UNEMPLOYMENT AS A GLOBAL PUBLIC BAD AND THE ROLE OF FISCAL POLICY

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ABSTRACT
At the present time, the factors that determine the rate of unemployment lie to a significant extent outside the control of the state. What is more, with the increase in global labour, wage differentials lead to the globalization of the production process, thereby making it even more difficult to control unemployment. To offer a solution to unemployment as a Global Public Bad through the growth model based on domestic demand with a relationship established between the wage rate and productivity will only be possible on the basis of cooperation between countries.

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INTRODUCTION
As growing trade and finance flows as well as cross-border mobility of people convert the world into an ever more integrated place, they also create new problems. Domestic policies remain helpless in the face of problems that threaten global stability, problems such as unemployment, climate change, epidemic diseases, or financial crises, which all call for global cooperation for their solution. Hence, in a rapidly globalizing world, people’s welfare no longer simply depends on the equilibrium between private and public goods, but also on that between national, regional and global public goods.

Over the last three decades, unemployment has emerged as one of the most significant problems in the advanced as well as the developing worlds, for it simultaneously increases poverty and threatens social peace and political stability. However, unemployment is no longer a problem that each country can resolve on its own. It is a Global Public Bad that affects all countries and can only be eliminated on the basis of international cooperation.

The concept unemployment came into widespread use in the literature from the 1970s on, replacing the earlier concept “full employment” in the process. It was the changing role of macroeconomic policy and the aims and limitations of state action that necessitated this shift. Up until the 1970s, full employment as an objective remained among the priorities of the state. In that period, unemployment was regarded as a waste of resources as well as a loss in national income and considered to be a factor that constrained an increase in living standards. That is why the provision and maintenance of full employment was seen as a priority target for macroeconomic policy. By tying wage increase to the rise in productivity, total demand was assured to rise in a robust manner alongside wages so as to promote investment through a rise in demand, thus creating a virtuous circle of further productivity and wage increases, thereby achieving the target of full employment (Palley 2007).

However, with the spreading of Friedman’s theory of the natural rate of unemployment, which holds that the economy will spontaneously and swiftly return to the natural rate of
unemployment, and subsequently of the NAIRU debate from the mid-1970s on, the target of full employment was converted into that of “full employability” and regulation of the labour market fundamentally in the interests of capital came to dominate the scene (Mitchell and Muysken 2008). In this approach, a low level of unemployment provides an excess of bargaining power to the working classes. As long as unemployment is kept below its natural rate, this power will lead to a demand for higher wages, which then feed into higher prices, thereby creating spiralling inflation. Hence the state should refrain from intervening in the economy with the purpose of providing full employment or creating better jobs for the working classes. For this kind of intervention is self-defeating since it results in higher inflation and fails to create an improvement in employment (Pollin 2008). In the neoliberal age, when this approach has become overriding, the responsibility for unemployment and underemployment does not belong to the state. The view that insufficient demand restricts employment and results in involuntary unemployment is abandoned. It is no longer the failure of the system, but the failure of the individual that is emphasized. It is widely held that individuals do not put in the necessary effort to acquire the appropriate skills, that they do not sufficiently strive to find the right job for themselves, or that themselves prefer joblessness by behaving lazily or in too demanding a manner and that government reinforces this state of inertia by policies on issues such as income transfer, employment and redundancies (Mitchell and Muysken 2008). Within this framework, counter-cyclical fiscal policy has been abandoned and flexibility in the labour market has been encouraged through microeconomic reforms, thus abandoning the solution to the problem of unemployment to the market. For this purpose, radical shifts are stipulated in economic and social policy. Concerning the labour market, the removal of all constraint in the areas of hiring and firing and the determination of working hours, the removal of rules regarding seniority pay and the minimum wage, the elimination of workers’ right to representation in decision-making processes, the setting of unemployment benefits at the lowest possible level for the shortest possible term, and the disempowerment of labour unions are some of the new arrangements imposed on the working class. For it is held that measures that protect labour step up the natural rate of unemployment by making the downward adjustment of wages more difficult.

Hence, the period of the 1970s was a watershed in the perspective government adopted on employment as well as a break-point in macro policy. In the new period that has since continued, the main objective of macroeconomic policy has become price stability rather than full employment and the new system has focused on financial markets rather than the labour market. Counter-cyclical fiscal policy has been abandoned and fiscal policy restricted to the aim of assuring the sustainability of the budget deficit and sovereign debt. The connection between full employment and fiscal policy has been severed.

In the process, as countries have progressively opened up their economy, they have lost the capacity of curing the problem of unemployment on their own. For one thing, unemployment has risen at the global level. For another, the power of government to control the variables that determine the level of unemployment has been considerably reduced. Moreover, the impact of domestic macroeconomic policy on unemployment is restricted by the significant leakages to which this policy is subject. Hence, under neoliberal globalization, unemployment is a phenomenon that can be characterized as a Global Public Bad that can only be eliminated or alleviated through cooperation between countries. But cooperation is not easy since it requires that countries adopt a pattern of growth based on domestic demand rather than export-led growth and that the wage-productivity nexus is established.

In part two of this article, we will focus on how government control over the determination of the rate of unemployment has been reduced, then go on in part three to discuss the character
of unemployment as a Global Public Bad, to dwell in the concluding part on domestic solutions to the problem of unemployment and the importance of cooperation between countries.

THE DIMINISHING ROLE OF THE STATE IN THE DETERMINATION OF THE RATE OF UNEMPLOYMENT

In the process of neoliberal globalisation, while the outlook of the state on unemployment has changed, the latter has also become a function of factors determined outside the control of single countries. Moreover, the wage differentials that come about with the increase in global labour have led to the globalization of the production process, thereby making it even more difficult to keep unemployment under control.

In heterodox macroeconomics, the relationship between the growth of employment and the growth of output is determined on the basis of the Kaldor identity. According to this identity (1975), the rate of growth of employment is equal to the difference between the rate of growth of the economy and the rate of growth of labour productivity. But since under present circumstances both the rate of growth and labour productivity are largely determined outside the control of the state, the rate of growth of employment and therefore (given the rate of growth of the labour force) the rate of unemployment lie to a considerable extent outside the control of the state. This is because policies of export-led growth implemented for longer than three decades have resulted in a situation in which the rate of growth of GDP has now become fundamentally dependent on the growth rate of exports and hence on foreign demand. Foreign demand is an exogenous variable, not susceptible to being controlled by the country in question. The contractionary monetary and fiscal policy that countries implement in order to keep inflation at bay has an adverse impact on output and employment in both their own country and, indirectly, in other countries since this reduces their demand for imports. On the other hand, the rate of growth of labour productivity is also an exogenous variable, in particular for developing countries. This is because technological progress is initiated by advanced countries. But when a developing country liberalizes foreign trade and capital flows, it needs to bring its pace of technological and structural change in tune with those of advanced countries. Thus the technology of advanced countries is put to use by developing countries, albeit with a brief lag. Technological development of the kind that enhances labour productivity is usually implemented first in the modern industries of the developing country and with the growth of the relative weight of the modern sector within the economy labour productivity rises throughout the whole economy. Hence, while labour productivity growth accompanies the opening up of a developing economy, it becomes more difficult for the country in question to control this growth within its borders. In this case, the rate of growth of employment, determined as this is by the difference between the rate of growth and the rate of labour productivity growth, given the distribution of income, becomes a variable determined by exogenous factors, not susceptible to being controlled by the state. For this reason, unemployment, which appears because there is a shortfall of the growth of employment with respect to the growth of the labour force, is determined outside the control of the state, in particular in open developing economies (Patnaik 2007, 2006).

While the state’s control over the determination of the unemployment rate decreased along with the opening up of the economy, at the same time, the transition to capitalism in the countries of the Soviet Bloc and in China and the opening up of India from the 1990s on resulted in the doubling of the global labour force from 1.46 billion workers to 2.93 billion and the lack of capital in these countries newly integrated into the global economy led to a fall in the capital/labour ratio by 61 per cent (Freeman 2007). As the equilibrium between labour and capital moved against labour, a higher number of workers started to compete for a
smaller number of jobs and a smaller amount of capital. This created important opportunities for capital to increase profitability through the exploitation of wage differentials between countries and led to the globalization of the production process. Thus, many jobs saw their mobility increase and became transportable from one country to another through international trade, foreign direct investment, or arm’s length outsourcing. Despite continuing constraints on the mobility of labour, the conditions on the labour markets of different countries became more and more interdependent (Akyüz 2006, Foster et al. 2011).

From being competition between firms and industries located in different countries, international competition has currently become competition between workers in different countries doing the same job. The considerable wage differentials between countries form the basis of competition. For instance, a Chinese or Indian worker receives 10 per cent or 25 per cent of the wages of a worker doing the same job in the United States or some other advanced country (Roach 2003).

By creating the opportunity of substituting low-wage labour in developing countries for the high-wage labour in advanced countries or, in other words, the opportunity of wage arbitrage, these wage differentials between countries provide capital with the possibility of increasing profitability (Roach 2004). It is mostly the stages of the production process that are more labour-intensive and involve more backward technology or the production of consumption goods that are relocated to developing countries. Thus, different stages of the same production process are carried out in different countries and the share of the trade of intermediate goods produced on the basis of foreign direct investment and arm’s length outsourcing within total international trade is on the rise (Milberg 2004b).

Capitalists can increase their profitability through global labour arbitrage only if there exist a global labour reserve and wage differentials between countries. These way unit costs are reduced and the prices of wage goods are kept at a low level. In this process, the increase in profits and the fall in prices benefit shareholders and consumers, but harm those who are made redundant. But it is not only those who lose their jobs that are made worse off. As a result of the threat of relocation of capital, wages gravitate towards subsistence levels and working conditions deteriorate, bringing down the living standard of workers. Those who have lost their job as a result of outsourcing are more willing to work for lower wages when they are being rehired. While these workers’ income is reduced, the fall in purchasing power has an adverse impact on a broader segment of the population.

Within the process of the globalization of the production process, there is an observable tendency for firms to outsource the production of goods and services rather than producing these themselves (Gereffi 2005, Milberg 2004a). This is because purchasing goods or services by way of arm’s length outsourcing both increases their profitability and at the same time makes it possible for them to avoid some risks. This choice on the part firms makes it possible to reduce wages even further by creating competition between outsourced producers, but at the same time gives them the possibility of avoiding both low value-added production processes and risks and costs that derive from demand fluctuations and imbalances that may...
arise on world markets. Furthermore, firms do not have to take direct responsibility for issues such as environmental degradation, repression of trade union rights, making workers work for long hours under bad conditions without providing guarantees such as social security, pension benefits, sick pay or holiday pay. Responsibility for all of this falls to the contractor who undertakes the production process. Additionally, there is no need for the transfer of capital if purchase of goods and services through outsourcing rather than FDI is preferred (Smith 2010).

On the other hand, the reduction in costs in the global production process encourages the financialisation of non-financial firms. As firms see their excess profits rise, the need for the reinvestment of this profit in their home country or abroad having fallen, these profits are then used to purchase financial assets and increase shareholders’ shares (Milberg and Winkler 2010). Hence, rather than feeding into capital accumulation and creating jobs, the global production process serves to redistribute jobs and investments among countries.

THE GLOBAL PUBLIC BAD: UNEMPLOYMENT

Global Public Goods (GPG) are goods which, in principle, provide benefits to all of humanity. Since it is difficult to give a flawless definition of GPG, it may be more useful to explain its functional properties. The global nature of GPG has to do with the fact that the utility of the good extends to more than one country, many different people or future generations. However, the extension may not be even. The public aspect derives from the fact that there exists nonrivalry (absence of competition) between individuals and nonexcludability (no individual can be excluded) regarding the consumption of these goods (Kaul et al. 1999).

The concept of Global Public Bad is closely related to the concept of Global Public Good. Its disutilities are non-rivalrous in consumption and non-excludable and quasi universal in terms of countries, people and generations. Because Global Public Bads create disutility for individuals, other things remaining equal, these are goods of which less is preferred to more. Where global public bads exist, there is an argument for external intervention to remedy the situation through the provision of global public goods.

Unemployment has the requisite functional properties of a global public bad. As a public bad, it used to be a specific problem for each single country, but in our day and age unemployment in any country has become a problem that affects all countries and has assumed a global dimension. The globalization of the production process and the adoption by many countries of the export-led growth model has been decisive in the transformation of unemployment into a global problem. The increase in job mobility through foreign direct investment and arm’s length outsourcing has led to a loss of jobs for people in the advanced countries and hence to a rise in unemployment in those countries, but this does not mean a decline in unemployment in developing countries. Because the tendency of developing countries to use the capital-intensive technologies of advanced countries to an increasing extent so as not to remain behind in international competition raises labour productivity in the former countries, resulting in increased unemployment.

Moreover, as the global labour force increases, competition between the workers of different countries prevents the rise of real wages as well as resulting in the deterioration of working conditions and a rise in precarious work. On the other hand, the fact that countries have adopted growth strategies based not on domestic but on foreign demand has an important part
to play in unemployment becoming a global problem. This is because the contractionary monetary and fiscal policies pursued by countries mean a fall in their demand for other countries’ goods, which leads to higher unemployment both in the countries that pursue these contractionary policies and those countries that sell goods and services to these countries.

Because its disutilities are non-rivalrous in consumption and non-excludable, it is not possible for single countries to find a solution to unemployment on their own. As was pointed out earlier, as a result of countries opting for the export-led growth model, unemployment has to a large extent become a variable that cannot be controlled by the state. However, simply implementing a growth model based on domestic rather than foreign demand does not bring the success it used to in Keynesian times because of increased spending leakages on imports, financial leakages, investment leakages via foreign direct investment, and job leakages via off-shoring of production (Palley 2011). For this reason, the problem can only be solved on the basis of cooperation between countries.

GROWTH BASED ON DOMESTIC DEMAND AND THE IMPORTANCE OF INTERNATIONAL COOPERATION

The export-led growth model that has come to be implemented in many countries in the process of neoliberal globalization is predicated upon the repression of wages and domestic consumption. In this growth strategy based upon foreign demand, success depends on increasing market share by cost reduction through a decline in wages. This practice geared towards a beggar-thy-neighbour attitude can raise production and employment in the country only temporarily since the advantage obtained at the cost of other countries is eliminated as soon as those countries also reduce wages. Because of a race to the bottom in wages, the fall in the purchasing power of wage workers leads to a fall in total demand, which results in rising unemployment at the global level. Moreover, since the demand for exports in the OECD and EU countries is not very sensitive to relative unit labour costs, bringing wages down in order to improve cost competition has only a restricted effect on exports, while it results in the shrinking of domestic demand (Carlin et al. 2001, Felipe and Kumar 2011).

Because wages are treated only as a cost item in the neoliberal approach, it is expected that with the flexibilization of the labour market, that is to say with the elimination of regulation concerning wages, working hours, occupational safety etc., demand for labour will increase and bring unemployment down. Hence it is assumed that the demand for labour is no different from the demand for other goods and that when wages fall the demand for labour will rise. However, as well as being a cost item, the wage bill is an important determinant of the level of domestic demand. To the extent that the purchasing power of those who receive a wage income falls, so does total demand, bringing output down and raising unemployment. For this reason, in order to solve the problem of unemployment, one needs to look first and foremost to the market for goods rather than the labour market and in particular to investment spending. Increasing investment is an important factor in reducing unemployment (Rowthorn 1995, Arestis et al. 2007, Akyüz 2006). For investment both acts to create income as an element of effective demand and at the same time make it possible to increase production capacity. The determinant of investment, then, becomes important. Total demand is the most important determinant of investment. That is why economic policy should focus on total demand management (Stockhammer and Klär 2011).

* This lack of empirical relationship between the growth in unit labour costs and export growth is known in the literature as Kaldor’s paradox.
† The OECD (2011) calls for greater labour market flexibility - reduced employment protection, more decentralized wage bargaining, lower minimum wages, higher retirement ages, but lower pensions and lower labour taxes.
Since the 1980s, demand management has relied on asset price inflation and borrowing rather than the labour market. In this period, monetary policy has shadowed fiscal policy, automatic stabilizers have been prioritized, and procyclical fiscal policy has been pursued, especially in developing countries. However, fiscal policy should once again have the upper hand in demand management because the question of employment, the most decisive determinant of welfare, is too important to be left to the functioning of markets. For this purpose, alongside the practice of countercyclical fiscal policy, the role of government as investor should be emphasized once again and public investment that creates employment, raises labour productivity and welfare should be stepped up, as well as investment in the physical and human infrastructure.

The increase in public investment financed through borrowing in times of economic stagnation on the basis of countercyclical fiscal policy helps protect the level of employment by giving the economy a boost, while reducing public investment or raising taxation in times of demand expansion re-establishes the stability of total demand. Government countercyclical fiscal policy that involves budget deficits if needed in order to balance demand and employment creates a macroeconomic environment where uncertainty recedes, which then acts as an incentive to raise private investment and consumption spending, thus reinforcing a process of growth with jobs.

However, expansionary macro policies aiming at full employment without regard to the wage-productivity nexus cannot provide for a sustainable improvement and may end up creating a fiscal crisis. For that reason, the export-led growth model should be replaced with a growth strategy based on domestic demand, where wage rises are tied to productivity rises. This kind of strategy can be attained by sharing out productivity rises between labour and capital in a way that will not reduce the share of wages in total income and domestic demand will increase in line with the increase in productivity, promoting additional employment and more investment (UNCTAD 2010, Palley 2007, 2011, Ghosh 2011).

By creating higher demand, wage increases promote higher capacity utilization and hence, by raising the rate of profit, encourage firms to make more investment. New investments both create jobs and raise labour productivity. The result is a sequence of rounds of demand growth and increases in capacity utilization and hence in the profit rate. If labour productivity rises more rapidly than output growth because of high wages, there may be a fall in employment growth. This can be offset by reducing the number of hours worked and/or increasing public employment in areas such as health care, education and the protection of the environment (Storm and Naastepad 2011). In this, the employment policy of the government as the largest employer should lead the way for the private sector. The reduction in working hours through systems of two or three shifts will be exemplary for the private sector.

In order to use fiscal policy effectively in demand management, it is necessary to effect changes in the taxation system as well. The tax system should be restructured so as to improve the progressive nature of income tax, increase the number of tax brackets and the marginal rates, and eliminate tax expenditures that create privileges in favor of capital income and convert income tax into a regressive system. In the area of corporate tax, the deferral of taxes on foreign profits should be eliminated as this promotes the relocation of investment and jobs abroad. Rather than tax corporations, the system should tax shareholders receiving profit income. This will stop corporations moving abroad for tax advantages (Palley 2011).

In addition, countercyclical tax policies should be implemented in the taxation of financial flows. This is because investment, the most volatile component of total demand, is quite sensitive, in particular in developing countries, to external shocks and financial flows.
increase in volatility in investment because of financial flows has an adverse impact on capital accumulation and employment since as the rise in investment in the phase of financial expansion remains below the decline in investment in the phase of financial contraction, the average rate of investment tends to fall over the cycle. Moreover, the composition of investment also deteriorates in the phase of financial expansion as speculative investment rises and production capacity expands excessively in certain industries. As the adverse effect of financial volatility on capital accumulation and economic growth is passed on to the labour market, unemployment and poverty rise, wages fall, and the distribution of income worsens (Akyüz, 2006). For this reason, it is necessary to impose an ad valorem securities transactions tax of a very low rate on equities, bonds, and options, as well as futures and financial markets and to establish financial stability. A broad tax base and a low tax rate minimize the distortion effect of taxation on resource allocation, while simultaneously creating an important source of revenue for countries (Göker and Balseven 2008).

Such a growth strategy based on domestic demand with wage rises tied to rises in labour productivity can be a solution to unemployment. However, as mentioned earlier, it is not possible for the economies of our times to find a solution to the problem of unemployment through this method on their own. This is because the additional income from wage increases may boost the demand for foreign goods rather than domestic goods. In this situation, a leakage is created in favor of other countries and output and unemployment do not rise. On the other hand, if no restrictions are imposed on the circulation of capital, the wages that rise on the domestic front create an opportunity for labour arbitrage, resulting in higher investment in lower wage countries or production being carried out in those countries on the basis of outsourcing, hence not creating the expected improvement in employment.

For that reason, there should definitely be cooperation between countries in order to solve the problem of unemployment, with exchange rates so determined as to reduce wage competition and establish a sustainable trade balance and multilateral norms adopted on standards relating to the labour market and taxation. Thanks to this kind of cooperation achieved between countries, while economies grow on the basis of domestic demand, unemployment will become a problem that they can solve within their own borders, and with relations established between wages and labour productivity, wage differentials between countries will vanish, leading to the elimination of investment and job leakages to a large extent.

CONCLUSION

In the process of neoliberal globalization, unemployment has assumed the character of a global public bad. For this reason, countries can solve the problem not on their own but through cooperation. Leaving aside the discussions on how to create cooperation, whether this should be established between leading capitalist countries or through a supra-national institution, cooperation between countries in favour of labour, developing strategies based on domestic demand, with a link between wages and labour productivity, will be resisted by capitalists, even if this does not create results against their interests. This is because an ever-growing global labour reserve provides capitalists with the opportunity of imposing upon labour lower wages and deteriorating work conditions and also with the freedom to choose the investment location, thereby raising their profitability.
REFERENCES


