



FOR DEBATE AND GUIDANCE

FIRST ITEM ON THE AGENDA

Current prospects and policies for decent work: The challenge of multilateral cooperation and policy coherence for a fair globalization

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A. Introduction

1. At the beginning of 2008 prospects for the world economy are clouded by considerable uncertainty emanating from the still-spreading credit squeeze. This paper aims to describe briefly the factors influencing growth globally and in different regions of the world. It then reviews the impact of emerging trends on prospects for decent work, possible contributions the ILO might make to efforts to avoid a prolonged and widespread global downturn and the challenge of multilateral cooperation and policy coherence. It concludes by suggesting some issues for discussion.¹

B. Turmoil on financial markets impacts economic prospects for 2008

2. Financial turmoil began in July 2007 in the United States with growing worries about the effect on securities markets of rising defaults on sub-prime mortgages.² The International Monetary Fund (IMF) has since reduced its forecasts for global growth twice and now projects 4.1 per cent for 2008 compared with 4.9 per cent in 2007. All regions' growth forecasts were scaled back with the largest reductions in the United States and Europe. The IMF update also suggests that "the overall balance of risks to the global growth outlook is still tilted to the downside" and that the main risk "is that the ongoing turmoil in financial markets would further reduce domestic demand in the advanced economies and create more significant spillovers into emerging market and developing economies".³
3. In January 2008 the World Bank, using a different economic model, reported that global growth slowed modestly in 2007 to 3.6 per cent after a strong 3.9 per cent in 2006.⁴ Growth in developing economies was a robust 7.4 per cent in 2007 offsetting somewhat the slowdown in US domestic demand. During 2007, developing countries accounted for more than half the growth in world imports, contributing – along with the depreciation of the dollar – to strong net exports for the United States and a reduction in global imbalances. The Bank forecasts global growth in 2008 to moderate to 3.3 per cent picking up in 2009 as the US economy regains momentum. The Bank report however also noted serious downside risks to this soft landing for the global economy. "External demand for the products of developing countries could weaken much more sharply and commodity prices could decline if the faltering US housing market or further financial turmoil were to push the United States into a recession."

Origins and spread of the credit crunch

4. In the United States, house prices have fallen sharply following the onset of the sub-prime crisis. This has had a multiplier effect on financial markets as a result of the securitization

¹ The paper was finalized mid-February 2008.

² Sub-prime mortgages are a category of housing loans made to clients without a good or "prime" credit record. They have a high interest rate over the life of the loan but often have low payments for the first two years.

³ IMF: *World Economic Outlook*, Update, January 2008.

⁴ World Bank: *Global Economic Prospects*, 2008.

of mortgages and other loans into bonds. This is a technique in which financial institutions raise money by selling bonds backed by the income generated by loans. Banks packaged a large number of mortgages together, often including both sub-prime and less risky loans, as the collateral to back bonds. At the heart of this system are complex mathematical models that calculate the value of the bond from the mix of its component income streams and the risks to the underlying collateral, such as a house. The practice is known as “originate and distribute” and has been used across a wide range of credit markets. It was thought to represent a new and more sophisticated financing method that made the whole industry more efficient by spreading and thus reducing risk.

5. The crisis in the US sub-prime mortgage sector has led to a general re-evaluation of risks by financial institutions. Because of the layers of complexity – and lack of transparency of some of the financial arrangements involved – this reassessment takes time not least because selling the underlying asset quickly, such as a repossessed home, is likely to involve a substantial loss against the value assumed in the securitization process. A further complication is the growth of a very large bond insurance market known as credit default swaps which are contracts to buy a bond if it goes into default in return for a regular fee or premium. With the underlying value of securities uncertain, these instruments are also having to be revalued and are no longer easy to resell.
6. These difficulties have created a major credit squeeze with financial institutions writing down the value of the loans and bond insurance contracts they have made, trying to rebuild their reserves and unsure of the soundness of their counter parties in financial markets. The squeeze has included lending to banks on the overnight inter-bank market,⁵ to major commercial borrowers, consumers and some local and national governments. The margin or “spread” over official interest rates required of lenders deemed to be more risky has widened leaving many borrowers paying more for loans despite the fall in the Federal Reserve’s official rates.
7. Within the United States, financial turmoil has spread from the housing market where house prices and new residential construction have fallen steeply. Employment figures are down, as are retail sales and other monthly and quarterly indicators. A number of private forecasters are predicting national output to fall in the second and third quarters of 2008 which would qualify as a recession. The IMF forecast for the United States is for 0.8 per cent growth between the fourth quarter of 2007 and fourth quarter of 2008. However, the depth and length of a US slowdown or recession is uncertain, as is its spread to other countries.

Effect on the world economy

8. Financial markets are highly integrated and this channel is spreading the effects of the turbulence to other countries. Major European banks were active in the US housing market and thus hit by the sub-prime crisis and the domino effect of the credit squeeze. In addition, the “originate and distribute” technique of securitization is now widespread although sub-prime mortgages are not a feature of European or Japanese housing markets. Despite low official base rates, risk is highly priced. The cost of credit has thus increased and lending conditions tightened especially in the euro zone and the United Kingdom. These parallel developments have resulted in reductions in credit availability to firms and for housing and a dampening of growth prospects.

⁵ The inter-bank market is the market in which banks borrow or lend among themselves for fixed periods of time to accommodate short-term liquidity problems.

9. A further channel transmitting the slowdown is an expected fall in exports to the US market as a result of reduced demand and a further decline in the exchange rate of the dollar. The IMF forecasts a reduction in growth to around 1.5 per cent in both Europe and Japan in 2008 from 2.6 per cent and 1.9 per cent respectively in 2007.
10. Forecasters remain unsure as to whether developing countries' strong growth in 2006–07 will be maintained in 2008 or the industrial country slowdown will spread. The IMF's latest projections suggest that as a group developing country growth will fall below 7 per cent in 2008 from nearly 8 per cent in 2007.
11. The direct financial effect of the sub-prime crisis on emerging markets has so far been modest. A number of countries have built large foreign exchange reserves since the Asian financial crisis of 1997/98 and are no longer major borrowers. Indeed, through their sovereign wealth funds, a number of developing countries have helped big international banks rebuild their reserves.
12. Reduced demand in industrial countries will affect developing country exports and thus growth to some degree. The United States accounted for 16.5 per cent of world merchandise imports in 2005.⁶ The latest IMF projections for China are 10 per cent growth in 2008 down from over 11 per cent in 2007. Developing Asia as a whole is forecast to grow by 8.6 per cent down from 9.6 per cent. Africa's growth is expected to continue to improve to 7 per cent from 6 per cent while Latin America and the Caribbean developing countries are seen as losing over one percentage point of growth in 2008 at 4.3 per cent from 5.4 per cent in 2007. Hardly any change from 2007's 6 per cent growth is expected in the Middle East. The CIS and Eastern European countries are each forecast to have a drop-off in growth of over one percentage point from 2007 to 7 per cent and 4.6 per cent respectively in 2008.

C. Global economic imbalances

13. One of the reasons economic forecasters and finance markets are uncertain about the depth, length and spread of the slowdown is that the turmoil generated by the US sub-prime crisis may be a symptom of deeper underlying imbalances in the global economy. The United States has run a large current account deficit for several years together with a very low savings rate and a substantial fiscal deficit. For most countries this would not be sustainable. However, countries with current account surpluses have invested their currency reserves, largely held in dollars, in the United States in a variety of assets including government bonds as well as new high-yielding commercial securities. The United States thus maintained relatively low interest rates and a fast pace of growth. With the slowdown in the second half of 2007 and the weakening of the dollar, the US current account deficit has started to narrow.
14. The counterpart of these deficits are surpluses in other countries notably Japan, Germany, some oil exporters, and China. Concern about imbalances had led in 2006 to the IMF initiating multilateral consultations between the major countries to investigate the possibilities for mutually reinforcing policy adjustments to encourage a gradual

⁶ WTO: *World Trade Report*, 2007, p. 200, table 5.

rebalancing of the world economy and the avoidance of an abrupt loss of confidence in the dollar and the so-called “hard landing” of a US recession.⁷

15. The long period during which the global imbalances grew but were in effect balanced by flows of dollars back to the United States coincided with the rapid growth of new financial instruments. It may be recalled that in the third quarter of 2001 central banks injected considerable liquidity into the financial system to ward off a loss of confidence and an economic downturn after the bursting of the “dotcom” bubble and exacerbated by the terrorist attacks on the United States. This relaxation of monetary policy coupled with an expansion of securitization set off a period of easy credit especially in the United States which in turn engendered a boom in house prices and consumption. Much of the lending was in fact undertaken by institutions not subject to the usual prudential rules concerning reserves, including so-called off-balance sheet activities of major banks.
16. While asset prices, especially property, continued to rise, the reserves of the system nevertheless seemed adequate and were confirmed by rating agencies. However, with the bursting of the asset price bubble in one important segment of the market, other practices were exposed as risky and speculative. Despite huge write-offs, major investment banks are yet to complete the process of revaluing their assets and reconstructing adequate reserves. One analyst has estimated the possible losses to the financial system to be more than US\$1,000 billion.⁸ It is increasingly recognized that financial regulation has not kept pace with innovation and new stronger systems of supervision may be needed to restore confidence and avoid similar crises in the future. Discussions are under way between the governments and central banks of the main financial centres through the IMF, the Financial Stability Forum and the Bank for International Settlements (BIS).⁹
17. Since mid-2007 the fall in the dollar has accelerated. Its real effective exchange rate is now 30 per cent below its 2002 level, with a quarter of the depreciation occurring in 2007. While costlier imports and cheaper exports will help to reduce the US trade deficit, other countries’ dollar reserves are losing value. The euro and several other countries’ currencies have risen as the dollar has fallen with an opposite potential effect on imports and exports. Currency fluctuations are thus adding to uncertainty about economic prospects.
18. A further complicating factor is inflationary pressure mainly caused by rising prices of food, fuel and mineral commodities. Strong growth in demand including from China was not met by sufficient increases in supply. Indeed, for a number of commodities, higher production levels may be difficult to achieve. Record grain prices are placing a heavy

⁷ At its October 2007 meeting the International Monetary and Finance Committee included the following paragraph in its communiqué:

The Committee calls for sustained implementation of the policy plans reaffirmed at the Spring 2007 IMFC meeting by the participants in the multilateral consultation on global imbalances. It reiterates that an orderly unwinding of global imbalances, while sustaining global growth, is a shared responsibility involving: steps to boost national saving in the United States, including continued fiscal consolidation; further progress on growth-enhancing reforms in Europe; further structural reforms and fiscal consolidation in Japan; reforms to boost domestic demand in emerging Asia, together with greater exchange rate flexibility in a number of surplus countries; and increased spending consistent with absorptive capacity and macroeconomic stability in oil-producing countries.

See also “IMF sees global imbalances narrowing, but more to be done”, by Hamid Faruquee, IMF Research Department, 19 Feb. 2008.

⁸ Professor Nouriel Roubini cited by Martin Wolf in “America’s economy risks the mother of all meltdowns”, in *Financial Times*, 20 Feb. 2008.

⁹ See article in IMF Survey Online of January 2008 on “IMF intensifies work on sub-prime fallout”.

financial burden on developing countries, forcing a small decline in food consumption. The world's poor countries will have to pay 35 per cent more for their cereal imports – taking the total cost to a record US\$33.1 billion (€22.8 billion, £17 billion) – in the year to July 2008, even as their food purchases decline by 2 per cent. Food consumption per capita will suffer a slight drop. Higher production for biofuels is part of the reason for high prices of some agricultural products.¹⁰

D. Policy responses

19. The combination of upward pressure on prices, the threat of a slowdown in economic growth and serious concerns about the solidity of the financial system place monetary and fiscal policy-makers before several dilemmas. The usual response to higher inflation is to increase interest rates and reduce budget deficits while exactly the opposite is needed to counteract economic slowdown. Central banks are also the lenders of last resort, meaning that if important financial institutions risk collapsing and provoking a systemic crisis they are ready to offer easy loans to give them time to recover. However, central banks are also aware that the current financial instability may have had its origins in an earlier phase of monetary easing provoked by such concerns.
20. As the gravity of the financial crisis has gradually emerged, central banks have acted in concert to ensure that banks had access to enough liquidity to meet their obligations. In addition, the US Federal Reserve cut official interest rates by 1.25 percentage points in January 2008 as worries about the financial viability of some institutions increased and concern over a recession grew. Cutting official interest rates has the effect of raising the price of government bonds which form an important part of many banks' reserves. Other central banks have cut their rates although less sharply or, in the case of the European Central Bank, refrained from raising them.
21. Lower interest rates may however not be enough to stimulate a turnaround in the direction of the economy, as with falling demand businesses may not be ready to invest. Similarly, lower interest rates may make it easier for firms and households to scale back their debts but not necessarily encourage them to spend. Moving towards a more expansionary fiscal policy is therefore another option for governments. On 13 February 2008, President Bush signed an Economic Stimulus Act injecting US\$152 billion into the economy through tax cuts to households and businesses and increases in unemployment and veterans' benefits. This is equivalent to about 1 per cent of US GDP and would start to take effect in mid-year. The package was initially proposed in mid-January and passed rapidly through Congress with bipartisan support.
22. Few other countries have taken similar measures although the United Nations in its 2008 report on the World Economic Situation and Prospects argued that "A global demand stimulus will be needed if the slowdown in the United States economy is not to slip into a recession and spill over to the rest of the world."¹¹ The United Nations suggested amongst other things stepping up public spending on social security, health and education services, especially those geared to the rural population in countries like China and an end to monetary tightening in Europe and Japan. At the end of January the Managing Director of the IMF also argued that "The global downturn can be short-lived and ultimately moderate if leading countries of the world understand the need for a sensible and well-timed policy

¹⁰ FAO: *Crop prospects and food situation*, Rome, 13 Feb. 2008.

¹¹ United Nations: *World economic situation and prospects*, 2008, pp. viii–ix.

response. And what is good for one country – a responsible combination of monetary and fiscal policy – will also be good for the world economy.”¹²

23. At their 9 February 2008 meeting in Tokyo, G7 Finance Ministers decided not to follow this advice but noted that:

... downside risks still persist, which include further deterioration of the US residential housing markets; tighter credit conditions from prolonged difficulties in the financial markets; high oil and commodity prices; and heightened inflation expectations in some countries. Each of us has taken actions, appropriate to our domestic circumstances, in the areas of liquidity provision, monetary policy, and fiscal policy. We also remain committed to strengthening our efforts to enhance growth through necessary reforms. Going forward, we will continue to watch developments closely and will continue to take appropriate actions, individually and collectively, in order to secure stability and growth in our economies.¹³

24. Possible policy responses to the threat of a slowdown are likely to remain on the top of national and international agendas in the coming months. Given the increased importance of large developing countries in the world economy, the spring 2008 meetings of the International Monetary and Finance Committee and the Development Committee provide a further opportunity to discuss the sort of concerted action proposed by the IMF Managing Director and in the UN's 2008 World Economic Situation and Prospects report.

E. Prospects for employment and decent work

25. The current slowdown began in the United States and spread to other industrialized countries. In 2005, developed countries represented 74 per cent of world GDP and 78 per cent of world final consumption (valued at current exchange rates).¹⁴ However, they accounted for only 16 per cent of the total world employment of nearly 3 billion.¹⁵ An assessment of the global impact on jobs of a slowdown thus depends on the extent of its spread beyond the industrial countries. In 2007, global employment grew by about 45 million, mostly in the developing world. Weaker growth in 2008 would reduce this expansion and depending on the size of the reduction lead to a slowing of the pace of poverty reduction in the developing world where more than four out of ten workers live with their families on less than US\$2/day per person.¹⁶
26. The lessons for developing countries of previous crises are that informal employment tends to rise more than outright unemployment and that recovery is long and slow for the most

¹² *The case for a targeted fiscal boost: A commentary*, by Dominique Strauss-Kahn, Managing Director of the International Monetary Fund, in *Financial Times*, 30 Jan. 2008.

¹³ Statement of G7 Finance Ministers and Central Bank Governors.

¹⁴ World Bank: *World Development Indicators*, 2007. If Purchasing Power Parity (PPP) estimates are used to construct these comparisons developed countries' share of world output is lower. The International Comparison Programme (ICP) has recently published new estimates for PPPs which will require a major revision in a large number of sets of comparative statistics. The new estimates give developed countries a 59 per cent share in world output in 2005.

¹⁵ Employment shares are taken from *Changing patterns in the world of work*, ILO, 2006.

¹⁶ ILO: *Global Employment Trends*, 2008.

vulnerable workers.¹⁷ In addition, many developing countries are faced with a substantial increase in their working-age population as well as large-scale migration from rural to urban areas. For example, in 2004–05, 24 million women and men were seeking jobs in China’s urban areas. However, China’s GDP growth rate of 9.6 per cent in 2004–05, yielded only 10 million new jobs in cities, leaving a shortfall of 14 million. It is likely that they joined the unemployed or found relatively unproductive work with very low incomes in the growing informal economy.¹⁸

27. Industrialized countries’ unemployment rates declined in 2007 to an average of 5.6 per cent of the labour force, against 5.9 per cent in 2006.¹⁹ Nevertheless, this relatively good performance occurred against the background of 2.5 per cent growth rates. A dip in growth will most likely lead to an increase in unemployment rates in 2008.
28. In industrialized countries, wage growth was contained in 2007 although labour markets had been tight. In contrast, in China, urban wages were growing at an annual rate of 22 per cent in the third quarter of 2007, following high labour demand especially for skilled workers in the export sectors. Inflation at an annualized rate reached 6.5 per cent in this period. However, food prices have increased much more than other prices adversely affecting poorer households in particular.²⁰ Wages in other parts of Asia have increased for highly skilled specialists such as engineers and IT specialists. In the Russian Federation, where the unemployment rate fell below the historically low level of 6 per cent in 2007, wages increased in real terms by 8 per cent during that year.
29. The increase in average real wages masks differences between top, middle and lower wage earners. Most countries are seeing greater inequality in the distribution of income and earnings.²¹ Top wages have grown much faster than average or lower wages in many developing and industrialized countries, reflecting the strong demand for highly skilled workers and substantial increases in top managers’ remuneration. Redistributive fiscal policies have not improved these trends in most countries and in some cases have added to the widening gaps in pre-tax and benefit incomes.²² In a number of countries, efforts have been made in recent years to strengthen minimum wages to provide some protection to workers at the lowest end of the wage scale.²³
30. In addition, the labour share in OECD countries declined to 52 per cent by the end of the 1990s from 58 per cent of national income in the first half of the 1970s. Several factors are responsible for falling labour shares, which require more research to be fully understood,

¹⁷ For an overview of the link between financial openness, crises and employment in crisis-affected countries, see R. van der Hoeven and M. Lübker, 2006: “Financial openness and employment: The need for coherent international and national policies”, Working Paper No. 75, Policy Integration Department, ILO, Geneva, May 2006.

¹⁸ Z. Junfeng and M. Mahmood, 2007: “Employment, decent work and poverty reduction in urban China”, ILO.

¹⁹ OECD: *Employment Outlook 2007*.

²⁰ National Bureau of Statistics of China.

²¹ IMF: *World Economic Outlook*, 2007.

²² V.A. Mahler and D.K. Jesuit, 2006: “Fiscal Redistribution in the Developed Countries: New Insights from the Luxembourg Income Study”, in *Socio-Economic Review*, Vol. 4, pp. 483–511.

²³ GB.291/ESP/5. See also the overall review in Eyraud and Saget: *The fundamentals of minimum wage fixing* (Geneva, ILO, 2005).

and include the shift to a more capital-intensive production process, but also financial and trade openness and their weakening effect on the bargaining power of labour.²⁴

31. Both technological change and opening of markets to international competition may have led to skill shortages and a consequent bidding-up of the wages of scarce skilled workers. Although indicators of educational attainment such as literacy rates have progressed significantly, the supply of skilled workers may not be keeping pace with new demands or not be attuned to employers' needs.²⁵ In addition, high demand for skilled workers in urban areas of some developing countries has exacerbated gaps between rural and urban populations. Such skills-based inequalities are particularly striking in emerging countries divided between export-led high-growth areas and the rest of these countries.
32. The gender equity effects of these wage movements are mixed. On the one hand, increases in top wages mostly benefit male workers and reverse progress achieved in some countries in narrowing the gender gap as a result of higher female educational attainment and increased participation in the labour force. In Canada, for example, the gender earnings gap for full-time full-year university educated young adults (25–29) widened over the 1990s.²⁶ At the same time, the relative position of unskilled men has deteriorated in some Anglo-Saxon countries, where declining earnings of men without post-secondary education are reported due to low demand for unskilled labour and low minimum wages. In developing countries, the demand for highly skilled specialists also tends to benefit men more than women.
33. If developing countries as a group avoid a substantial slowdown in growth, most will still have the ability to achieve the Millennium Development Goal of halving extreme poverty by 2015. The percentage of the population living below US\$1/day reduced by ten percentage points in developing countries as a whole between 1990 and 2004.²⁷ However, the percentage of the population in sub-Saharan Africa living below US\$1/day only reduced to 41 per cent in 2004 from 48 per cent in 1990. This pace of reduction means that the region will not have cut poverty by half by 2015. Were growth to decline more steeply and the earnings of the working poor fall, those who have moved just above the poverty line may be vulnerable to slipping below the line once more.

F. Multilateral cooperation and policy coherence for decent work

34. Indicators of the scale, depth and spread of any slowdown are uncertain at the time of writing. More pessimistic forecasts may prove mistaken. Nevertheless, as the IMF has suggested, the balance of risks appears to be on the downside. Such an outcome would result in a changed economic and political context for the promotion of the Decent Work Agenda and a setback for efforts to shape a fair globalization.
35. President Zoellick of the World Bank has said that:

²⁴ M. Lübker: *Labour shares*, Policy Integration Department Technical Brief 01, ILO.

²⁵ Southern and Eastern Africa Consortium for Monitoring Educational Quality (SACMEQ, 2000); *Progress in international reading literacy study* (PIRLS, 2001).

²⁶ R. Morissette and G. Picot, 2005: "Low-paid work and economically vulnerable families over the last two decades", Analytical Studies Branch Research Paper Series 2005248, Statistics Canada.

²⁷ The recent revision of PPP estimates will alter these poverty share numbers both for the base and the latest year. New figures may be released later in 2008.

Globalization has brought uneven benefits to the billions in middle-income countries who have started to climb the ladder of development since the end of the cold war. In many lands, social tensions are weakening political cohesion. These middle-income countries need to continue to grow, to offer inclusive development, and to adopt environmental policies for sustainable prosperity. The greater influence of developing countries presents another question: what will their place be in this evolving global system? This is not only a question of how large developing countries will interact with developed countries, but also with the poorest and smaller States of the world.²⁸

- 36.** The process of globalization has created important economic channels between countries which can stimulate growth but also propagate recession. Developments in labour markets are both affected by developments in other markets and are also a factor influencing important drivers of growth such as consumption and saving. Furthermore, developments in developing countries, especially the largest, increasingly interact with those in the G7 and other industrialized countries. The capacity of the multilateral system of cooperation to facilitate the emergence of a coherent policy response to a possible global slowdown is an issue of central importance to the ILO and its multilateral partners.
- 37.** Indeed, if the financial turmoil is a symptom of a failure to address global imbalances, a durable recovery may require a much higher degree of international policy coherence than has been achieved in recent years. Policy initiatives within the framework of the Decent Work Agenda could be an important component element of such an international policy response.²⁹
- 38.** The relevance of the ILO's Decent Work Agenda was highlighted by G8 Heads of State and Government at the 2007 Summit in Heiligendamm who amongst other things stated that:

We are convinced that a globalization that is complemented with social progress will bring sustainable benefits to both industrial and developing countries. We recognize our responsibility for an active contribution towards this objective. Therefore, we support the International Labour Organization's (ILO) Decent Work Agenda with its four pillars of equal importance: the effective implementation of labour standards, especially the ILO core labour standards, the creation of more productive employment, further development of inclusive social protection systems and the support of social dialogue between the different stakeholders.³⁰

At a meeting called by Chancellor Merkel on 19 December 2007 the heads of the IMF, World Bank, WTO, OECD and ILO agreed to work together to follow up the far-reaching commitments made at the G8 Summit.

- 39.** As mentioned earlier, financial integration and innovation have developed at a very fast pace in recent years and, as the current crisis has revealed, a large number of institutions took on risks that collectively threaten the system as a whole. Greater financial integration has increased the volatility of international capital movements, resulting in more frequent financial and economic crises. Such financial crises do affect growth, income and

²⁸ Address to the National Press Club, Washington, DC, 10 October 2007.

²⁹ The UN Commission for Social Development adopted in February 2008 a comprehensive resolution on promoting full employment and decent work for all which highlights the interconnection between the ILO's Decent Work and the UN's International Development Agendas.

³⁰ "Growth and responsibility in the world economy", G8 Summit Declaration (7 June 2007, Heiligendamm), para. 22.

employment not only in the short term but also in the longer term.³¹ Financial turmoil has stimulated a renewed discussion of international rules concerning banking supervision and their interaction with monetary policy. As argued by the Deputy Managing Director of the IMF, Mr Takatoshi Kato, “Ongoing events in the financial markets call for greater integration of financial stability and price stability policies to enhance monetary policy effectiveness.”³²

40. Lower interest rates, a fiscal boost and a lower dollar counteract the slowdown in the US economy but underlying imbalances particularly between domestic savings and consumption, the government deficit and on the current account of the balance of payments may remain. The US economy may not resume the role of spender of last resort in the global economy.³³ This would also put into question reliance on exports as a key driver of growth in a number of developing countries. The extent to which surplus countries will continue to finance the US deficit is also under question, as returns to government bonds are low and the dollar weak.
41. Exports to the United States and other industrialized countries have been an important component of developing countries’ recent surge in growth. China and South-East Asia have gained an important position in manufactured goods trade and have also contributed to commodity exporters’ growth as a result of their high demand for fuel and raw materials.³⁴ While other factors have also contributed to the acceleration in developing countries’ growth, including policy reforms to stimulate domestic investment and competition, the effect of reduced export markets on overall economic performance is a cause of concern.
42. Looking to the short- to medium-term policies that might reduce and counteract the spillover effects on developing countries of a rebalancing of the US economy, an important role could be played by reducing dependence on exports as a driver of growth by stimulating domestic consumption and job-creating investment, especially in countries with the fiscal and foreign account space to do so. Such policies could also focus on the employment and social protection needs of lower income women and men who from a macroeconomic perspective have a high propensity to spend.
43. Developing social security systems with a wider coverage in developing countries tackles both social and economic imbalances that weaken the sustainability of development. Middle-income developing countries, in particular in Asia, have high saving rates, up to 25 per cent of GDP in some cases, in part as an answer to the lack of universal health and old-age insurance, as well as to cover the cost of education. Well-designed social security systems both give better overall protection and release income for consumption and thus domestic and global demand. Minimum wage fixing policies can also compensate for the

³¹ GB.294/WP/SDG/2(& Corr.).

³² “The nature and magnitude of financial innovation”, keynote address by Mr Takatoshi Kato, Deputy Managing Director of the International Monetary Fund at the Conference on Challenges for Monetary Policy from Financial Innovation and Globalization, IMF Offices in Europe, Paris, 29 January 2008.

³³ The phrase “spender of last resort” has been much used to describe the US economy but was coined in a note for the Levy Institute by Wynne Godley and Bill Martin in 1999 entitled: “How negative can US saving get?”

³⁴ The United States was the destination of 21.4 per cent of all China’s exports in 2005, against 8.5 per cent in 1990, according to the UNCTAD (2007) *Handbook of Statistics*, 2006.

weak bargaining position of the lowest paid workers and ensure that the benefits of growth are more equitably shared between workers and employers.

44. Side by side with measures to extend social protection, many countries could develop measures to promote an environment conducive to the creation and growth or transformation of enterprises on a sustainable basis combining the legitimate quest for profit – one of the key drivers of economic growth – with the need for development that respects human dignity, environmental sustainability and decent work. The ILO’s strategy for the promotion of sustainable enterprises developed and agreed at the 2007 International Labour Conference³⁵ could be used by many countries to help ensure that private investment, especially by smaller businesses, is at the heart of strategies to stave off recession and stimulate a quick rebound.
45. Investment in human resources development is also a key aspect of preparing economies for recovery and meeting the skill shortages which may be part of the imbalances that underlie the end of the upswing in many countries.
46. Infrastructure investment can be an important direct stimulus to employment. If the risks of a prolonged slowdown increase, such investment programmes should ideally be initiated early in the downswing to take effect when most needed. Since many countries are looking to renew their infrastructure as part of strategies to reduce greenhouse gas emissions, programmes focused on creating “green jobs”, which are economically and environmentally sustainable, could be part of policies designed to counteract a slowdown. Investment in building insulating has proved to be a valuable source of employment in the construction sector as well as making a significant contribution to energy saving.³⁶
47. Balanced growth within countries is an important part of a more stable international economic environment. At the international level, greater policy coherence between trade, aid, and financial policies is required to address global imbalances, as highlighted by the World Commission in its 2004 report and re-emphasized by many participants at the ILO Lisbon Forum on Decent Work for a Fair Globalization.³⁷ The ILO has facilitated the holding of a series of meetings between international organizations under its Policy Coherence Initiative which have discussed various aspects of the challenge.³⁸
48. Financial markets are the most integrated part of the global economy. The credit crunch in the United States and other industrial countries is having repercussions on businesses and jobs worldwide. In addition, the squeeze on borrowing is affecting investment and consumption and thus production both in the richer countries and, through the trade channel, developing countries. It is unclear as to how severe, long and widespread the credit squeeze will be and how much effect it will have on production and employment. Governments and central banks are watching developments closely and are aware that coordination is needed to ensure that national policy initiatives do not work at cross purposes. A number of formal and informal mechanisms for such multilateral cooperation are available to improve policy coherence. The ILO’s Decent Work Agenda offers both

³⁵ ILO: *The promotion of sustainable enterprises*, Report of the Committee on Sustainable Enterprises, International Labour Conference, 96th Session, Geneva, 2007.

³⁶ As reported in GB.300/WP/SDG/1, many such jobs have been created in Brazil, Germany and Spain.

³⁷ GB.301/WP/SDG/2.

³⁸ GB.298/WP/SDG/2. Subsequent to this report, two further meetings were held in 2007 with the World Bank, the IMF, UNDESA, UNDP, WTO and UNICEF and one with the OECD and IFAD.

policy tools that have heightened relevance in a period of slowing growth, such as those developed through the Global Employment Agenda,³⁹ and the mechanism of social dialogue based on international labour standards for developing consensus over priorities.

G. Issues for discussion

49. The Working Party may wish to discuss the implications of the prospects for the global economy in 2008 for the ILO's Decent Work Agenda and the scope for improved multilateral cooperation and policy coherence. Amongst the issues are:
- (1) What assessment do members of the Governing Body have of decent work prospects in their countries in the light of the forecasts of a slowdown in global growth?
 - (2) Given the possibility of a period of rebalancing and thus slower growth in industrial countries, what measures could developing countries consider to sustain progress on decent work and poverty reduction?
 - (3) How could any partnerships with other international agencies, for example the World Bank, enable the ILO to offer stronger support to developing countries' policies in areas such as sustainable enterprise, skill development, basic social protection and employment-intensive infrastructure?
 - (4) In reviewing international financial regulations, should the competent organizations be giving greater priority to encouraging investment in sustainable enterprises and productive employment?
 - (5) Should the ILO suggest to constituents that tripartite meetings be held nationally to review economic prospects and their implications for decent work with the outcomes communicated to the Governing Body?

Geneva, 5 March 2008.

Submitted for debate and guidance.

³⁹ GB.295/ESP/1/1.