GLOBALISATION, EMPLOYMENT, WAGES AND CORE LABOUR STANDARDS

Opening Statement

by

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The OECD Convention which was signed in December 1960 commits the Organisation, among other objectives, to promote policies designed "to contribute to the expansion of World Trade on a multilateral, non-discriminatory basis in accordance with international obligations". Since then, the Organisation has prepared many analytical studies on the potential benefits of trade and investment liberalisation -- the most recent example being our 1998 publication, *Open Markets Matter*. At the same time, we have not neglected the potential costs of liberalisation and globalisation, notably in terms of the possible impacts on the labour market, in order to inform the public debate in as objective a way as possible.

The purpose of my opening statement today is to summarise some of the findings from recent OECD work with respect to the impacts of globalisation on labour markets. In particular, I would like to focus on the increased flows of trade and foreign direct investment (FDI) and their association with employment, wages and so-called "core" labour standards -- the latter being defined in line with the ILO's 1998 Declaration on Fundamental Principles and Rights at Work.

A. Evidence on the impacts of trade and FDI on wages and employment in OECD countries

One topic which has attracted much interest in recent years concerns the impact of trade with developing countries on trends in employment and wage inequality in OECD labour markets. There is a vast and growing literature on this topic, much of it focussed on the U.S. situation. The OECD has contributed to this debate by (a) undertaking some empirical analysis of its own -- see chapter 4 in the 1997 OECD *Employment Outlook* and the 1996 monograph by Bob Lawrence -- and (b) by commissioning a recent survey of the literature from a leading international expert, Professor Drusilla Brown [see Brown (2000)].

The results of our empirical research reported in OECD (1997) match the broad consensus in the literature found by Brown (2000), namely that the contribution of trade and FDI liberalisation to observed trends in employment and in wage inequality between skilled and unskilled workers in OECD countries is modest, and second-order compared with the impact of other factors such as skill-biased technical change or changes in labour market institutions and policies. For example, in the United Kingdom and the United States during the 1980s, the fall in relative trade prices of import-competing sectors would appear to explain less than 10 per cent of the widening earnings inequalities in both countries.[1]

This finding of small effects from trade with LDCs on employment and wages in OECD labour markets is not a surprising one for two main reasons.First, the OECD countries are shielded from trade competition with low-wage countries due to the structure of their economies. Almost 70 per cent of output and employment in the OECD countries, on average, originates from the service sector – which largely produces non-traded goods. Second, to the extent that OECD output is traded, the competition generally comes from other developed countries. Moreover, imports of manufactured goods from the developing countries during the 1990s amounted in value terms to less than 2 per cent of OECD countries' combined output.

The situation is similar with respect to foreign direct investment (FDI). Most FDI flows are between OECD countries (85 per cent of outflows and 65 per cent of inflows) and, globally, most FDI flows are to the service sector whose output is largely not traded. While FDI flows to developing countries have increased, particularly to China, the biggest share of flows remains within the OECD area.

B. Policies to foster workforce adjustment to globalisation

These conclusions and facts do not mean that the impacts of globalisation on OECD labour markets should be ignored. Certain sectors and groups of workers in OECD countries may be negatively impacted and forced to undergo painful adjustments. How should these displaced workers best be helped by policy?

One response to the risk of negative impacts on employment and wages from imports of goods from low-wage countries might be to protect industry and workers by raising trade barriers. However, such protection would entail a substantial cost to the economy and society by raising the prices of both imports and competing domestic products, restricting consumer choice and, in some cases, placing the heaviest burden on those in society who are least well off.[2] The answer to increasing competitive pressures is not protection that slows change by lessening the incentives for firms and workers to remain competitive and adaptable. Rather the answer is to foster greater workforce adjustment and for society to compensate the losers.

One might argue that this message is all very well during a period of full employment, but it is much harder to implement when countries are suffering high and persistent unemployment and workers and their families are much more fearful about their future job. Such fears are understandable, but there is no need for pessimism. High and persistent unemployment can be overcome in OECD countries if countries put in place a **comprehensive** package of reforms to tackle the problem and mobilise the political will to implement such a package. The OECD Jobs Strategy, which was launched by Ministers in 1994, sets out the necessary reforms in macroeconomic policies and a very wide range of structural areas covering labour and product markets. While it clearly takes quite a long time for the results to bear fruit, the evidence shows that the Jobs Strategy works.[3]

Labour market policies have an important role to play in the Jobs Strategy, notably in terms of helping to promote workforce adjustment to structural changes. Our research shows that it is important to secure the right balance between “passive” policies of income support for the unemployed (e.g. unemployment or early retirement benefits) and “active” policies aimed at getting them back to work (e.g. policies to foster job search, training, employment subsidies targeted at specific groups, in-work benefits). It is also important to increase the effectiveness of active policies[4]

C. Links between trade and core labour standards in OECD and non-OECD countries

The argument is sometimes made that globalisation is a channel for competitive pressures that may push down core labour standards, requiring policy to prevent a “race to the bottom”. In open, competitive markets in democratic societies, however, there are a number of checks and balances limiting this possibility.

As argued in Hirschman (1970), in competitive markets, employees experiencing declining conditions in a workplace may well use their leverage to bring about change or exercise their option to exit to competing employers. A firm that tries to gain competitive advantage by failing to uphold core labour standards risks problems in retaining high-quality workers -- particularly where labour markets are tight. The significant threat of losing such workers provides an incentive for employers to improve conditions because there are transaction costs to replacing experienced workers.

Moreover, in most modern market economies, democratic institutions have established basic enforcement mechanisms for minimum standards. These include corresponding laws, labour inspection agencies, and recourse for employees through courts or administrative procedures. In many countries, employers violating core standards risk fines or other sanctions.

There are indications of a virtuous circle, whereby countries that improve their respect for core labour standards tend to improve their trade and economic performance. Palley (1999) makes a similar argument when he noted that implementation of improved rights of freedom of association had a large statistically positive effect on country GDP growth rates in the subsequent five-year period. This point is reinforced by the OECD’s recent study on *International Trade and Core Labour Standards*, which found a positive association between respect for freedom of association and real per capita GDP, confirming a finding in an earlier OECD study from 1996. Moreover, our study found that most FDI flowed to countries with high labour standards, which may help to reinforce further this virtuous circle.

D. Selection, application and promotion of core labour standards

The ILO is the competent body to set and deal with core labour standards. International instruments such as the ILO's fundamental conventions and the 1998 ILO Declaration, play an important role in setting internationally-recognised norms for core labour standards. International recognition of core labour standards has greatly increased in recent years, a point highlighted by the growth in the ratifications of the ILO's fundamental conventions.

Nevertheless, there remains a continuing gap between the international recognition of core labour standards and their application in practice.[5] Efforts to close the gap between recognition and application of core labour standards increasingly focus on promotional mechanisms. A key recent development was the establishment of a follow-up mechanism under the 1998 ILO Declaration. This is complemented by a variety of bilateral and multilateral mechanisms, as well as private-sector initiatives such as voluntary codes of conduct.

The OECD has made a significant contribution in this regard through its Guidelines for Multinational Enterprises. The Guidelines are recommendations on responsible business conduct addressed by governments to multinational enterprises operating in, or from, the 33 countries that have agreed to adopt them (all OECD countries plus Argentina, Brazil and Chile). First published in 1976, they span the full range of activity by these enterprises. Their aim is to help multinational enterprises to operate in harmony with government policies and societal expectations.

Following more than one year of negotiations involving both government officials and representatives of business, labour and civil society organisations, a comprehensive review of the Guidelines was completed in June 2000. Existing chapters in the Guidelines on the environment, labour relations and general business policies were substantially revised and new chapters on combating bribery and protecting consumers were added.

The chapter on employment and industrial relations was revised to add references to all core labour standards including effective abolition of child labour and elimination of forced labour. New procedures to enhance the effectiveness of the implementation of the Guidelines were agreed upon, including guidance for the National Contact Points in promoting the Guidelines, handling enquiries and helping to resolve issues that arise. In sum, as noted in the OECD news release marking the event, the adoption of the revised Guidelines was "a significant step forward in the process of creating a consensual framework for a global economy".

E. Conclusion

A balanced mix of policies is needed to reinforce adaptive capacity in the face of all structural changes, including those stemming from globalisation. Labour market and social protection policies can be oriented to ensure that those who lose their jobs as a result of trade or investment liberalisation are insured against excessive income loss and assisted during the period of search for a new job. There is no inevitable connection between increased openness and less social protection.

Concerns about core labour standards do not call into question the fundamentals of trade and investment liberalisation. Rather, the issue is one of finding the most effective way to ensure implementation of those standards. OECD studies have concluded that low standards are not generally a significant competitive factor in trade with the countries concerned; and there tends to be a positive association over time between sustained trade liberalisation and improvements in core labour standards. At the same time, OECD work has found that concerns expressed by certain developing countries that core standards would negatively affect their economic performance also are unfounded. Indeed, it is possible that the observance of core standards would strengthen the long-term economic performance of all countries.[6]

Notes

1 . Similar orders of magnitude for the impact of trade on wage inequality are reported in Lawrence (1996) and Cline (1997)..

2 Nor is it obvious that labour would benefit greatly from increased protection. Cline (1997) found that, if trade liberalisation were halted at 1993 levels, wages of skilled workers in the United States would decline by an estimated 2 to 5 per cent by the year 2013, compared with what they would be otherwise; wages of unskilled workers would remain unchanged. If industrial countries imposed a 30 per cent tariff on all goods imported from developing countries, the results would be even worse: wages for unskilled workers would fall 1 per cent because of higher import costs, and wages for skilled workers would drop 5 per cent. The wage gap would narrow, but only because *everybody* would get poorer.

3 See OECD (1999) for an extensive review of the evidence concerning the implementation of the OECD Jobs Strategy over the second half of the 1990s.

4 See Martin (2000) for a review of the evidence on what works among active labour market policies.

5 . OECD (2000) found little evidence of substantial progress overall in reducing non-compliance with respect to freedom of association and the right to collective bargaining among a sample of 69 countries during the 1990s. This assessment was based on published observations of the ILO’s Committee of Experts on the Application of Conventions and Recommendations. It covered only countries that had ratified at least one of the two corresponding ILO fundamental conventions.

6. This argument is developed in Swinnerton (1997).

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