

# 7. SYSTEMIC REFORMS FOR FULL EMPLOYMENT AND DECENT WORK

Global responses to the economic crisis have given impetus for reform on long-standing systemic deficiencies in global economic governance. This final chapter briefly reviews some of these in terms of their direct and indirect bearing on progress toward full productive employment and decent work for all. These include international tax issues, a new international debt architecture, a new global reserve system and staving off currency speculation.

## INTERNATIONAL TAX ISSUES

Where progress has been most significant is in the area of international taxation and tax cooperation. International resource transfers are an integral part of the strategies needed to finance the global social protection floor, public investments for productive employment and more generally the transition to low carbon development paths. However, the OECD-DAC is already warning that, due to the financial crisis, 2010 will be a “crunch year” for ODA.<sup>54</sup> Progressive taxation efforts on multiple fronts become all the more indispensable. The good news is that large fiscal deficits ensuing massive bank bailouts and stimulus packages in the rich countries have increased the political will to institute collective measures needed to combat tax evasion, tax competition and explore innovative financing mechanisms. There is still a long way to go, but some important developments are worth highlighting.

- The UN 2008 Doha Conference on Financing for Development decided to set in motion a process to consider strengthening the UN Committee of Experts on International Cooperation in Tax Matters – which the Stiglitz Commission subsequently proposed should be upgraded into an intergovernmental body to strengthen its ability to enhance international cooperation in this area, notably “to ensure that all countries commit themselves to the voluntary automatic exchange of information that would help root out tax evasion and corruption and also the repatriation of illegal funds” (UN 2009:83-84). In this regard, the global civil society consultation for the Stiglitz Commission highlighted among others things the need to end the practice of transnational corporations manipulating their accounts through distorted “transfer pricing” to show their profits where they are taxed least heavily, rather than where they are earned.
- The G-20 have stepped up pressure on tax havens and are exploring options on “how the financial sector could make a fair and substantial contribution toward paying for any burdens associated with government interventions to repair the banking system.”<sup>55</sup>

---

54. Presentation of OECD-DAC of its new survey on future aid plans at the second meeting of the Inter-Agency Consultative Group on the Fourth UN Conference on LDCs held on 4 November 2009 in Geneva.

55. Paragraph 16 of the G-20 Leaders’ Statement: The Pittsburgh Summit.

Some civil society activists have described this decision as a possible step towards establishing a **Financial Transaction Tax** (FTT) – a broader concept than a currency transaction tax (or “Tobin Tax”) to encompass also taxes on other financial transactions such as in relation to bonds, equities and derivatives.<sup>56</sup>

- Soon after, the Leading Group on Innovative Financing for Development (regrouping nearly 60 countries from North and South as well as NGO observers) decided in October 2009 to set up a Task Force “to explore several options for financing development based on an assessment of the feasibility of an approach focused on international financial transactions.”<sup>57</sup>

It is important to distinguish the introduction of new international taxes from measures to prevent a “race to the bottom” in terms of **tax competition** between countries to attract or retain footloose capital. The latter would eventually imply international agreements on, for example, what should be a minimum tax floor on FDI. The ILO World Commission suggested that regional initiatives to that effect among countries with comparable levels of development might be an important stepping stone in that direction (ILO 2004a).

## **A NEW INTERNATIONAL DEBT ARCHITECTURE**

The debt crisis that hit developing countries in the early 1980s paved the way for structural adjustment policies that had a devastating and enduring impact on jobs and livelihoods. Just as their debt situation was finally improving in recent years, this new crisis – for which they had no role in causing – risks plunging many of developing countries into a new debt crisis.

The UN Conference on the world economic and financial crisis affirmed that “appropriate measures must be taken to mitigate the negative effects of the crisis on the indebtedness of developing States and to avoid a new debt crisis.”<sup>58</sup> In this respect, *UNCTAD has called for a debt moratorium on all official debts to all low-income countries without exceptions, conditionalities or performance criteria* (UNCTAD 2009). The IMF has since decided to suspend interest payments on low-income country debt up to 2011. According to UNCTAD, this is a step in the right direction but is not sufficient, given that the suspension only covers interest payments rather than much larger repayments on principal; and the time-frame is too short in light of prospects of only slow recovery.<sup>59</sup> Many civil society organizations are concerned that emergency support to developing countries is in the form of loans rather than grants – and sometimes subject to pro-cyclical conditionality as discussed in Chapter 4. They have called for **unconditional debt cancellation** as part of crisis response measures that would not be drawn from existing and new ODA resources (NGLS 2009a).

Beyond that, many voices are calling for fundamental reform of the international debt architecture. Some of the ideas on the table were already developed in the aftermath of the 1997-98 East Asian crisis, but soon lost steam as developed countries dropped their support for meaningful financial architecture reform in the euphoric speculative boom that

---

<sup>56</sup>. Joint NGO letter to IMF Managing Director dated 11 November 2009 concerning: “Request for civil society participation in IMF study on how the financial sector can help pay for the bailouts.”

<sup>57</sup>. See Declaration: <http://www.leadinggroup.org/article465.html>.

<sup>58</sup>. Paragraph 33 of the Conference Outcome Document.

<sup>59</sup>. Yuefen Li, UNCTAD (Per. Com.).

followed (UNCTAD 2001). This includes the proposal for a **fair and equitable debt work-out mechanism** that would allow debtor countries in difficulty to declare a unilateral “standstill” on debt payments, with creditors having to abide by the terms for debt restructuring of an independent arbitration panel. More fundamentally, civil society groups are calling for a rethink of current debt sustainability criteria that would not be based on debt-to-export ratios, but on sustainable development criteria. One specific criterion that many groups have been advocating for some time would be the domestic resources needed to meet the MDGs (NGLS 2009a). What would the criteria imply if estimated domestic resources required would integrate the new MDG target of full and productive employment and decent work for all?

## **THE BALANCE-OF-PAYMENTS CONSTRAINT (PART 2)**

Chapter 5 reviewed the conventional approach to the “balance-of-payments constraint” that places limits on what developing countries can achieve without facing a balance-of-payments crisis (which causes a chain reaction often leading to mass unemployment and deterioration of social conditions). This section examines an alternative approach that Professor Joseph Stiglitz presented at the ILO Global Employment Forum in November 2001 and which he referred to as the “**trade deficit trap**.”

Professor Stiglitz argued that an essential dimension of international financial reform is related to the question of trade deficits. He said that in the current doctrine, “countries with large trade deficits are told to cut them back,” but without comparable pressure on large surplus countries. If a country cannot boost its export earnings sufficiently to close its trade deficit, it depends on capital inflows to make up the difference. If these are not sufficiently forthcoming or the deficit is prolonged for too long, to avoid a crisis the country must sooner or later turn to the IMF for help, which one would expect would provide resources for expansionary policies to avoid cut backs on imports that would have negative spill-over effects on export-related jobs in other countries.

However, the IMF had not only abandoned its original mandate, Professor Stiglitz noted: it had taken up “the opposite banner,” all too often providing funds to countries only on the condition that they engage in measures to reduce imports and reassure foreign investors. Since the raising import barriers is discouraged, there remain few options but to cut back effective demand through contractionary policies, despite their contribution to global slowdown and their predictable toll on job losses and cut backs in public services. “The sum of all trade surpluses minus deficits must add up to zero,” he continued. If some countries insist on having large surpluses, other countries must have correspondingly large deficits. “*The deficits are like hot potatoes: as one country is forced to eliminate its deficit, it must show up somewhere else in the system. With a focus on trade deficits, no wonder then there is always an impending crisis somewhere in the world*” (NGLS 2002:5).

## **TOWARDS A NEW GLOBAL RESERVE SYSTEM?**

The solution to this systemic impediment that Professor Stiglitz proposed at the ILO in 2001 was a cornerstone of the Stiglitz Commission recommendations and in the negotiations for the 2009 UN Conference on the world financial and economic crisis – the move towards a **new global reserve system**. The idea was originally proposed by John Maynard Keynes some eighty years ago in his 1930 *Treatise on Money*. Current discussions on the need for a

new global reserve system are usually linked to the systemic risks posed by global imbalances and the fragility of the US dollar as the world's *de facto* reserve currency. However, another angle to examine the same problem is the fact that ***the present global reserve system is incompatible with global full employment and is inequitable***. The following sections explain why and what are some of the ideas on the table for reform at global and regional levels.

In making his proposal at the 1944 Bretton Woods Conference for an *International Clearing Union* with an international reserve currency named the “**bancor**,” Keynes was concerned that the above-mentioned asymmetric adjustments between trade deficit and surplus countries would tend towards a ***deficiency of global aggregate demand*** (money is hoarded instead of spent in the surplus countries, while import demand is cut back in deficit countries). This asymmetry also implied a ***constraint on the policy space needed for policies in support of full employment***. Adjustments to these imbalances could be smoothed with the emission of this international reserve currency that would act as a buffer to compensate deficit countries for the gap created by foreign exchange reserves “hoarded” in countries that maintain structural surpluses. More equitable (“symmetric”) disciplines were also envisaged for both deficit and surplus nations. This concern was never adequately addressed at Bretton Woods, which partly explains the above-mentioned “trade deficit trap.”

The deflationary bias of the system has been compensated to some extent by the fact that the United States, as emitter of the world's global reserve currency, has been able to sustain large trade deficits for a long time. The United States is not only the “consumer of last resort,” but also the “deficit of last resort.” The problem of using a *national* currency as an *international* reserve currency was identified by Robert Triffin in the 1950s and has become known as the “**Triffin dilemma**”: dollar deficits necessary to increase global liquidity can erode confidence in the dollar as a reserve currency. There are other reserve currencies, but the dollar still remains the main choice for settling international payments. With confidence in the dollar eroding, holders of large dollar-denominated reserves have an incentive to diversify, but further diversification away from dollar holdings may precipitate a downfall of their remaining dollar assets. A disorderly collapse in the dollar's value could be the cause of yet another global financial crisis.

A move to a multiple currency reserve system based on multiple, competing reserve currencies, would not resolve the problems associated with the current system; it would in fact add an extra layer of instability. Indeed, matters have been made much worse since the breakdown, in the 1970s, of the Bretton Woods system of fixed exchange rates tied to the gold convertibility of the dollar. The move to flexible exchange rates among the major currencies, combined with widespread relaxation of controls on capital movements, has dramatically increased global instability and the frequency of crises, as well as the inability to guarantee full employment.

Especially since the 1997-98 East Asian crisis, developing countries that could afford it have been accumulating very large foreign exchange reserves as a buffer against future crises and to create the policy space to respond if they occurred. This view was reinforced with the record of pro-cyclical policy conditions imposed by the IMF as the only “collective insurance” system at the global level. In addition, restrictions on the ability to use industrial policies to encourage nascent industries in emerging economies under recent WTO agreements may have led some countries to substitute exchange rate policies to effect similar outcomes, thus contributing to reserve accumulation (UN 2009).

As a result of these factors, reserve accumulations more than doubled in the decade after the East Asian crisis, rising from 5.6 percent of world GDP in 1997 to 11.7 percent in 2007. Reserve accumulation in the period 2003-2007 amounted to an annual average of US\$777 billion, or 1.6 percent of GDP. When these reserves are “earned” through trade surpluses as opposed to being “borrowed” through foreign capital inflows, there is a deficit in global aggregate demand. Thus the system is incompatible with global full employment; but it is also highly inequitable: developing countries have been transferring resources (typically at very low interest rates) to the developed countries that issue the reserve currencies. That amount was estimated at US\$3.7 trillion in 2007. *The difference between the lower lending rate and the higher interest rate that developing countries pay developed countries when they borrow from them represents a net transfer of resources from poorer to wealthier countries.* In proportion to GDP, the amount of reserves that developing countries have been holding is multiple times greater than developed countries: 26.4 percent for developing countries versus 4.8 percent for high-income OECD countries in 2007 (UN 2009).

### **HOW WOULD THE SYSTEM WORK?**

Since the global economic crisis, Keynes’ idea of a new global reserve system is back on the international agenda. It is now implicitly part of the follow-up to the UN Conference on the world economic and financial crisis (see below). Considerable discussion will be needed for the international community to decide the precise arrangements. According to the Stiglitz Commission, the basic idea would be the annual emission of an international currency that would be targeted to offset the increase in “non-borrowed” reserves – meaning to compensate for reductions in global purchasing power resulting from excessive reserve accumulation. The system of allocation could also have built-in incentives or penalties to discourage countries from maintaining large surpluses. It could build on the potential new source of global liquidity known as **Special Drawing Rights (SDRs)**<sup>60</sup> that was created in the 1960s. The potential of SDRs was never fulfilled (with only minimal emissions in 1970-72 and 1979-81). However, the recent approval by the IMF (as a result of a decision at the April 2009 London G-20 Summit) of a new emission of SDRs equivalent of US\$250 billion constitutes an important breakthrough on which more fundamental reforms could evolve. In this regard, the UN Conference on the world financial and economic crisis agreed that:

“The crisis has intensified calls by some States for reform of the current global reserve system to overcome its insufficiencies. We acknowledge the calls by many States for further study of the feasibility advisability of a more efficient system, including the possible function of SDRs in any such system and the complementary role played by various regional arrangements.”<sup>61</sup>

A major stumbling block is inequitable allocation of SDRs, which is tied to a country’s IMF quota (in turn derived from its weight in the global economy) rather than a country’s need. Another problem is widespread scepticism about the IMF being in a position to administer the system, at least in the absence of fundamental governance reform. An alternative proposed by the Stiglitz Commission is to assign this role to a new institution such as a

---

<sup>60</sup>. SDRs are valued as the weighted average of the major currencies. In July 2009, the SDR basket contained the value of 0.632 US dollars, 0.410 euros, 0.0903 pounds sterling and 0.0543 yen (UNCTAD 2009).

<sup>61</sup>. Paragraph 36 of the Conference Outcome Document.

“Global Reserve Bank.” The Stiglitz Commission outlines a variety of options on how the system could function. In its more sophisticated version, the system would allocate SDRs on the basis of “need” (which could be equated to estimated demand of reserves) in a counter-cyclical fashion. It could also enable to provide revenues to finance development and global public goods via multilateral development banks – an old idea already proposed by an UNCTAD panel of experts in the 1960s (UNCTAD 2009). The UN Conference recognized in this regard “...the need for keeping under review the allocation of SDRs for development purposes.”<sup>62</sup>

According to the Stiglitz Commission, there are many reasons why major reserve currency countries, including the United States, would find it in their interest to join such a system. There are of course the benefits of a more stable global economy that can more readily operate at full employment. In the current system, the United States has the benefit of borrowing at low cost, but also suffers from its role in supplying global reserves. The demand for global reserves has led to increasing current account deficits in the United States that have had adverse effects on US export-related jobs: when dollars are held to meet demands for liquidity in surplus countries, there is no countervailing increase in demand for US goods. This necessitates the US maintaining persistent fiscal deficits, if it wishes to keep the economy at or near full employment. And the periodic need to correct these deficits requires contractionary monetary or fiscal policies that have adverse effects on the domestic US economy as well as the world economy (UN 2009).<sup>63</sup>

Besides strengthening political support for wider and more equitable use of SDRs, some analysts point to the need to build confidence in the use of SDRs as an accepted means of international payments – so as to bypass the need to convert SDRs in dollars or other hard currencies before making such payments.<sup>64</sup>

## **A “BOTTOM-UP” REGIONAL APPROACH?**

Given the complexities and political resistance involved, it may be difficult to achieve the transition through a global agreement from the outset. Civil society organizations have also expressed reservations of a global system built from the “top down” – where asymmetries between “hard” currency and “soft” currency countries could lead to an inequitable outcome. An alternative, also proposed by the Stiglitz Commission, would be a “bottom-up” approach through existing and new regional initiatives involving currency swap arrangements or even pooling of reserves that could enable the issuing of a new reserve asset (a “regional SDR”) that could be used at regional or even global levels.<sup>65</sup>

---

<sup>62</sup>. Paragraph 35 of the Conference Outcome Document.

<sup>63</sup>. According to the Stiglitz Commission, the costs for the US far outweigh the benefits of the current system, especially now that major shareholders of dollar reserves are worried about the value of their reserves should the US adopt policies leading to a depreciation of the dollar. The only way to respond to these concerns would involve a loss of monetary autonomy for the US as it would have to take into consideration the effects of its monetary policy on the rest of the world and perceptions of these impacts (UN 2009).

<sup>64</sup>. See for example, Aldo Caliarì “Can the G20 have it both ways? Addressing global imbalances without reform of the world monetary system,” Center of Concern: <http://www.coc.org/node/6441>.

<sup>65</sup>. In Asia, for example, a high-level meeting of senior officials of finance ministries and central banks of the region held in Dhaka in July 2009 supported “regional arrangements that lessen reliance on traditional reserve currencies, such as multilateral systems for payments of trade transactions with domestic currency, complemented by regional units of account and clearing unions. These could eventually become the basis of regional currencies. Such arrangements would have the added value of increasing fiscal space – by relaxing pressure on hard currency reserves – >>>

Regional initiatives could become part and parcel of the global reserve system. Some have suggested that the reformed IMF should be a network of such regional reserve funds. Such a decentralized system would have the advantage of better solving problems with crises in the smaller countries at the regional level, in which they would also have a greater voice. One way to link regional and global arrangements would be to make contributions to regional arrangements one added factor in determining SDR allocations (UN 2009).

### **STAVING OFF CURRENCY SPECULATION FOR STABLE EMPLOYMENT**

The move to a new global reserve system can help deal with chronic liquidity short falls and some of the asymmetries in the current system described in this volume. Together with the use of appropriate capital management techniques, it could increase the “armoury” available to national or regional authorities to combat (among other systemic risks) currency speculation, and the devastating toll that currency gyrations cause to enterprises and workers around the world. But would it be enough?

According to UNCTAD, the longer term solution would involve a multilateral agreement for managing exchange rates so that “real” exchange rates remain stable at a sustainable level. It is premised on the notion that, contrary to mainstream theory, currency markets have a tendency to “get the price wrong” through speculative arbitrage between interest rates that lead to “overshooting” and “undershooting” of currency values. So the task of managing exchange rates should be returned to governments, but there are limits to what individual monetary authorities can do on their own – thus the call for international cooperation. In the proposed system, the “nominal” exchange rate would be adjusted periodically using inflation differentials as the main guide (so the “real” exchange rate remains stable), and the value of each currency would be anchored to a new artificial currency – whether SDR or some other international unit of account. The difficulty would be in determining the initial purchasing parities of each currency, but then coordinated “symmetrical” interventions from member central banks (through essentially emissions of the appreciating currencies to buy up enough of the devaluating currency) would by and large defeat the arbitrage strategies of speculators. Again, regional initiatives might be the most realistic way forward. **Currency swap arrangements** are already part of regional agendas under construction in Latin America and Asia (UNCTAD 2009; NGLS 2009b).

It remains unclear whether such a system would necessarily involve a loss of monetary policy autonomy, as is the case for Eurozone member countries, although more policy space would be gained in other areas. In addition, by removing exchange rate tools, would there be intensified pressures on domestic labour markets to become more “competitive?” According to UNCTAD’s current chief macro-economist, Heiner Flassbeck, the answer is yes: to avoid “**wage dumping**,” the system would also need to include an agreement by member countries to take the necessary steps needed to ensure that average wages rise in line with productivity growth (NGLS 2009b).

---

>>> and boost intra-regional trade, thus help in mitigating the impact of trade-related shocks.” (See paragraph. 33 of the Dhaka Outcome Document : <http://www.coc.org/system/files/Outcome+Document.pdf>.) Similar discussions are taking place in Latin America on a “New Regional Financial Architecture” built around three pillars: the Bank of the South (*Banco del Sur*); the Common Reserve Fund of the South (*Fondo Común de Reservas del Sur*); and a regional settlements clearing system based on a new currency unit called SUCRE (*Sistema de Compensación Regional de Pagos*). Source : Ecuadorian Technical Commission for a New Regional Financial Architecture (Per.Com.).

---

As we have seen throughout this volume, the need for decisive progress on **aligning wages with productivity growth** is an essential cross-cutting priority. Any rigid legally-binding agreement, if desirable, might be difficult to achieve, at least from the outset. But certainly, there would need to be much more public debate at national and international levels on what should be the panoply of policies and institutions required in different contexts to reach that goal (as we have seen some of them well beyond the remit of the ILO and labour institutions). Progress on that front alone could make a decisive difference in efforts to rebalance growth patterns and (together with other policies such as redistributive taxes) reverse systemic income inequalities associated with globalization.