SIX

Protecting Job Mobility and Workers' Rights

Gainful, productive employment is crucial to enhancing equity and income growth and to reducing poverty.[1] But its importance goes well beyond that, making employment a legitimate policy concern in its own right, not just a means to other ends. Productive employment is not only about income. It is also about human dignity and a place in society.

In Latin America jobs and the labor market were not part of the reform agenda of the 1990s, and little progress has been made in this area compared with others (see figure 6 in our Introduction). Surprisingly, neither jobs nor wages were part of the political discourse in the 1990s. Yet recent surveys of attitudes indicate that lack of jobs and low wages are the main concerns in the region—ahead of crime and other social problems (figure 6-1).[2] That is not surprising. Unemployment rose in the 1990s (figure 12 in the Introduction), and only 50 percent of workers are employed in the formal sector (table 6-1).

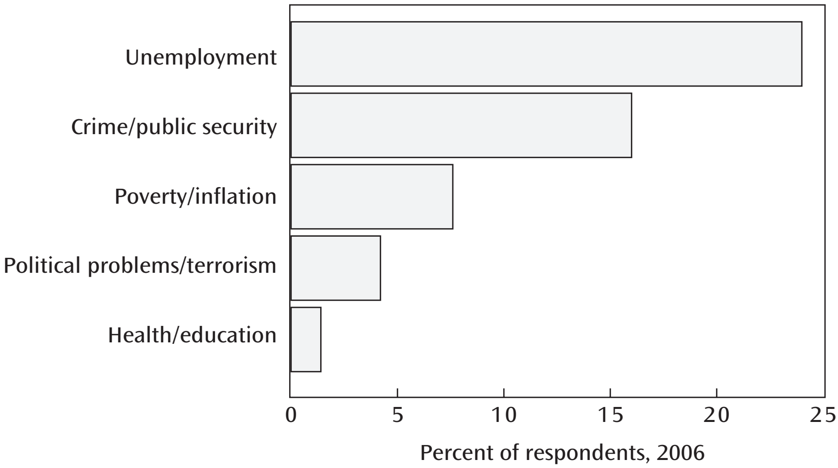
Labor markets in the region, though highly regulated (figure 6-2), fail to protect the great majority of workers.[3] Regulation focuses on job security

1. Krugman (1994) singles out productivity, employment, and income distribution as the three things that matter most in economics.

2. See also Latinobarómetro (2003, 2004, 2005).

3. The exceptions are Chile and, by some measures, Uruguay. Mandatory transfers to workers are low in Uruguay, but the total cost of labor regulations is still relatively high—well above that in Chile and most developed countries, mostly because of high payroll taxes (social security contributions) (Botero and others 2003; Heckman and Pagés 2004).

FIGURE 6-1. What do you consider to be your country's most important problem?



Source: Latinobarómetro (2006).

(for example, mandating certain forms of severance pay), not on rights of association or collective bargaining that would allow workers to negotiate directly with employers. Inflexible labor rules and practices discourage worker mobility and undermine the creation of productive employment in the formal sector.[4] Jobs and wage income are insecure—especially for the large majority of young, female, and unskilled workers. Training financed by employers benefits only the small percentage of workers who are more educated and skilled.[5] There is little or no public support during spells of

4. Labor rigidities became even more binding with the loss of real wage flexibility in the 1990s, as the policy crutch that inflation had (ironically) provided disappeared.

5. Surveys by the IDB and World Bank in 1999–2000 show that three of four Latin American firms provide training for workers, a percentage not that different from those in the United States and Canada. As in the United States and Canada, in Latin America more educated and skilled workers receive more training for longer periods. The difference is that the percentage of educated workers in the labor force is much higher in the United States and Canada, so a bigger share of the labor force ends up trained than in Latin America. Also, in Latin America a much smaller share of the workforce is employed in the kind of firms that provide training (IDB 2001; Duryea and Pagés 2002; World Bank 2006e).

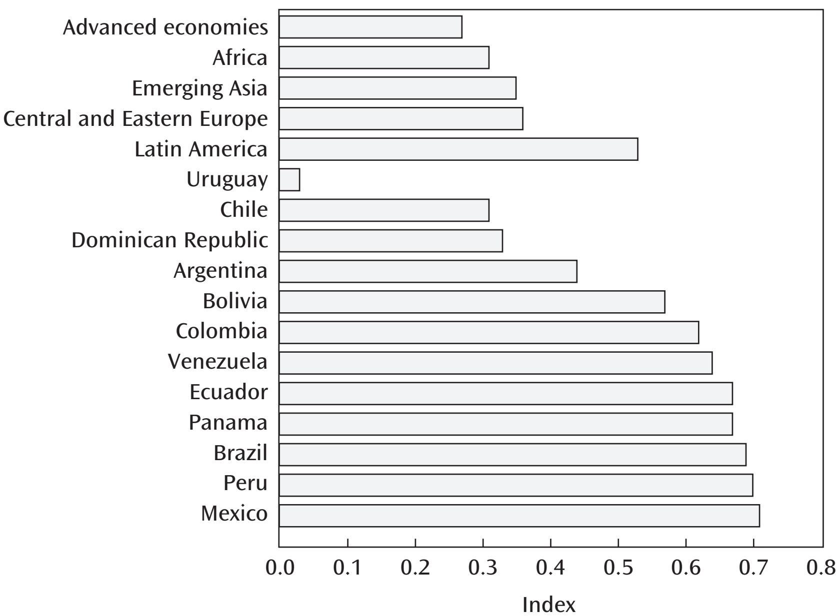
TABLE 6-1. Structure of Urban Employment in Latin America, 1995–2005

Percent

	1995	*2000*	*2004*	*2005*
Informal sector	50.1	48.6	49.2	48.5
Self employed[a]	26.2	25.4	25.7	25.1
Domestic service	6.5	6.3	6.4	6.3
Microfirm[b]	17.4	17.0	17.2	17.0
Formal Sector	49.9	51.4	50.8	51.5
Public sector	13.2	12.8	12.8	12.8
Private firms[c]	34.7	36.4	35.8	36.5
Self employed	2.0	2.2	2.2	2.3

Source: ILO (2006).
a. Includes self-employed workers and workers with no pay.
b. Includes employers and salaried workers.
c. Includes businesses with 6 or more employees.

FIGURE 6-2. Index of Labor Market Rigidity[a]



Source: Botero and others (2003).
a. 0 = low level of labor market rigidities; 1 = high level of labor market rigidities.

unemployment because few countries have society-wide unemployment insurance schemes.[6] Overall, fewer workers today are covered by full-benefit contracts (around 40 percent) than at the beginning of the 1990s.[7] Open unemployment remains high (figure 12 in our Introduction). A large informal sector in which labor productivity is low and workers lack minimal protection and benefits persists everywhere.[8] Labor laws and regulations are often ignored by employers and employees alike because they are obsolete and incompatible with the dynamics of today's markets. And the plethora of rules is such that even sensible regulations—say, on occupational safety—cannot possibly be enforced by ill-staffed labor ministries.

Ironically, severance payments—the insurance mechanism of choice in Latin America—are a costly regulation for workers. Applying only to

6. Five countries in Latin America have functioning unemployment insurance programs: Argentina, Brazil, Chile, Ecuador, and Uruguay. Where they exist, such programs do not work very well. Coverage is limited to workers with regulated, tax-paying contracts. More than 30 percent of government spending on unemployment insurance in the region goes to the richest quintile of the population; less than 10 percent is directed toward the poorest quintile (Perry and others 2006; Goñi, Lopez, and Servén 2006). The level and duration of benefits are low compared with those in more developed countries, and unemployment insurance systems generally lack any connection with training programs or national employment services (IDB 2004a).

7. ECLAC (2006b). In Mexico (1990–2001) and Argentina (1993–2001), more than 60 percent and 80 percent respectively of the unemployed who found jobs did not receive social security benefits in their new jobs (IDB 2004a).

8. The informal sector tends to act as a cushion (given the absence of unemployment insurance) that expands with the loss of formal sector jobs. Uncertainty and weaknesses in labor contracting have been associated not only with a large informal sector but also with the increased irrelevance of labor market regulations in the formal sector. Even when unenforced, unrealistic regulations are perceived as a threat that can cause firms to go informal. Informal sector employment now constitutes half of all nonagricultural employment in the region. In the United States in the early 2000s, the informal sector accounted for about 8.8 percent of the labor force (ILO 2006; Angelelli, Moudry, and Llisterri 2006). Informality is particularly widespread among the poor. IDB (2004a) estimates that 60 percent of working members of the poorest 40 percent of families in Latin America work in the informal sector. In Colombia, available estimates put overall informality at about 61 percent of the labor force, but that estimate rises to 91 percent of the poor (Departamento Nacional de Planeación, cited in Lindert, Skoufias, and Shapiro 2006). Recent studies suggest that the region's informal sector is very heterogeneous, with an upward tier of largely voluntarily informal workers (including most self-employed and some informal salaried workers) and a smaller lower tier for which the sector functions as a safety net. See Maloney (2004); and Perry and others (2007b). But even if voluntary, informal employment (including work in very small firms or self-employment) usually reflects low average productivity and wages (Perry and others 2006; IDB 2004a; Saavedra 2003).

those covered by full-benefit contracts in the formal sector, they are unrealistically generous, leading employers to find ways to avoid paying them. The result is less job security because employers often fire employees before severance payments are vested or become too onerous. There is little incentive for job creation; rather than accept the regulatory burden and risks of hiring new permanent workers, employers invest more in labor-saving capital equipment.[9]

In the 1990s, many countries (for example, Argentina, Peru, Colombia, and Brazil) introduced temporary and fixed-term employment contracts with no benefits or incentives for training as part of half-hearted, partial reforms to address labor rigidities. These are classic second-best measures: they probably are an improvement but they have perverse effects that have not yet been measured, such as reducing incentives for employer-financed training and increasing wage gaps between protected and temporary workers in the long run.[10]

Labor market reform has no doubt been politically difficult. The idea of deregulation and greater "flexibility" is highly inconsistent with the pre-1980s social contract based on industrial sector job protection, and in most countries an alternative safety net of unemployment and health benefits for unemployed workers and their families barely exists. But governments can no longer ignore the "jobs" problem. Lagging labor reform may already have cost countries a great deal by undermining the equity effects of other structural reforms in the region, as discussed in the Introduction.

9. Heckman and Pagés (2004, 2000) find that severance pay in Latin America has negative and high negative effects on employment, mainly for younger and less experienced workers. In Argentina, Pessino (2001) estimates that in 1999–2000 severance payments and advance notice layoff costs represented between 6 percent and 7.5 percent of firm payroll costs (excluding additional litigious expenses that may come up when layoffs occur).

10. IDB (2004a). Overall, temporary contracts accounted for most of the recent rise in formal wage employment in the region—only 4 percent of the jobs created between 2002 and 2005 came with a permanent contract (ECLAC 2006a). In Mexico, 62 percent of the increase in formal employment (covered by the Mexican Social Security Institute) in 2005–06 was accounted for by temporary contracts (which increased by 26.2 percent); only 38 percent corresponded to permanent contracts (which were up by 2.8 percent). In Colombia, the rise in seasonal employment (6.7 percent between January and September of 2006) accounted for all of the increase in manufacturing employment (2.1 percent); the level of permanent employment in the country fell by 1.5 percent in the same period (ECLAC 2006c).

Latin America's rigid labor laws and regulations are obsolete and incompatible with the dynamics of today's markets. In a global economy, creative destruction is the norm. Creative destruction—the process in the market economies whereby new, better companies are allowed to topple old, less competitive ones—creates new opportunities, promotes efficiency, and generates prosperity. But it also triggers an enormous degree of job instability and dislocation. Many new jobs are created, but many also are destroyed. The cost of being competitive in a global economy is, in short, some job insecurity and dislocation.

Those who lose their jobs are not always those who can easily find a job that has equivalent wages and benefits. That fact naturally creates an incentive for uncompetitive businesses to ally with workers demanding more job security and protection from the creative destruction process.[11] The way to avoid such a reaction is to make job changes easier for workers and to soften the blow of dislocation with a reasonable package of temporary unemployment payments and access to training and additional education for displaced workers. Developed countries instituted unemployment insurance when they were much poorer than they are today and not much richer than some countries in Latin America now. Unemployment insurance may not be the top priority in the poorer countries of Central America or in Bolivia and Paraguay. But there is a wider range of policy options that include facilitating the portability of pension and other benefits; protecting collective bargaining; and providing minimal tax-financed income security to workers without jobs. For example, governments could establish emergency programs like Argentina's Trabajar (see chapter 3) and subsidize firms to upgrade workers' skills through on-site apprenticeships for unemployed youth (box 6-1).[12]

The real challenge for governments is to go beyond "deregulation" and "flexibilization" to adopt a proactive stance that focuses on creating new

11. Rajan and Zingales (2004) argues that the group of opponents formed by workers tends to surface during economic downturns. Those who have lost out in the process of creative destruction unleashed by markets see no legitimacy in a system in which they have been proved losers. They want relief; since the markets offer them none, they try the political route.

12. Evidence suggests that unless workers' skills are upgraded, integration into international markets would increase wage disparities in the region, probably because capital tends to substitute for unskilled labor but to complement skilled labor.

BOX 6-1. Linking Work and Education: The Role of Firms and Governments

Policies and practices crucial to encouraging the constant renewal and growth of the human capital of the labor force include the following:

- Governments: Offer tax incentives to encourage firms to give scholarships for short-term classroom training and on-site apprenticeships, particularly for unemployed youth. Scholarship stipends should be set low enough to avoid discouraging recipients from searching for jobs.
- Firms: Create jobs that allow young people (sixteen years of age and older) to work and attend school at the same time. That would offset the pressure to leave school in bad times to compensate for a decline in household income and in good times to take advantage of a booming labor market. It would also be an effective way for firms to recruit highly qualified youth for potential full-time employment. Legal or regulatory changes might be necessary to allow special contracts for young people who attend school—featuring flexible hours, below minimum wages, and greater ease of firing or quitting. To avoid cheating, school attendance should be required in youth training or apprenticeship programs.

jobs rather than protecting old ones and encourages individuals to prepare for job mobility throughout life rather than seek job permanence. A proactive stance also involves simplifying the legislative and regulatory framework in order to enable better enforcement and redefining the role of the labor ministry.[13] The function of the ministry would shift from making unrealistic attempts to enforce regulatory minutiae toward disseminating information (for example, on economy-wide productivity changes to help guide wage negotiations), setting broad standards (say, for occupational safety), and protecting a fair contracting environment for individuals and for unions.

13. Most Latin American countries have ratified most of the basic labor standards embodied in International Labor Organization conventions: free association, the right to collective bargaining, minimum working age, the prohibition of forced labor, and the prohibition of discrimination.

Specific policies to strengthen workers' rights include

- Protecting workers' rights of association and encouraging collective bargaining (covering wages as well as work conditions) at the firm level, within sector- or economy-wide guidelines.[14] Providing flexible guidelines for negotiation and conflict resolution. Raising penalties for illegal anti-union practices and easing regulations that discourage the creation of unions within firms. At the same time, establishing regulations that emphasize transparency and accountability in labor unions, including public sector unions, to ensure that unions are democratic and corruption free.[15] Supporting training programs for union leaders on emerging demands of their members—such as issues pertaining to women in the workplace—and education programs for union members on their rights and obligations.
- Ensuring that the law does not prohibit flexible hiring arrangements. Laws should allow employment contracts for hourly, part-time, and seasonal employment. These contracts should have adequate social protections, proportional to that in the law for open-ended contracts, to prevent large-scale substitution of workers with new contracts for workers with full-benefit contracts.

To increase labor mobility while reducing uncertainty for workers, governments should aim to empower workers to adapt to economic change, succeed in multiple career paths, and choose periods of self-employment.[16] Policy approaches include

- Certification of skills based on national standards. In Mexico, a system for certifying skills provides a bridge for workers between training and

14. Public sector unions in the region (for teachers, health workers, public enterprise workers) are strong in most countries, although often their leadership is more politically ambitious than is consistent with their members' interests. We refer here primarily to unions representing private sector workers.

15. Often the product of old, highly centralized systems for delivering public services, public sector unions (for teachers, health workers, public enterprise workers) have become an obstacle to privatization and political decentralization. While they often lack democratic structures, their militancy and political power bring their members job stability and other benefits, sometimes at the cost of other socially desirable public spending.

16. In addition to the ideas listed here, see emergency employment programs in chapter 3 of this volume.

jobs and from jobs back to formal education. It also requires a stronger partnership between the public and private sectors to better disseminate updated information on job vacancies and to develop effective job-search assistance programs.

- Pension, health care, and other benefits that are portable across and between jobs (see box 6-2 on Chile's program).[17] Developing the financial system to enhance workers' capacity to manage savings throughout their life would contribute much to achieving that goal.
- In the more advanced economies in the region, a system of unemployment insurance (in lieu of high severance payments) that covers all workers in regulated contracts. The system can be built on a partially self-financed program of mandatory employee and employer contributions to individual accounts, which can be rolled over into retirement funds, as in Chile.[18] Both individual accounts and collective insurance can be combined within the system to widen coverage and limit adverse effects on work effort.[19]
- Creation of health insurance, unemployment insurance, and pension systems for informal sector workers.[20] Spain has had success in implementing programs in these areas for the self-employed.[21]

17. In Chile, Bolivia, Costa Rica, El Salvador, and Peru, structural reforms have allowed governments to consolidate disparate systems, making pension portability possible (Mesa-Lago 2005).

18. For further discussion on Chile's unemployment insurance model, including its applicability in other developing countries, see Acevedo, Eskenazi, and Pagés (2006) and Sehnbruch (2006).

19. The Chilean unemployment insurance scheme includes a common fund built with a portion of employers' contributions and direct contributions from the state that pays for partial insurance benefits for workers with insufficient funds in their individual accounts.

20. While the goal of reform should be to bring as many people into the regulated segment of the economy as possible, in the short and medium term many workers and firms may remain out of the formal economy. It is important to address how to reach this large segment of the labor force.

21. For more information on Spain's program see ILO (1999).

BOX 6-2. Portability in Chile

Chile has pioneered a funded, portable system of individual worker accounts that can be used for retirement, work injury insurance and disability, and survivors' pensions.[1] A separate component, a subsidy funded by the state out of general revenues, ensures a minimum retirement benefit level to workers with insufficient funds in their individual accounts.[2] The system has been a success financially, generating accumulated assets equal to about 64 percent of Chile's GDP as of early 2005 and fostering the development of financial markets, with spillover effects on foreign investment, productivity, and growth. The partially self-financed system is also more equitable and progressive than the old pay-as-you-go system, which in Chile applied different rates to different groups, depending on their political clout.

But coverage under the new system—at around 60 percent of the labor force—has not increased compared with that under the old system and so remains a serious challenge. Partly to blame are high job-turnover rates and high levels of informal employment and self-employment, which provide a disincentive to save in a plan that is not liquid. (Self-employed workers, who constitute at least 25 percent of the labor force, are not required to contribute and rarely do.) High and regressive management fees on workers' private accounts also are a problem.[3]

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1. Other worker-initiated withdrawals are permitted only if the remaining balance in the worker's account is large enough to produce a pension that is at least 150 percent of the minimum pension guarantee and 70 percent of the worker's average wage over the past ten years. So far, very few workers have met that requirement.

2. The subsidy is paid to workers who have contributed for at least twenty years to a pension fund and whose savings have been exhausted. As of mid-2007, a new solidarity pillar was being debated in the Chilean congress as part of a comprehensive reform package submitted by the Presidential Advisory Council for Pension Reform that aims at, among other things, expanding coverage and increasing support to those with lower capacity to contribute.

3. Fees are calculated on gross wages instead of a percentage of the assets managed, as in developed countries. Insufficient competition also is a concern. There are about six private pension fund administrators in Chile, and they dominate the financial system.

Sources: Larraín Ríos (2005); Berstein, Larraín, and Pino (2006); James, Martinez, and Iglesias (2006); Arenas de Mesa (2005); Arenas de Mesa and others (2007); Marcel (2006).