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## **EMPLOYMENT GENERATION AS AN ECONOMIC STRATEGY FOR UNCERTAIN TIMES**

Any formulation of economic strategy for our times must rest on some increasingly evident current realities: periods of “rapid growth” have been based on unsustainable bubbles; such growth has contributed little in terms of generating more decent work and has significantly increased inequality; and popular sentiment is now against accepting these outcomes as reflected in the waves of protest in many different countries. This requires a completely different approach to macroeconomic policy making, which will be more compatible with the increasingly more vocally expressed aspirations and expectations of citizens.

### *Global uncertainties*

The global economy is now in uncharted waters. The two largest economic entities – the US and the European Union – are clearly in economic conditions that will prevent their being positive engines for global growth for some time. The continuing crisis in the eurozone is unfortunately unlikely to be quickly resolved with any of the proposals that are currently on the table. Meanwhile in the United States, there appears to be inadequate political appetite for the policies that would ensure a more sustained recovery. Expectations that China or developing Asia in general can become an alternative growth pole immediately to take up the slack are unwarranted, given the relative size of these economies and their continued export dependence on the US and the EU.

Two major misreadings of economic policy requirements have combined to intensify the ongoing global crisis. The first is the notion that the immediate concern is the reduction of public debt and reduction of fiscal deficits. In fact, worsening fiscal imbalances in most major economies were a *result* of the 2008 financial crisis, not a cause of it, as automatic stabilizers and fiscal stimulus packages came into play. In the developed world (including now troubled economies like Ireland and Spain) public bailouts accounted for a large part of the deficit, as private bad debts were taken into public hands. The median public debt to GDP ratio in developed countries almost doubled (to more than 60 per cent of GDP) between 2007 and 2010.

It is already evident that fiscal tightening in stressed economies is self-defeating. By reducing GDP growth and thereby fiscal revenues, it makes economic recovery more difficult and is counterproductive in terms of improving fiscal indicators. It is difficult if not impossible to reduce debt to GDP ratios in a period when the rate of interest on debt far exceeds the nominal growth rate. Further, the fact that surplus countries show no willingness to reduce surpluses or enlarge deficit bodes ill for global growth prospects. What will drive growth – globally and nationally - when countries (even those with external surpluses) persist in following austerity programmes that cut incomes and demand?

The second major misreading is an over-optimistic assessment of the self-correcting powers of financial markets. It has meant that thus far attempts to re-regulate of financial markets have been limited and halting. Financial deregulation led to a large, opaque and undercapitalized “shadow banking system”. It increased concentration in the traditional banking segment in a few “too big to fail” institutions and increased systemic risk. Post-crisis, governments’ lender-of-last-resort support to the financial system has even extended to the shadow banking system, creating massively increased moral hazard. Global commodity markets have also been affected by financial speculation, causing food and fuel prices to spiral with grave consequences for people across the world. This context makes strong re-regulation of finance urgent and essential. Controls have to be tighter on the “too-big-to-fail” institutions; cover the “shadow banking” institutions so to avoid regulatory arbitrage; and incorporate a macro-prudential dimension, with anti-cyclical capital requirements and capital controls. But re-regulation alone will not orient credit to real investment or make it accessible to small and medium-sized firms. So there must be restructuring of the financial system: giant institutions must be downsized; the activities of commercial and investment banking should be clearly separated, in order to reduce the risk of contagion; and the aim should be more diverse financial systems, with a bigger role for public and cooperative institutions. Commodity markets, which have been subject to wild price swings related to speculative and herd behaviour, need to be made more transparent, with controls on financial activity in these markets and direct intervention when required to curb price bubbles and prevent sharp declines.

#### *Limitations of the dominant economic strategy*

(The transition here from crisis to nature of pre-crisis growth is a bit abrupt) seems a bit abrupt)

However, it is not just the crisis that has emphasised the urgent need for a shift in economic strategy. The need for a major reconsideration of macroeconomic strategies is even evident in the experience of the previous boom and of the performance of “successful” economies. Recent economic growth has been associated with and even depended upon the

greater power of capital (both multinational and domestic), reflected in rising shares of profit and interest in national income. Governments have not seen higher wages, more employment and better conditions as economic policy priorities, but rather as eventual by-products of the growth process. Unfortunately, in many economies, income growth has not necessarily been accompanied by more decent work. Also, this profit-led growth is not sustainable beyond a point, as has become increasingly evident in the past few years.

The export-driven model of growth has come to be seen as the most successful strategy, driven by the success of China and Germany in particular. The model, sought to be emulated by almost all developing countries, was associated with suppressing wage costs and domestic consumption in the attempt to remain internationally competitive and increase shares of global markets. Managing exchange rates to remain competitive, despite either current account surpluses or capital inflows, was a central element of this strategy. This was associated with the peculiar situation of rising savings rates and falling investment rates in many developing countries, and to the holding of international reserves that were then sought to be placed in safe assets abroad. This is a classic dilemma of a mercantilist strategy: such economies are forced to finance the deficits of those countries that would buy their products, through capital flows that sustain the demand for their own exports, even when those countries have significantly higher per capita income than their own.

The strategy also generated fewer jobs than a more labour-intensive pattern based on expanding domestic demand would have done, which meant that employment increased relatively little despite often dramatic rises in aggregate output. This is why globally the previous boom was associated with the South subsidising the North: through cheaper exports of goods and services, through net capital flows from developing countries to the US in particular, through flows of cheap labour in the form of short-term migration. Despite the current fragile recovery, such a strategy is unsustainable beyond a point, especially when a number of relatively large economies seek to use it at the same time. This strategy bred and increased global inequality, and also sowed the seeds of its own destruction for both external and internal reasons. Externally, deficit countries will either choose or be forced to reduce their deficits through various means, including protectionist responses. Internally, suppression of wage incomes and domestic consumption will meet with political resistance.

In either case, the pressures to find more sustainable sources of economic growth, particularly through domestic demand and wage-led alternatives, are likely to increase. So countries must diversify their sources of growth, looking for other export markets as well as for internal engines of growth. This is what makes arguments for a shift in strategy towards domestic wage- and employment-led growth so compelling.

### *The current crisis as opportunity for change in economic strategy*

This is a historic opportunity to move away from the single-minded obsession with GDP growth delivered by large private corporate actors, towards feasible economic development trajectories that are more just and democratic. This is no doubt a challenging task, but it is now essential. The critical shift required is most of all in terms of orientation. It is important not to see the generation of decent work simply as a potential positive by-product of income growth, but as a *means* to sustainable growth, as well as an end in itself. This approach relies on strong positive multiplier effects to create virtuous cycles of employment and productivity growth. It allows for more stable economic growth that is based on expanding the domestic market, but it does not need to conflict with increasing exports. It encourages a greater emphasis on aggregate productivity growth (rather than only through cutting-edge new technologies), thereby generating a “high road” to industrialization from the bottom. Thus, a focus on generating more decent work can actually become a competitive advantage rather than allowing fear of global competition to generate a race to the bottom in labour standards.

In developed countries with relatively strong institutions that can affect the labour market, including collective wage bargaining, effective minimum wage legislation and the like, it is probably easier to think of wage-led growth and strategies to allow wages to keep pace (or at least grow to some extent) along with labour productivity growth. But what about most developing countries, where such institutions are relatively poorly developed and where many of not most workers are in informal activities, often self-employed? How are wage increases and better working conditions to be ensured in such cases? And what does a macroeconomic policy of wage-led growth entail in such a context?

In fact, such a strategy is also possible in economies with large informal sectors, through policies that increase the availability of consumer goods, basic services and various forms of social protection, and also improve the viability of small-scale production. Employment diversification, in terms of a long term sustained shift of workers away from low productivity (largely primary sector) activities to activities with higher productivity and value added, has long been seen as a central aspect of development. The growth of good quality wage employment in both the public and private sectors is central to the diversification process. In addition, the conditions of self-employment have to be improved, made less insecure and fragile and with excessive burdens of risk that are hard to bear for small producers.

There are several important elements of such a wage- and employment-led strategy in most developing countries. First of all, the focus of macroeconomic policies must be on the generation of decent work and on improving conditions of life, **not** on income growth

*per se*. This is important because it makes the provision of basic needs (employment as well as access to food, sanitation, housing, health and education) and improving the quality of life of all citizens the central guiding principles. Quantitative GDP growth targets, that still tend to dominate the thinking of policy makers, are not simply distracting from these more important goals, but can even be counterproductive. For example, a chaotic, polluting and unpleasant system of privatised urban transport involving many private vehicles and over-congested roads actually generates more GDP than a safe, efficient, affordable and “green” system of public transport that reduces vehicular congestion and provides a pleasant living and working environment.

Second, it is necessary to ensure the greater viability of informal and small-scale production, through better access to institutional credit to farmers and other small producers (including through directed credit, subsidies etc.), greater integration into supply chains and marketing that improves their returns, focus on co-operative arrangements that can provide the benefits of scale economies to small producers and technology improvements that increase labour productivity in such activities. It is particularly important to be aware of the specific needs of women producers and workers in informal activities when designing policies. Such a strategy is critical for both agriculture and non-agriculture, and the revival of small holder cultivation is an essential aspect of this.

Third, the strategy must emphasise the expansion of and better delivery systems in the provision of public services, especially in nutrition, sanitation, health and education. This allows for improved material and social conditions and has positive employment effects directly and through the multiplier process. This in turn requires increases in public employment, which incidentally also sets the floors for wages and improves the bargaining power of workers. This often not recognised as a crucial element of a possible wage-led strategy, but it can be extremely significant, and can be used effectively even in export-oriented economies, as long as surpluses from industrialisation and exports can be mobilised to provide wage goods publicly. Indeed, this has been an important and unrecognised feature of successful Asian industrialisation from Japan to the East Asian NICs to (most recently) China. In these countries, the public provision of affordable and reasonably good quality housing, transport facilities, basic food, school education and basic health care all operated to improve the conditions of life of workers and (indirectly) therefore to reduce the money wages that individual employers need to pay workers. This not only reduced overall labour costs for private employers, but also provided greater flexibility for producers competing in external markets, since a significant part of fixed costs was effectively reduced. It also provided important multiplier effects that generated employment expansion in other activities.

Fourth, a related aspect is the need to provide much better social protection, with more funding, wider coverage and consolidation, more health spending and more robust

and extensive social insurance programmes including pensions and unemployment insurance. This is important in itself, particularly for reducing human insecurity and gender gaps in living conditions. It also has great macroeconomic significance because it increases the presence of countercyclical buffers that reduce the negative effects of periods of economic downswing.

Obviously, such a strategy requires overall a significant increase in government spending, which seems to be almost an unrealistic demand in the current global economic context. The usual concern is that of finding the resources for it. In a context in which fiscal deficits are seen as anathema, increasing public expenditure appears to be an idealistic and impractical proposal. There are two reasons why this is not true. The first reason is that the multiplier effects of public expenditure in economies with significant unemployment and excess capacity involve increases in income and therefore also public revenues, which means that the increases in spending will not be matched by equivalent increases in deficit. The second reason (that tax revenues raised from the rich can pay for this increased spending) is potentially even more significant in the current socio-political climate, because it provides an opportunity to redress the dramatically increasing inequality in assets and incomes that has come to dominate the global economy. It is increasingly evident that across the world there have to be conscious attempts to reduce economic inequalities, both between countries and within countries. We have clearly crossed the limits of what is “acceptable” inequality in most societies, and future policies will have to reverse this trend. Paradoxically, the extreme inequality that is now evident actually makes it potentially easier to raise resources through taxation, by imposing reasonable taxes on “the 1 per cent” of the population that is now increasingly the target of the public protests by “the 99 per cent”. Far from disrupting economic activity, as is threatened whenever such taxes are talked of, the use of such revenues in the directions mentioned here is more likely to generate more broad-based and sustainable economic expansion and improved quality of life overall.

Finally, such increased public spending must also be associated with some additional critical features. Greater state involvement must be associated with efforts to make such involvement more democratic and accountable to the people, especially those who have been marginalised or dislocated by the economic growth process. Also, it is not enough to talk about “cleaner, greener technologies” to produce goods that are based on older and increasingly unviable patterns of consumption. Instead, we need to think creatively about such consumption itself, and work out which goods and services are more necessary and desirable for our societies.

