.

Although globalization has brought prosperity to some, there have been important political effects from greater economic integration that were largely unforeseen (Acemoglu and Robinson, 2013). One important effect was the widespread weakening of the political power of labour, as manifest in the decline of unionization rates in much of the industrialized world and some developing countries (Chapter 4). As Hayter explains in Chapter 4, labour's weakened ability to act as a 'countervailing force' meant that in some countries, reforms were instituted that negatively affected workers, including trade reforms, financial deregulation, orthodox monetary policies⁴ and the scaling back of the welfare state. Moreover, even where labour's voice in national affairs remained strong, because capital became global but the scope of policy intervention remained national, many countries had difficulty in responding to the challenges brought about by globalization.

In developing countries, globalization did sometimes lead to the creation of new jobs in employment-intensive export industries, but governments often held down wages and repressed unions, out of concern that wage increases would lessen their countries' competitive edge. Moreover, in countries where the economic reforms had less than satisfactory results with regard to economic performance and employment, 'rigid' labour markets were blamed for impeding the potential of globalization. In industrialized countries, the debate on labour market flexibility came to the fore with publication of the 1994 OECD *Jobs Strategy*, which argued that the lower unemployment rates of the United States of the early 1990 were due to its more flexible labour market. Thus, if Europe wanted to lower its unemployment rates it would need to flexibilize its labour market, particularly its employment protection laws, restrictions on working time, wage

policies and unemployment benefit systems. It was argued that wages needed to respond to signals in the market, thus decentralized collective bargaining was preferred, or in its absence, a system that allowed opt-out clauses at the firm level. Minimum wages were discouraged and the report suggested that countries should ease restrictions on dismissal and permit the use of fixed-term contracts (OECD, 1994).

In developing countries, a similar viewpoint was espoused.⁵ Here again many of the same institutions attacked in the OECD *Jobs Strategy* became targets for labour reforms in developing countries.⁶ Furthermore, labour market reforms were often included as part of conditions on loan agreements, such that, even in countries where reforms were not supported or deemed necessary by the government, the countries were urged to implement them in order to receive bail-outs.⁷ This occurred in the Asian crisis of the late 1990s, and is occurring in the 2010s in Southern Europe under the troika (comprising the European Central Bank, European Commission and International Monetary Fund).

Perhaps the most emblematic of efforts to deregulate labour markets was the World Bank's 'Doing Business' indicators. Launched in 2002, the index ranks countries according to their 'ease of doing business', and includes a sub-index on labour laws, known as the 'Employing Workers' index. The Employing Workers index assessed the degree of regulation in labour markets in the areas of working time, minimum wages, dismissal protection, severance pay and non-wage labour costs, based on a benchmark of no regulation and zero cost. As a result, countries with more regulated labour markets were ranked lower in the index.

Support for the deregulatory stance of the multilateral organizations came largely from economic theory, as empirical evidence on the effect of institutions was mixed (Nickell and Layard, 1999). Under the standard (neoclassical) economic model of labour markets, wages are determined by the intersection of demand and supply in the labour market; the labour market clears – meaning that there is full employment – as long as there are no impediments. As a result, unemployment is viewed as a problem of the labour market, rather than as a problem of insufficient aggregate demand. Policy-makers, unfortunately, came to depend on the predictions of this simplistic model, ignoring its numerous critiques.⁸

In the 2000s, there seemed to be some recognition that the push to deregulate labour markets had gone too far. In 2006, the OECD published a reassessment of the *Jobs Strategy*, which, although nuanced, gave greater scope to minimum wages, softened the position on employment protection legislation, and recognized the positive economic and employment performance of economies with centralized collective bargaining (OECD, 2006; Watt, 2006). In 2011, the World Bank revised its

Employing Workers index based on criticisms from trade unions, the ILO and some governments, and dropped the score of this index from the calculation of overall country rankings under the Doing Business indicators.⁹ While there was political pressure against the calls for labour market deregulation, a prime motivation was the new empirical evidence, discussed in Part II of this volume, which showed that minimum wages were not detrimental to employment creation, that more flexible employment protection legislation had resulted in more segmented labour markets, and that encompassing collective bargaining systems delivered beneficial outcomes to workers, firms and economies. This debate was also addressed in the 2013 *World Development Report: Jobs*, in which the World Bank concluded that ‘the impact of labour policies and regulations on the labour markets of developing countries was modest’ and ‘certainly more modest than the intensity of the debate would suggest’ (World Bank, 2012, p. 26).

1.4 THE WORKINGS OF LABOUR MARKET INSTITUTIONS

An underlying thesis of this book is that labour market institutions do not work independently but have important interaction effects. Thus, when designing policies it is important to not only understand that there may be secondary effects from the policies, but also to consider how to take advantage of these secondary effects in policy design. These effects may be economic, but they can also be social or political, by changing the balance of power in society, thus affecting future policy design (see Acemoglu and Robinson, 2013). Tinbergen (1967) famously argued that we need as many instruments as targets in order to reach a policy goal. But just as we are better off having more tools than goals, we also should not expect so much from just one tool. Too often policies are criticized for failing to reach goals that were never prescribed to them in the first place. Some examples include unemployment insurance, which is criticized for not covering the poor when its intention is to smooth the income of displaced workers during labour market transitions. If it fails to help the poorest in society, the policy response should be to enact policies that help the poor, not destroy unemployment insurance.

Similar arguments can be made regarding the minimum wage. In the USA, as elsewhere, the minimum wage is criticized for not ‘lifting families out of poverty’ when its stated objective under the US Fair Labor Standards Act (1938) was to prevent and eliminate low labour standards that harm workers and undermine fair competition (Kaufman, 2010). We should therefore assess its effectiveness on these grounds. In other cases,

the minimum wage is over-used, often to compensate for underdeveloped collective bargaining and industrial relations' systems.¹⁰ Examples include the Dominican Republic, which has minimum wages by sector, occupational category, and in some cases for the task at hand – for example, there are varying wages for construction workers who install beams of different sizes or operate machinery with greater horsepower. This complex and fragmented system hinders compliance by making it more difficult for workers and employers to know the correct wage, and also makes monitoring more difficult (OIT, 2013a). Countries with weak or non-existent collective bargaining also run the risk of setting their minimum wage too high, at a level that benefits the average worker, rather than as a floor to prevent low standards. Too high a minimum wage can result in non-compliance, as well as weaken the productivity–pay link (Lee and Gerecke, 2013; Rani et al., 2013).

Labour Institutions and the Production Process

Labour market institutions can affect firms' decisions on how (or where) to structure production, including how much to invest in training or technological upgrading. In their seminal study, *Industrial Democracy*, Webb and Webb (1902) argued that wage floors were an effective policy for preventing what they termed 'parasitic' industries, or industries that paid wages that were insufficient to cover the social costs of the worker. Similar arguments were advanced in the 1950s by the Swedish trade union economists Rudolf Meidner and Gösta Rehn who argued about the importance of collective bargaining and minimum wages for putting 'technological laggards' out of business, coupled with policies to boost investment and aggregate demand (Galbraith, 2012).

Piore (2004) explains how many of the first labour standards in the USA were directed against the sweatshop production model and industrial homework. As he explains, under a piece-rate system, employers have little incentive to invest in technological or organizational improvements, or worker health and safety, since it is the workers' earnings that fall if they are less productive. But state regulation of working conditions, including health and safety laws, minimum age requirements, minimum wages, and employment protection, altered the incentives of employers.¹¹ By mandating health and safety and requiring that a minimum wage be paid, employers had no choice but to upgrade production processes and make technological improvements, contributing to the decline of sweatshops in the USA in the first part of the 20th century. Yet under the current model of globalization, with the ease and low cost of communication and shipping, sweatshops have re-emerged as businesses in many industrialized

countries have subcontracted their manufacturing to countries with weak and unenforced standards on health and safety, wages and working time, as well as constraints on freedom of association and collective bargaining rights. The April 2013 collapse of the Rana Plaza Building in Bangladesh, which left over 1200 garment workers dead in one of the deadliest industrial accidents of all time, is a grim and shocking reminder of the need for regulating working conditions.

Labour Institutions and Workers' Access to the Labour Market

Institutions also affect workers' access to the labour market, influencing their decision to participate in or withdraw from the labour market, as well as affecting the types of jobs they pursue. Several chapters in this volume address this theme. One emblematic example concerns the provision – or lack of provision – of care services, which can determine women's ability to enter or remain in the labour market, with consequences for both gender and income inequality. As discussed in Chapters 11 and 12, most women shoulder the primary burden of care responsibilities. If care services are not provided publicly, then women either outsource these services if they can afford to do so, or withdraw from the labour market. Alternatively, they choose professions that allow them to balance their work and family responsibilities, or work in part-time and informal employment, often with marked differences in wages, hours and access to benefits (see Chapter 7 on part-time work).

Reconciling care responsibilities with work is most difficult for lower-income women. Women from higher-income quintiles have the financial means to outsource or 'commodify' care responsibilities, thus perpetuating inequality between groups. Among women with children under six years of age in Latin America, the labour force participation rates of women from the poorest quintile are just 40 per cent compared with 70 per cent for the richest (Chapter 11). Moreover, those of the poorest income quintile who do work may either be exacerbating 'time poverty' or redistributing responsibilities to other, typically female, household members. This finding is substantiated by the higher share of young female NEETs (not in education, employment or training) from lower-income families, as demonstrated in Chapter 14 on youth.

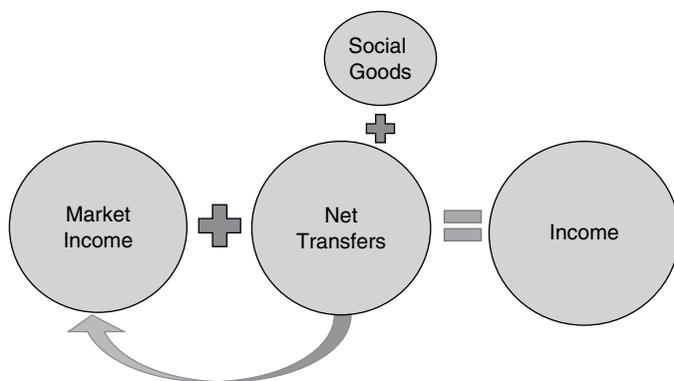
In other cases, labour institutions, particularly social policies, can be an effective means for reducing labour supply. Increased access to secondary and tertiary education can help postpone youth entry into the labour market, allowing young people to further their education and training, thereby boosting their human capital formation and relieving pressure on the labour market. The availability of social protection, especially old-age

pensions, affects the labour supply decisions of the elderly. Chapter 9 documents the significant negative relationship between coverage and benefit levels of pensions and the labour force participation of the elderly. Social assistance programmes, by raising family incomes, can also mitigate desperation and thus the likelihood of falling victim to forced labour or other forms of exploitative work. In Brazil, the decline in forced labour in the country has been partly attributed to the conditional-cash-transfer programme, Bolsa Família (OIT, 2013b).

Labour Institutions and Wage Determination

The relationship between earnings on the job and institutions that regulate the labour market such as collective bargaining, minimum wages and contract type is relatively straightforward, but earnings are also mediated by the existing social policies of a country. As Figure 1.2 illustrates, a household's income is not just the sum of market income plus transfers – transfers can influence wage-setting.

A good example is employment guarantee programmes (also known as employer-of-last-resort programmes). Since India instituted the Mahatma Gandhi National Rural Employment Guarantee Scheme in 2005, which entitles rural households to 100 days of employment per year, paid at the state-level minimum wage, compliance with the minimum wage has improved. Between 2004/05 and 2009/10, the number of waged workers earning less than the minimum fell from 73 million to 62 million. In the state of Maharashtra, which has had an employment guarantee programme since the 1970s, the proportion of workers paid below the



Source: Author's elaboration.

Figure 1.2 Net transfers and social goods affect market income

state-level minimum wage was much lower than the levels recorded for other states in India (Belsler and Rani, Chapter 5 of this volume).

Unemployment insurance is another institution that can affect market earnings. One of the policy goals of unemployment insurance is to allow displaced workers sufficient time for job search, so that they can find a job that better matches their skills, thereby reducing the likelihood or degree of a wage reduction (Chapter 10). Other social policies, such as employment subsidies can have the opposite effect by lowering market wages. In times of economic crisis some countries respond to rising unemployment by offering employment subsidies to employers to encourage hiring. Although a reasonable policy during times of slack demand and falling profits, permanent employment subsidies, either paid directly to employers, or to workers in the form of in-work benefits, can provide incentives to employers to underpay their workers, thereby lowering market earnings.

Finally, a large determinant of wage setting is the relative tightness of the labour market. An explicit government commitment to full employment that relies on aggregate demand management to relieve slack in the labour market is likely to influence wages. Given the importance of the macroeconomic setting on workers' welfare, the next section discusses how full employment policies contribute to greater equity and thus of the need to direct macroeconomic policy towards this goal.

1.5 MACROECONOMIC POLICIES AND FULL EMPLOYMENT

The promotion of full, productive and freely chosen employment is a central tenet of the ILO, enshrined in its 1944 Declaration of Philadelphia, which states that nations should '[further] programmes to achieve full employment and [raise] standards of living'. Two decades later, the International Labour Conference approved the Employment Policy Convention, 1964 (No. 122), which obliged ILO member States that ratified the convention to 'declare and pursue, as a major goal, an active policy designed to promote full, productive and freely chosen employment'. The policy should aim to ensure that 'there is work for all who are available for and seeking work' that the work is 'as productive as possible' and that it is freely chosen. In 2008, Convention No. 122 along with three other conventions¹² were designated by the ILO's Governing Body as 'priority instruments', given their significance for labour market governance. By designating the convention as a priority instrument, the ILO sought to encourage ratification and thus, compliance, by its member states; by 2014, 108 of the ILO's 185 member States had ratified the convention.¹³

Full employment policies are cornerstones for ensuring equitable societies. Persons who are unable to find waged work or promising opportunities for self-employment will suffer want unless they have income from other sources, be it income-bearing assets, family or social networks, or transfers from the government. Yet even with private or public transfers, there is an income loss to the individual and the household, as well as a loss to society by not benefiting from that person's productive potential.

Moreover, the incidence of unemployment among workers differs, with less-educated, poorer workers having a greater probability of experiencing unemployment when compared with the well off and more highly educated workers. This is particularly true in industrialized countries, where unemployment rates are two to three times higher for lower-educated workers, but also higher for women and other minority groups. (In developing countries, it is the more educated who experience higher unemployment rates, as the less educated typically turn to self-employment in the informal economy, and thus do not show up in unemployment statistics.)¹⁴ Thus, the policy to raise interest rates to contain inflation when unemployment drops below a certain level (the so-called NAIRU, non-accelerating inflation rate of unemployment), is particularly harmful to specific groups in the labour market. For this reason, policies directed at reducing unemployment are beneficial for reducing overall income inequality as well as inequality among groups. Indeed, in a recent analysis of 24 OECD countries, the OECD finds that a one percentage point increase in the share of employment reduces the overall Gini coefficient of the working-age population by 0.65 percentage points (OECD, 2011).

Unemployment, in addition to hurting individuals who cannot find work, can also have a dampening effect on the wages of those who remain employed, as both individual and collective bargaining positions are weakened. The extensive literature on the wage curve (Blanchflower and Oswald, 1995) documents the responsiveness of pay to shifts in the level of unemployment, with findings for most countries that a doubling of unemployment leads to a real wage drop of between 7 to 9 per cent. Figures vary slightly among countries depending on the strength of certain labour market institutions, particularly employment protection legislation. If a worker is not concerned about unemployment because there are employment protection laws that limit a firm's ability to dismiss a particular worker, then the worker will be in a better negotiating position and wage levels may not fall as sharply. Thus, the more flexible the labour market, the more susceptible is workers' pay to changes in the level of unemployment, potentially affecting the distribution of wages in an economy. The relationship between unemployment and falling wages is also due to the decline in hours that occurs during downturns in the business cycle. Thus,

even if workers are able to retain their hourly wage rate, the reduction of hours worked during periods of lax demand can contribute to declining overall and average wages (Galbraith, 2012).

Unemployment can also be detrimental to the sustainability of welfare states. It is for this reason that countries that have pursued universal social policies, such as the Nordic countries, have made increasing employment rates, particularly among women, a cornerstone of their economic and social development strategies (Esping-Andersen, 1990). These countries recognize that unemployment puts pressure on the fiscal resources needed to sustain the programmes, but also on societies' willingness to support transfer policies. By assuming responsibility for the welfare of children and the elderly, the Scandinavian countries are able to encourage greater labour force participation of women who, less burdened by care responsibilities, can more easily enter the labour market.¹⁵ Moreover, the many public services offered provide numerous decent employment opportunities, and the high quality of these services ensures support from society as a whole.

Instituting policies that allow people to work is one important piece of the puzzle, but these policies must also be complemented by policies to sustain and boost aggregate demand.¹⁶ Achieving full employment requires supportive monetary and fiscal policies that can stabilize the business cycle and ensure productive investments that create jobs. In most countries in the world, there are fewer jobs than there are workers who would like, or who need, to work – full employment is not the natural outcome of market forces. But unfortunately, over the past several decades, job creation has fallen off the macroeconomic policy agenda. Price stability has been the sole policy goal of monetary policy, as attested to by the large number of central banks that have adopted inflation targeting as their sole mandate (Epstein, 2007). While controlling inflation is important, it should not come at the expense of unemployment and underemployment; rather it should be considered alongside policies to boost investment and job creation (Islam and Kucera, 2014).

In Chapter 3 of this volume, Islam and Hengge argue for the need to revive the 'full employment compact' that held sway during the golden age of capitalism. To do so, countries in the developed world will need macroeconomic policies that emphasize both price stability and an employment objective, whereas low- and middle-income country governments 'need to act as guardians of stability as well as agents of inclusive development' (p. 66). Achieving these objectives will require an array of both monetary and fiscal policies.

As the authors explain, too often interest rates have been set high to stave off inflation, and in the case of many developing countries, to attract foreign investment in order to roll over liabilities. As a result, credit for

domestic investment is not only squeezed, but is also too expensive. It is thus not surprising that firms in low- and middle-income countries often report access to finance as a major constraint to their businesses (Islam and Hengge, Chapter 3). But these problems can be overcome by having central banks or national development banks use policy tools that promote lending to key economic sectors for employment creation and growth (Epstein, 2007).

Also important is the need to institute fiscal policies that boost aggregate demand, particularly during downturns, but which also provide funds for public investment in both physical and social infrastructure. Unfortunately, in many developing countries, tax-to-GDP ratios are low (in some cases around 10 per cent of GDP) limiting the ability of governments to invest in infrastructure that is fundamental for economic development, as well as important sources of employment creation (Chapter 3). Low tax revenues also limit the ability of governments to invest in public services, with implications for the quality of the labour force and workers' ability to access the labour market (Chapter 11), but also on the amount of redistribution that is possible (Chapter 8). Moreover, fiscal policy is not only limited in many developing countries (and some developed countries as well), but has tended to be pro-cyclical, augmenting boom-and-bust cycles and further harming the labour market.

Managing financial flows is also necessary for ensuring that finance is directed at productive investments, but also for avoiding financial crises, which plagued the developing world in the 1990s and ushered in the Great Recession in 2008. Indeed, a disturbing trend over the past several decades has been the growing 'financialization' of many economies. Epstein (2006) defines 'financialization' as the increasing importance of financial markets, financial motives and financial actors in the operations of the economy; Freeman (2011) refers to it as the '800-pound gorilla'. It is clear that in the case of the United States, the rise in finance – both in the power of its actors and in the importance of finance in the domestic economy – was the result of financial deregulation in the 1980s and 1990s that permitted the development of large and powerful financial institutions. The influence of these institutions, coupled with an ideological belief in efficient markets by economists and policy-makers alike, permitted the blocking of regulation of the derivatives market and the development of a shadow banking system, further increasing the size and the degree of pooled risk of the large financial institutions. The deregulatory stance was also a feature of the Federal Reserve, which lowered bank reserve requirements and refused to use regulatory tools such as stock margin requirements or credit controls to temper the growth of risky financial practices (Palley, 2012).

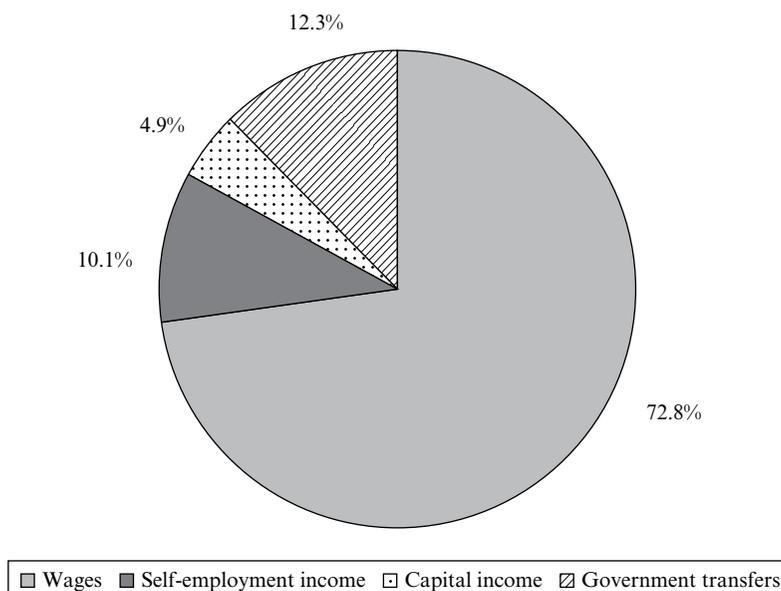
Financialization was also supported by the rise of 'shareholder

capitalism', which shifted company strategies toward focusing on the value of their share price, in order to increase the market value of the firm and subordinate management exclusively to the interests of owners. Management came to be rewarded with share options and bonus payments based on profits, thereby fuelling a business model of short-run 'profits without investment' (Dullien et al., 2011). Flexibilization of labour practices, including outsourcing, helped to cut costs and boost profits, but weakened the employment relationship, ultimately hurting labour (Weil, 2014). These practices were not disconnected from developments in financial markets since the deregulatory reforms spawned a mutual fund industry that sought ever-increasing returns on its investments and pressured firms to pay dividends.

The result of these interconnected forces is manifest in the declining wage shares and the growth of the income of the top 1 per cent, as well as the growing divergence between labour productivity and wage growth, as discussed earlier in the chapter. These trends have had feedback effects on economic growth as falling labour shares negatively affect private consumption (ILO, 2013a).¹⁷ The determination of wages goes beyond firm-level negotiations between a worker and his or her employer; macro- and mesoeconomic structures play a determining role. Moreover, both the personal and the functional distribution will determine the course of economic growth. Nevertheless, it is not possible to isolate specific causes for why wage shares have fallen in recent decades. This is probably because ultimately the causes are inter-related: financialization, globalization, technological change and the weakening of labour institutions have all played off one another, contributing to declining wage shares. And just as financialization has affected management practices that have weakened labour, what is needed are supportive labour institutions that can allow labour to be a countervailing force (Freeman, 2011).

1.6 INCOME FROM WORK

An individual's well-being is, for the most part, dependent on the income that the individual and the individual's family earns from work. As discussed earlier in the chapter, the labour market and how workers fare from the market is not simply the result of market forces, but depends on the myriad of institutions that guide the labour market. Part II of this volume analyses some of the labour institutions that determine earnings, including unions and collective bargaining (Chapter 4), minimum wages (Chapter 5), and the different forms of contractual engagement in the labour market (temporary contracts, Chapter 6; part-time work, Chapter 7).



Note: Data are standardized by applying average tax rate of the 30 OECD countries for which information is available.

Source: OECD (2011).

Figure 1.3 Components of disposable income, working-age population, mid-2000s, OECD-30

Income from waged work and self-employment accounts for the vast majority of individual and family incomes across the world. According to the OECD (2011), based on data for 30 countries, 83 per cent of household disposable income amongst the working-age population is earnings from work, with 73 per cent stemming from waged work and 10 per cent from self-employment. The remaining income sources include rents (4.9 per cent) and government transfers (12.3 per cent) (Figure 1.3). Among countries there is wide variation in income sources. In Chile, Italy and the Republic of Korea, self-employment income accounts for over one-quarter of income, with waged income playing a less important role. Similarly, government transfers are nearly negligible in Chile (0.81 per cent), low in the United States (4.9 per cent), but comprise 15–20 per cent of income in Continental Europe (Austria, 20 per cent; France, 18 per cent; Sweden, 15 per cent).

In countries where labour markets are less regulated, there is a wider

dispersion of labour market earnings. Collective bargaining and minimum wages are two institutions that directly affect workers' earnings, compressing the overall wage distribution by propping up wages at the bottom of the wage pyramid.

Chapter 4 of this volume by Susan Hayter addresses the role of unions and collective bargaining in reducing wage inequality. Unions' influence on wage distribution in an economy can come from their role as 'actors' representing labour in broader economic and social policy debates, but also as parties to collective bargaining agreements negotiated at either the firm or sectoral level. In her extensive review of the impact of collective bargaining on wages, Hayter distinguishes between collective bargaining systems that are narrow, or limited to the parties or bargaining unit, versus encompassing systems, in which collective bargaining agreements are extended to workers in the broader economic sector who are not members of the union. Under both systems there will be wage compression, but because narrow systems are limited to unionized firms the effect of the wage compression on broader wage inequality in the labour market will depend on the degree of unionization in the economy. Hayter gives data showing that trade union density has, in general, fallen in both developed and developing countries. As a result, the wage compression effects of the narrow systems have become even more limited. Under encompassing systems, collective bargaining agreements continue to be extended despite declines in trade union density, though movements from centralized to decentralized systems and opt-out clauses have eroded some coverage. Nevertheless, extension has allowed these systems to have a greater effect on compressing wages in the overall economy.

Hayter argues that debates on the equity versus efficiency of unions and collective bargaining has distracted attention from the decline in labour's share in the national income, the growing dispersion of personal incomes, as well as the overall decline in unionization. Moreover, her review shows that there is no systematic evidence to support the claim that unions help 'insiders' to the detriment of 'outsiders'. Rather, unions, as representatives of workers in larger social and economic debates, have played an important role in influencing policies to the benefit of workers, particularly those at the bottom of the pay scale. This is particularly true for tripartite negotiations on the minimum wage, working time, as well as public spending on social protection and social services. But the declining influence of labour has affected its ability to act as a countervailing force in many countries. The financial crisis of 2008, the Great Recession, the austerity measures being imposed in many parts of the world, and the deregulation of labour laws and collective bargaining in Europe in the 2010s, are manifestations of its weakening voice.

Chapter 5 of this volume by Patrick Belser and Uma Rani concerns the relationship between minimum wages and wage inequality. According to the ILO, approximately 90 per cent of countries have minimum wages though there is a wide diversity in the systems, including the wage-setting process, as well as in their scope, complexity and effectiveness, and their absolute and relative values (ILO, 2008). Minimum wages, by ensuring a minimum level of earnings for those at the bottom of the pay scale, are an effective tool for compressing the wage distribution as well as lessening the incidence of low pay in both developed and developing countries.¹⁸ In their chapter, Belser and Rani review the extensive empirical evidence of the effect of minimum wages on inequality and employment, supplementing discussion with their own empirical analysis of 11 developing countries. They find that even in developing countries where enforcement is lax, minimum wages help to reduce inequality. In most countries, this occurs at the bottom of the distribution (D5/D1), though in some countries where minimum wages are higher relative to average wages, the compression occurs in the middle of the distribution (D75/D25). They attribute the important wage compression impacts at the bottom of the distribution in part to 'lighthouse effects', whereby formal minimum wages provide a reference for bargaining among informal waged employees and their employers.

Despite the benefits of minimum wages on inequality, there has been considerable debate in the economics profession on its employment effects, specifically whether raising the minimum wage leads to job losses as the competitive labour market model suggests. Yet as Belser and Rani document in their chapter, there exists substantial empirical evidence to the contrary, demonstrating negligible effects on employment and sometimes positive effects as a result of encouraging workers to enter the labour market. Moreover, at the macroeconomic level, higher minimum wages can stimulate consumption and thus, aggregate demand. Here again, they complement the extensive literature review with their own analysis from five developing countries, and find no significant disemployment effects. Belser and Rani caution, however, that minimum wages must not be set at a level that is too high, as then it ceases to help the poorest workers and promotes non-compliance, nor at too low a level, which negates the effectiveness of this important policy tool.

The type of employment contract that a person works under affects the pay and working conditions of the worker, including his or her sense of job and income security. The decline of the standard employment relationship, witnessed by the rise in temporary employment contracts, dependent self-employment, temporary agency work, or other forms of subcontracted work, is just beginning to be understood.¹⁹ Moreover, in

many parts of the world, large parts of the labour force continue to work under informal employment contracts with scant protection by the law and access to social security. Two chapters in the volume address employment contracts: Chapter 6 on temporary contracts and wage inequality and Chapter 7 on part-time work. In both chapters it is clear that the type of contracts that exist in a country is an outcome of the regulations of the country. This implies that the law, if well designed and enforced, can be an effective tool for improving working conditions.

In Chapter 6 of this volume, Sandrine Cazes and Juan Ramón de Laiglesia document the increase over the past several decades in temporary contracts in both advanced and emerging economies, with temporary contracts becoming a notable feature of labour markets in Southern Europe, the Andean countries, and parts of Asia. In Europe, temporary contracts cover approximately 15 per cent of the labour force and in some countries, such as Spain, over one-quarter of the labour force is on temporary contracts. Temporary contracts entail significant wage penalties for the individual workers. Moreover, in countries with high shares of these contracts, there are low transitions between fixed-term and indefinite contract jobs, with the risk that workers become trapped in these jobs. As the authors argue, this is problematic not just for the individual, but for the labour market as a whole, as it leads to segmented labour markets and inhibits investments in training that are important for improving productivity. Moreover, workers employed under temporary contracts are often excluded from legislated benefits, and in some cases, are not covered by collective agreements.

In Chapter 7, Jon Messenger and Nikhil Ray tackle the issue of part-time work and inequality. Whether part-time work will be a source of inequality will depend largely on how it is regulated in national labour markets. In countries where the laws reflect the principle of equal treatment of part-time workers, wages and benefits will be on a pro-rata basis. Moreover, some countries grant employees the right to switch into and out of part-time work, mitigating the risk of the job becoming a career trap. Under these conditions, part-time work can be an attractive option for workers who need to reconcile work with care responsibilities or schooling, as these workers may otherwise not have participated in the labour market. However, in other countries, unregulated part-time work is sometimes a strategy on the part of employers to evade paying social security contributions, health insurance, or paid leave, resulting in lower earnings and poorer job quality. Many of these jobs also suffer from unpredictability in work schedules, hindering the principal positive attribute of part-time work. Part-time work can also be associated with less investment in training, adding to the potential scarring effects of part-time work on

career development. In developing countries, part-time work is also commonly found among informal, self-employed workers, at times reflecting a strategy for reconciling domestic responsibilities with work, but also reflecting insufficient opportunities for work.

1.7 THE REDISTRIBUTION OF INCOME

Market income constitutes the bulk of income for persons of working age, but there are times in life when we are either not of working age or are not employed. Societies have to find a way to smooth income across the different stages of life as well as prepare for possible contingencies that may arise. Redistributive social policies are the principal means that governments have to alter the distribution of income. However, the reasons for, and commitment to redistribution vary widely across countries, as does the degree of redistribution. Part III of this volume addresses redistributive social policies and their effect on inequality.

In Chapter 8, Malte Luebker analyses how redistributive policies, in the form of taxes and transfers, can reduce overall income inequality in a society. He reviews some of the problems with measuring redistribution and presents findings on trends and cross-country differences in redistribution. Luebker cautions that fiscal redistribution measures are a 'snapshot' that cannot account for the contributions of some policies, particularly the provision of public goods. Moreover, as discussed previously, there are important interaction effects from social policies, such that the 'design of welfare states will affect market inequalities', by, for example, affecting decisions to participate in the labour market (Esping-Andersen and Myles, 2009, p. 640).

Nevertheless, there are notable differences between countries, indicating divergence in the commitment and political will to build just societies. According to Luebker's calculations, in Latin America and East Asia, taxes and transfers have little impact on reducing the Gini coefficient (a reduction of a mere 0.02 percentage points), indicating how this is an underdeveloped policy tool. Comparing Europe with Australia, Canada, Israel and the United States, both groups' initial levels of inequality were about the same, but transfers in Europe had twice the impact as in the other four countries. In Australia, Canada, Israel and the United States, tax policy had a more significant effect in reducing inequality, but as redistributive policies were less important, the final level of inequality was nearly 25 per cent higher than in Continental Europe.

Tax policy is a critical component of fiscal redistribution. In developing countries, tax systems are less developed and tax revenues as a percentage

of GDP are usually much lower than in industrialized countries, ranging from 18 per cent in Thailand, 12 per cent in Bangladesh, 15 per cent in Peru and 13 per cent in Dominican Republic. The low tax base explains, in part, the limited redistributive impact in Latin America and East Asia. Amongst industrialized countries, tax revenues as a percentage of GDP are higher, but there is also much variation, ranging from 25 per cent in the USA and the Republic of Korea, to 36 per cent in Germany. With lower tax bases, there is less scope to use taxes as a means to redistribute incomes and less money available for investment in public goods that are needed for social and economic development. Moreover, the design of tax policy – whether it is progressive or regressive – will affect the ability of taxes to alter the distribution of income.

Indeed, the design of tax policy, as well as transfer policy, is an important distinguishing element among countries. Luebker shows, for example, that the amount of money spent, as a percentage of national income, on the welfare state only accounts for one-third of the overall variation in redistribution – the rest is due to the design of tax and transfer systems. The chapters that follow in Part III discuss different social policies, how they are characteristic of specific welfare state models as well as the degree to which they attenuate inequality in income as well as among groups.

Pensions are long-term social security benefits that are paid over prolonged periods in situations of old age, disability and loss of breadwinner. They are the most important redistributive policy, in some countries accounting for up to 80 per cent of total transfers. Their budgetary importance varies among countries, however, depending on the share of elderly in the population, but also the design of the social security system, particularly the availability and importance given to other transfers such as social assistance. In Chapter 9, Christina Behrendt and John Woodall analyse how the design of pension and other social security income transfer systems affects overall income inequality in a country as well as inequality between groups, namely the elderly and those of working age, and women and men. Pension coverage varies across regions of the world, with 90 per cent of older persons in Europe receiving a pension compared with 75 per cent in North America, 50 per cent in Latin America and the Caribbean, 25–30 per cent in Asia and the Pacific, the Middle East and North Africa and only 15 per cent in Sub-Saharan Africa. These differences largely reflect the percentage of formal waged employment in the particular countries, thus countries with large informal economies generally have lower pension coverage of the elderly, unless non-contributory pensions form part of the system.

As Behrendt and Woodall explain, how redistributive a pension system

is will depend on its design, including the mix between public and private pensions, whether there are non-contributory elements of protection, and if there are minimum pension guarantees for those who are unable to build up sufficient entitlements. Contributory pensions tie coverage and benefit levels to employment and as a result often perpetuate inequalities in the labour market. This is particularly true for women, who as a result of shorter work histories, make fewer contributions and ultimately receive lower benefits. But the same could be argued for all workers who have more erratic work histories, thus the growing share of workers in temporary contracts, as discussed in Chapter 6, may have important impacts on future pension coverage. Non-contributory pensions can compensate shortfalls in contribution by providing coverage to those who normally would not qualify for benefits and, indeed, women are the principal recipients of non-contributory pensions. But these pensions are often means-tested and benefits tend to be low.

Like many contributory pension systems, unemployment insurance can perpetuate existing inequalities in the labour market, as workers with stronger labour force attachment are the ones who benefit if displaced. In Chapter 10, Janine Berg analyses the different forms of income support for the unemployed and the poor and their contribution to mitigating inequality. She begins with an analysis of unemployment benefit schemes, noting how only 42 per cent of countries have schemes and amongst those countries that do, coverage rates are low, with only 61 per cent of the unemployed in high-income countries receiving benefits. She argues for the need to adapt unemployment insurance systems to changes in the world of work, including the rise of new forms of contractual arrangements as well as the increased participation of women in the labour market, some of whom have weaker labour force attachment, and thus may not qualify for benefits under existing systems.

Social assistance programmes are an important complement to unemployment benefit systems, as they can provide income to the long-term unemployed, but also to workers who do not earn enough to support themselves and their families. Countries differ, however, with respect to the importance that they assign to social assistance, as well as how social assistance programmes fit into the broader social protection system. In more universal welfare states, proportionally fewer resources are devoted to social assistance, given the wider range of programmes available, including family allowances. Developing countries have recently expanded social assistance programmes, which is a welcome development given their effectiveness at reducing poverty. But because of the low level of benefits, and the lack of other complementary social protection policies, the programmes are less likely to alter the distribution of income in a society.

The latest trend is conditional-cash-transfer programmes, which require families to attend to the educational and health needs of their children. While certainly laudable goals, the programme requirements can have the unintended consequence of excluding those who are most in need. It does, however, have the benefit of putting pressure on governments to provide health and education services for its citizens, a necessary social good that is fundamental to both human and economic development. Moreover, it represents an important step in filling a void in the existing social protection systems of many developing countries.

As discussed previously, public social services can have an important bearing on access to the labour market, particularly of women. The availability (or lack) of public social services also has a direct bearing on household incomes, as lower-income households who are forced to purchase these services of the market will pay a proportionally larger share of their income than higher-income households. Chapter 11 on public social services by Juliana Martínez Franzoni and Diego Sánchez-Ancochea analyses the relationship between the provision of public social services in the areas of healthcare, education, early childhood education and care (ECEC), and income inequality. The provision of high-quality public services in these areas is not only fundamental for breaking the inter-generational cycle of poverty by providing better opportunities for the next generation, but also in minimizing present inequality between different groups.

The authors cite data from the OECD that shows that public services increase disposable income more than transfers, with the greatest impact occurring in the Scandinavian countries. Indeed, the differences in income inequality between the USA and Sweden partly reflects the provision of care services; in Sweden these are provided publicly, compared with the USA where they are attained, for the most part, through private means. As the authors argue, public social services democratize access to services, allow families to re-allocate income to other needs, and release time from unpaid work.

When health, education and ECEC services are only provided through the market, the inequality of market incomes is propagated as lower-income families either cannot afford the health and care services, or spend disproportionate amounts of their income on these services when they do buy them, and attain services of inferior quality. Moreover, the lack of public care services affects women's ability to engage in paid work, and their more tenuous attachment to the labour market translates into lower earnings and benefits. An important conclusion to draw from this chapter, and which relates to the wider theme of this book on the interaction of institutions, is that market incorporation alone will not be a sufficient condition for reducing inequality; other policies, including

the provision of quality public services, but also broader social welfare policies, are needed.

1.8 DO LABOUR INSTITUTIONS HURT OR HELP VULNERABLE GROUPS?

As mentioned previously, the World Bank's *World Development Report 2013: Jobs* (World Bank, 2012) concluded that the effect of labour market institutions on employment performance was negligible. The report, however, went on to argue that most of the impact was redistributive, but 'generally to the advantage of middle-aged male workers (as opposed to owners of capital, women and younger workers)' (p. 26). In this conclusion, the World Bank is essentially putting forth the argument that labour market institutions benefit 'insiders' to the detriment of 'outsiders', who are typically women, youth and migrants. But this is ironic, given that women fare worse when the labour market is less regulated (Rubery, 2011), as do youth and migrants. For this reason, and because of the important relationship between group inequality and overall income inequality, this volume included a fourth part addressing the impact of labour market institutions on gender equality (Chapter 12), migrant workers (Chapter 13) and youth (Chapter 14).

In Chapter 12, Sarah Gammage explains how women generally have a more tenuous attachment to the labour market, due to the unequal distribution of care responsibilities within the household. Women are more likely to transit in and out of paid work as a result of these responsibilities and many women require more flexible forms of employment that allow them to better balance work and family life, if they are to engage in paid work. Moreover, there are greater fixed costs for women in entering the labour market as they may have to pay for those tasks that they are currently doing at the home. Labour market institutions can mediate women's entry into the labour force by providing public care services but also by legislating more flexible forms of employment.

Once in the labour market, women are more likely to work in feminized occupations, including informal or part-time work, with marked differences in wages, hours and access to benefits. Moreover, like other minority groups, they are more often found in low-waged work and in sectors that have lower collective bargaining coverage. As a result, minimum wages are sometimes the only policy tool available; by raising the wages of low-wage workers, they reduce gender wage gaps as well as overall wage inequality. Minimum wages can also correct for discriminatory practices that set differential wages for work of equal value.²⁰ Moreover, by raising wages at

the lower end of the income distribution, minimum wages may increase labour force participation rates of lower-income women who need to cover the fixed costs of going to work.

Collective bargaining is an important institution for compressing the wage distribution and improving working conditions and thus can help to improve gender and wage equality (Chapter 4). Gammage, while citing the important benefits of collective bargaining for compressing the wage distribution and lowering gender wage gaps cautions that women generally have lower union membership. She argues that gender concerns are often excluded in collective bargaining negotiations and thus, for the need to improve women's voice in unions and at the bargaining table.

Gammage concludes by arguing that labour market institutions have a significant role to play in fostering gender equality in the labour market, but that there is also a need for explicit policies to change the gender distribution of labour within the household, which is not immutable. She argues that the state has a role to play in actively encouraging men to take on more domestic responsibilities, particularly with regard to care duties, through parental benefit and leave policies, gender equity laws and non-discrimination laws. She argues that without addressing this fundamental inequality, there will be limits to what minimum wages, collective bargaining and other labour institutions can correct.

Chapter 13 by Christiane Kuptsch tackles the difficult issue of providing equal protection to low or semi-skilled migrant workers, some of whom have irregular status. Kuptsch reminds us that the eight fundamental conventions of the ILO on freedom of association and collective bargaining, freedom from discrimination and the elimination of forced and child labour apply to all workers, regardless of their status or location. She cites the example of Spain where trade union rights of illegal migrant workers were upheld on account of these conventions. Yet with few exceptions, it has been difficult to ensure the rights of migrants, making them vulnerable to exploitation. Low-skilled migrant workers tend to be employed in sectors that are often less protected, such as agriculture and domestic work. Moreover, some countries with sizeable migrant populations, such as the Gulf States, lack fundamental labour institutions that can guarantee protections for the workers. In some cases, countries overtly discriminate against migrant workers, by, for example, setting lower minimum wages for non-nationals, or tying migrants to particular employers, thus negating all possibility for bargaining and leaving the workers more exposed to abuse.

This chapter is interlinked with the chapters on public social services (Chapter 11) and gender (Chapter 12), as many low-skilled migrant workers form part of the international 'global care chain', whereby

families in destination countries hire migrant domestic workers to compensate for the lack of publicly available quality daycare – the so-called ‘pull for care’. Labour shortages in key occupations such as nursing have also led to important migrant flows, at times involving several countries. These examples serve to demonstrate the inter-connectedness, and thus responsibility, that national governments as well as the international community have in regulating and respecting the rights of migrant workers.

In Chapter 14, Gerhard Reinecke and Damian Grimshaw analyse the inequality between youth and adults as well as between youth, and assess how labour market institutions contribute to shaping the employment prospects and conditions of young workers. In some countries of the world, youth unemployment has reached alarming levels, raising concerns about the prospects of a lost generation (ILO, 2013b). The dramatic fears on one end of the debate contrast markedly with more dismissive positions that argue that the problems that youth face are transitional and will go away with age. As in most labour market debates, so much depends on where the worker – in this case the young worker – lives, and the labour market that the individual faces. Also, in countries where social mobility is constrained, the inequalities present in the young workers’ upbringing will likely manifest in their transition to the labour force and the conditions under which they work.

As the authors explain, in some countries, notably those with developed vocational training systems and regulated apprentice programmes, the transition from school to work is relatively seamless; in other countries, youth struggle to find a first job in their chosen field, or work in jobs with precarious conditions and few prospects. That youth earn less than adults is to be expected given their lack of experience; the concern, however, is whether youth get trapped in poor-quality jobs. Thus, an important policy question is who transits and what policies support the transition. In countries where a smaller proportion of the labour force is low wage (defined as earning less than two-thirds the median wage), there is greater probability of these jobs serving as stepping stones. This is the case in Denmark, for example, where many youth are employed in low-wage jobs, often in part-time positions, but the youth transit out of low wage over time (Esbjerg et al., 2008). This differs from other countries, such as the USA, where low-wage employment is a problem for the core workforce, particularly prime-age women. In these countries, youth employed in low-wage work are less likely to transit out (Gautie and Schmitt, 2010). This is partly due to the lack of collective bargaining in many low-wage sectors, which implies that if workers remain in the same firm, even though they are gaining experience, they are not likely to advance much in pay. In contrast, where unionization is stronger, less-educated workers

receive more training and rewards from experience, allowing them to advance further in pay scales.

The chapter surveys the literature on the impact of employment protection legislation on youth unemployment and concludes that the results are mixed, and when positive, are negligible – much like the general literature on the topic. Regarding youth minimum wages, the authors note that there is a policy divide on this topic, with many countries legislating specific wages for youth. The authors conclude that youth minimums are unlikely to be a panacea for employment problems, and that if instituted, countries should use wider age bands with smaller differentials, thereby lessening the problem of annual wage increases.

Many of the policies addressed in this book come to the fore in the discussion of youth. Policy debates on equality of opportunity and the use of conditional-cash-transfer programmes to upgrade educational levels, labour market transitions, the effect of wages, temporary contracts, and collective bargaining on working conditions, the inequalities that exist between groups and how they translate into overall earnings inequality, emerge from this discussion. The chapter reveals the complexity of the debate on labour market institutions, but also the importance of good policy design in improving the well-being of workers – both young and old.

1.9 CONCLUSION

The chapters in this volume make clear that ‘inequality is . . . a matter of political choice and institutional design’ (Luebker, Chapter 8, p. 236) and that the enactment and design of labour market institutions is a manifestation of a society’s commitment to greater equity. Thus, to be successful, countries must institute a wide range of policies that can support this objective. This book addresses the labour market institutions that are needed. It discusses the importance of having explicit macroeconomic policies to support full employment, of having well-designed institutions that govern work contracts, as well as the need for social policies and public social services that support the working and non-working alike.

While it may seem odd to have a discussion of macroeconomic policies in a book on labour market institutions, achieving full employment will only occur if there are explicit macroeconomic policies that support aggregate demand and job creation. Removing ‘rigidities’ in the labour market will not bring about full employment; it will only worsen workers’ well-being, increase inequality and insecurity, and promote industries that compete on cheap labour rather than technological innovation. Countries

must also regulate finance to ensure that investments are directed at productive activities that better societies and create jobs. Finance needs to return to being a means to fund these investments rather than being a source of its own profits.

Highly skilled workers have benefited from the rising share of capital of the past decades. Less skilled workers, however, have seen their wages and working conditions decline as unions have lost power, minimum wages have weakened and non-standard employment contracts have proliferated. The chapters in this volume provide evidence on how these labour market institutions, when designed well, can promote greater equality and support the earnings of those at the bottom of the pay scale and of more equitable societies in general.

Redistributive social policies, including public social services, improve workers' access to the labour market, remove workers from the labour market who should not be there (adolescents, the elderly), and help in wage bargaining by setting a reference wage. They can protect those who cannot work or are unable to find work as well as those who earn too little from work. Countries differ exceedingly on the resources that they collect as well as those that they dedicate to social policies. But even countries with similar budgets will have different outcomes in income distribution depending on the other policies discussed in the book as well as the design of their welfare states.

Women, migrants and youth face distinct hurdles in the labour market. Women's weaker labour force attachment emanates from the unequal distribution of care responsibilities. Migrants are either not protected, or are not aware of the protections that they may have in host countries; they are also in an even more unequal position vis-à-vis their employers. Youth have difficulty getting their foot in the doorway and risk getting stuck in precarious and low-wage jobs when labour markets are less regulated. The chapters discuss how labour market institutions can protect vulnerable groups in the labour market, calling into question the assumption that labour market regulations hurt these 'outsider' groups. Rather, what is needed are labour markets that are well-regulated, and policies that are designed, instituted and enforced to take into account the specific constraints that vulnerable groups face in the labour market.

There is a wide range of distributive and redistributive policies that countries can adopt if they want to build just societies. There is no one-size-fits-all model; rather, policies should be designed to reflect the economic, social and institutional characteristics of the country. Building just societies, however, requires an explicit commitment to this goal. It remains to be seen whether this commitment will be supported in the 21st century.

NOTES

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1. Belgium, Chile, France, Greece, Ireland, Portugal, Spain and Turkey. The deregulation of the labour market and austerity policies enacted during the Great Recession, with the stated goal of making unit labour costs competitive, have likely eroded the gains of the bottom quintile in Greece, Ireland, Portugal and Spain.
 2. Data is from the Standardized World Income Inequality Database (SWIID). Trends in income distribution are sensitive to the indicator used (Gini, Theil, decile comparisons), the unit of analysis and the data chosen. Thus, particular country trends may differ under alternative measures.
 3. Data from the Congressional Budget Office and cited in *Economic Report of the President* (2012).
 4. See Epstein (2007).
 5. See, for example, the World Bank 1995 *World Development Report: Workers in an Integrating World*.
 6. In countries where the political environment did not allow deregulation, there was still de facto flexibilization of the labour market, as a result of the scaling back of budgets on labour administration and inspection. For example, Mexico in the 1990s and 2000s.
 7. For a more recent evaluation of policies recommended under Article IV consultations, see Islam et al. (2012).
 8. See, for example, Manning (2003) and Fine (1998).
 9. See <http://www.doingbusiness.org/methodology/employing-workers> for a discussion of the changes made to the methodology; last accessed 24 August 2014.
 10. Lee and Gerecke (2013) refer to this problem as 'regulatory indeterminacy'.
 11. Many of the health and safety laws in the United States were enacted in response to the 1911 Triangle Shirtwaist Factory Fire in New York City, which caused the deaths of 146 garment workers.
 12. The other conventions concern labour inspection (the Labour Inspection Convention, 1947 (No. 81) and the Labour Inspection (Agriculture) Convention, 1969 (No. 129)) and the Tripartite Consultation (International Labour Standards) Convention, 1976 (No. 144).
 13. To read the full convention, see ILO Normlex at https://www.ilo.org/dyn/normlex/en/f?p=1000:11300:0::NO:11300:P11300_INSTRUMENT_ID:312267; last accessed 24 August 2014.
 14. In the Arab States, there are high rates of unemployment among tertiary-educated workers, particularly youth.
 15. Alva Myrdal explains the comprehensive set of policies that are needed to ensure family security and women's access to the labour market in a 1939 article in the *International Labour Review* (Myrdal [1939] 2013).
 16. Sweden, which pioneered policies to boost women's participation in the labour market, was also the first country to pursue Keynesian policies during the Great Depression. See Ohlin ([1963] 2013).
 17. Indeed, stagnating real wages and growing inequality are often advanced as an explanation of the current crisis, particularly in the USA. Households compensated for their falling incomes by increasing debt, which was sustained initially because of rising home prices, but which eventually collapsed when the bubble in the US housing market burst (see Stiglitz, 2010; Islam and Kucera, 2014).
 18. See the two special editions of the *International Labour Review* on low-pay work in industrialized countries (Vol. 148, No. 4) and emerging economies (Vol. 151, No. 3).
 19. For an in-depth discussion of the causes and implications of subcontracted work, see Weil (2014).
 20. Unfortunately, in some countries where minimum wages are set by occupation, the wage floors sometimes institute discriminatory policies by setting lower wages for jobs that are typically held by women.

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