

OECD Employment Outlook - 2005 Edition

Editorial

Globalisation: Coping with the Challenge

By John P. Martin

Director for Employment, Labour and Social Affairs
June 2005

The many faces of globalisation reflected in rising imports, outflows of foreign direct investment (sometimes tied directly to offshoring of production) and inflows of immigrants, have contributed to rising job insecurity in many OECD countries recently. According to some commentators, globalisation is leading to significant job losses, not just in industry, but increasingly in some hitherto non-traded services, and exerting downward pressure on the wages and working conditions of many OECD workers. When this is combined with rapid technological change (*e.g.* in the ICT sector and the Internet), the spectre of job losses is not confined mainly to blue-collar workers but could also hit many white-collar workers too. These anxieties have been fuelled by the rapid integration of two huge labour-surplus countries, China and India, into the world trading system, as well as the recent EU enlargement.

Not surprisingly, these anxieties have been heightened against the backdrop of relatively sluggish employment growth in a majority of OECD countries, notably in continental Europe. OECD projections are for a small improvement in the employment record in 2005-2006 for the OECD area as a whole. On current trends, there would be 36 million unemployed workers in the OECD area in 2006, only one million less than in 2004.

Globalisation holds the promise of better living standards...

Such concerns are in stark contrast with evidence that past episodes of trade and investment liberalisation have been an important source of rising employment and living standards. Increased market openness creates new business opportunities for all participating countries, promotes consumer choice and makes room for higher real incomes. Past experience also shows that protectionist policies are a blind alley: countries that have been more open to trade have also tended to experience higher economic growth than less open economies.

... but also entails adjustment costs

Yet, realising the gains from trade requires the move of production factors away from activities in which a country is relatively less efficient than its trading partners and towards activities where it is relatively more efficient. This means that job losses in some sectors, along with new job opportunities in other sectors, are an inevitable accompaniment of the process of globalisation. The challenge is to ensure that the adjustment process involved in matching available workers with new job openings works as smoothly as possible.

The size of the adjustment challenge needs to be put in perspective. Only a fraction of job losses recorded in OECD countries is likely to be directly attributable to trade and investment liberalisation. To illustrate this, data for 15 OECD countries over the period 1900-2000 show that the high-import-competition industries within manufacturing only accounted for 4 per cent of total employment on average. However, adjustment is neither automatic nor painless. Chapter 1 shows that workers losing their job in high import-competing industries are slower to become re-employed and experience larger wage cuts once re-employed than other job losers. This reflects the fact that trade-displaced workers tend to be older, less educated and more often possess skills specialised in declining occupations and industries, as compared to other job losers.

Programmes targeted on trade-displaced workers may be justified in specific circumstances...

Though trade-displaced workers tend on average to suffer larger adjustment difficulties than other groups, it does not necessarily follow that specific policy measures are needed. However, there may be grounds to implement targeted support measures and re-employment services when trade shocks disproportionately affect specific regions giving rise to largescale lay-offs in local labour markets with few alternative jobs available on the spot. Indeed, as illustrated in Chapter 2, regional employment imbalances are often persistent, even in countries where workers are relatively mobile across regions. Likewise, targeted programmes may make sense when entire sectors are affected by trade and investment liberalisation – and the problem is particularly acute when declining sectors are located in already depressed regions. But it has to be acknowledged that such targeted measures have a mixed record, sometimes becoming *de facto* barriers to

adjustment. So they should be used sparingly, strongly oriented towards facilitating orderly adjustment and time-limited.

In addition, it is sometimes claimed that trade-displaced workers have a particular claim to public assistance on the grounds that their situation results from a deliberate policy decision to liberalise trade and investment flows which will increase income and welfare for the rest of society. A variant of this argument, much used in the United States, is that without specific aids for trade-displaced workers, it may be impossible to pursue trade liberalisation initiatives. If such political economy arguments prevail, care should be taken to minimise the inefficiencies and inequities that can result from singling out trade-displaced workers for assistance beyond that offered to other workers encountering similar difficulties in the labour market.

... but the overarching goal is to provide income support for job losers in general, while also promoting re-employment incentives

Except in these specific circumstances, the challenges of trade displacement are not very different from those arising from job loss in general. Therefore, the overriding policy requirement here is to provide income support to job losers in general, while at the same time fostering their move into new jobs.

Unemployment benefits are the most obvious way to compensate “losers” from import competition and delocalisation. These benefits may further equity goals by leading to a more even distribution of the benefits and costs of international economic integration. They may also support efficiency goals by enabling job seekers to look longer for a job that makes good use of their skills. However, inefficiencies might also result, since unemployment benefits tend to blunt incentives for trade-displaced workers to search actively for a new job. Labour supply disincentives may be particularly strong in the case of trade-displaced workers whose job experience and skills are a poor match for the available jobs. Typically, such workers will have to accept a significant cut in pay in order to become re-employed. In such instances, unemployment benefit payments that appear quite modest, when compared to previous earnings, may be much higher compared to *prospective* earnings, thereby creating a strong unemployment trap.

Since the overall policy requirement is to ensure that displaced workers have opportunities and incentives to adjust, measures that incite displaced workers to withdraw from the labour market, *e.g.* through the use of early retirement, disability benefits or unemployment benefits with lax job-search requirements, should be avoided. Indeed, every effort should be made to keep displaced workers in close contact with the labour market. Nonetheless, it should be acknowledged that policy makers often face a difficult trade-off between providing adequate benefits and preserving work incentives.

*Ensuring that work is financially attractive
vis-à-vis benefit receipt is one way of
achieving this,...*

One way to address this trade-off is by providing a financial incentive to jobseekers who find a job. Such in-work benefits are typically targeted on low-income individuals and care should be taken in designing them in a manner that reduces the risk of deadweight loss. But experience shows that they can be an effective way of promoting work incentives (Chapter 3). Wage insurance schemes, which replace part of the difference in earnings between old and new jobs, are an interesting innovation being tried in a few countries (France, Germany and the United States) with the aim of encouraging displaced workers to find new jobs more quickly. However, such schemes raise difficult design issues and have not been evaluated rigorously yet.

*... activation strategies, if well designed, can
help promote access to new jobs,...*

“Activation” strategies are essential for ensuring that adequate benefit levels are consistent with strong work incentives (Chapter 4). Such strategies, which include job-search assistance, counselling, training and other re-employment services, are particularly well suited to situations of trade displacement. Indeed, successful adaptation to changing trade patterns requires that labour flows smoothly from declining to expanding industries. For example, the re-integration of displaced workers possessing obsolete skills can be facilitated if adequate re-training programmes can qualify these workers for new jobs at a reasonable cost. Active labour programmes should be designed carefully, however. For instance, it may make sense for many displaced workers, especially older ones, to become re-employed in the same sector – rather than moving into new occupations which would imply a significant retraining investment. This is possible because high labour turnover rates mean that there is considerable hiring, even in declining industries. Earnings losses are also significantly smaller for workers finding a new job in the same industry. In short, training and other intensive measures should be reserved for a relatively small number of individuals for whom job-search assistance alone is inadequate.

Providing the right individualised services for displaced workers is part of the general challenge of designing effective employment services, evaluating their impact, and expanding the provision of programmes which are found to be cost-effective. Good performance management of employment services is key to meeting this challenge (Chapter 5).

*..job-search assistance following advance
notification of job loss can also help...*

The job losses caused by trade shocks are sometimes sufficiently predictable to allow adjustment assistance to begin in advance of workers’ layoffs. The period of advance notification before lay-offs occur, which is often provided by legislation, can provide a breathing space for implementing proactive measures. It is also of value in its own right for giving workers a head start in searching for a new job. Displaced workers receiving advance notification tend to spend less time unemployed than workers

laid-off without any advance warning, and there is also some indication of a positive impact on postdisplacement wages for workers who have received advance notification. Dispatching staff from public employment services to firms where layoffs have been announced, or even creating a public employment office on the premises of the dismissing firm, may be especially helpful.

... and, more generally, well-functioning labour markets should be in place

Assisting displaced workers to find new jobs will be much easier where overall labour market performance is strong. In this respect, ensuring that labour markets are dynamic and that people of working-age have opportunities and incentives to work is more important than ever. The OECD's on-going reassessment of its *Jobs Strategy* should provide a comprehensive framework for achieving this.

In sum, the adjustment costs of globalisation should be acknowledged and addressed by policy

Overall, claims that globalisation is the main cause of the labour market problems experienced by OECD countries are exaggerated. The process through which the gains from open markets occur, however, leads to adjustment costs. And these costs should be acknowledged and addressed mainly by general policy measures that compensate job losers while promoting re-employment chances. Failure to acknowledge the worker adjustment challenges of globalisation, and to implement much-needed reforms, may erode public support for open trade policies.

© OECD 2005

Reproduction of this summary is allowed provided the OECD copyright and the title of the original publication are mentioned.

Multilingual summaries are translated excerpts of OECD publications originally published in English and in French.

They are available free of charge on the OECD Online Bookshop
www.oecd.org/bookshop/

For more information, contact the OECD Rights and Translation unit,
Public Affairs and Communications Directorate.

rights@oecd.org

Fax: +33 (0)1 45 24 13 91

OECD Rights and Translation unit (PAC)
2 rue André-Pascal
75116 Paris
France

Visit our website www.oecd.org/rights/

