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macroeconomía del desarrollo

Job Creation in Latin America in the 1990s: The Foundation for Social Policy

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Santiago, Chile. July 2001

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United Nations Publication
LC/L.1572-P
ISBN: 92-1-121314-2

Sales No.: E.01.II.G.115
Printed in United Nations, Santiago, Chile

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Summary

This paper analyzes labor market trends in Latin America and the Caribbean in the 1990s, arguing that employment must be the foundation of a social policy strategy for the region. The paper begins with a discussion of the expectations for labor market performance that were generated by the reform process in the region. It then provides an overview of what actually happened with respect to participation rates, employment generation, unemployment and wages. It also suggests some reasons why reality was less positive than was expected. Next it examines a new hypothesis about the differential performance of labor markets in the northern and southern subregions. Finally, on the basis of evidence to support the hypothesis, it makes policy recommendations for subregion-specific steps to increase job creation as well as policies relevant for the region as a whole.

I. Introduction

Any effective program of social policies must begin with a strategy for expanding employment. Jobs are the main link between economic and social development. On the economic side, labor is one of the basic factors of production and is increasing in importance, given the central role of human capital for productivity and economic growth. On the social side, for an overwhelming majority of Latin American households, jobs are the principal source of income. Thus, without a sufficient number of jobs that provide the minimum resources necessary to reproduce the labor force and their families, social policies will be overwhelmed by the demand to meet the basic needs of the population. As a consequence, they will be unable to fulfill their appropriate function as a complement to the labor market, both through improving the qualifications of current and prospective workers and providing a safety net for those unable to work. This is the basic premise behind the analysis in this paper.

The paper focuses on the decade of the 1990s, when the new market-oriented economic model had been introduced in the majority of countries. The reforms that led to the new model raised high expectations with respect to employment generation and the resulting positive impact on equity. The first section discusses those expectations and the reasons that the results thus far have been disappointing. The second section examines regional trends in the labor markets according to a series of indicators: participation rates, aggregate employment creation, job creation according to sector and size of firms, and the results of all of these factors in terms of unemployment rates. We also present data on wages and the wage gap between skilled and unskilled workers, which are important links between labor market performance and income distribution. This analysis confirms that the 1990s were a decade of serious problems on the labor front, as jobs grew slowly and unemployment increased. While wages picked up, the wage gap between skilled and unskilled workers also expanded.

The third section of the chapter turns to a recent hypothesis, which suggests that there is a substantial difference in employment creation in the northern and southern parts of the Latin American region. Specifically, it posits that the assembly industries in Mexico and Central America have been more job-intensive than their counterparts in South America, where the leading role has been played by capital-intensive industries that process natural resources. Our data provide support for this hypothesis. Employment (especially industrial employment) grew faster in the north, in part because output was expanding more rapidly. In addition, however, there is evidence that employment elasticities were higher in Mexico and Central America.

Based on the above analysis, the final section provides a set of policy recommendations to improve the employment picture as we move into the new decade. It includes a discussion of the relationship between employment and other social policies and the synergies between them.

II. Reforms and Employment: Expectations versus Reality

In the last ten to fifteen years, the Latin American and Caribbean region has undergone the most significant transformation of economic policy since World War II. Through a series of structural reforms, an increasing number of countries have moved from closed, state-dominated economies to ones that are more market oriented and open to the rest of the world. The reforms included such processes as import liberalization, domestic and international financial liberalization, and privatization. Labor reform has also been part of the agenda, but most changes in this area have been *de facto* rather than *de jure*.[1]

Expectations about the outcomes of the reforms –based largely on a literature from the late 1970s and early 1980s– were very high.[2] The primary focus of this early literature was on raising growth rates through moving from production that was mainly oriented toward the domestic market (through the so-called import substitution industrialization, or ISI, model) to a greater emphasis on exports. Such a shift was expected to result in increased efficiency at the microeconomic level, better exploitation of economies of scale, and moderation of stop-go cycles deriving from foreign exchange shortages.

Of particular interest for our purposes, this literature also argued that removing the distortions caused by the ISI model would generate

[1] There has been some debate about the status of labor market reforms. The IDB (1997) says that very few reforms have been carried out. Weller (2000, chp. 7) argues that substantial changes have occurred, but that they have frequently not been codified into law.

[2] The most important of the early works that argued for structural reforms were those carried out by Anne Krueger (1978, 1981-83) for the National Bureau of Economic Research. The fact that Krueger served as chief economist of the World Bank in the early 1980s gave her opinions a weight well beyond academic circles.

more employment, especially for unskilled workers. Several mechanisms were specified to link the reforms to increased employment. The most basic was that a more efficient allocation of resources would facilitate faster growth, and faster growth would result in more job creation. This would occur even if employment elasticities remained the same, but the elasticities were also expected to be more favorable, owing to a shift in investment and the production structure. Investment and technical change were projected to be more labor intensive, once the alleged biases in favor of capital and against labor were eliminated, in line with the assumption that Latin America's comparative advantage lay in unskilled labor. An increased emphasis on exports would also expand job creation, because exports were thought to be more labor intensive than import-competing products. This last point was consistent with the sectoral analysis, which asserted that agriculture and light industry would be especially favored under a new trade strategy. Finally, it was increasingly argued that if the high costs of hiring workers were lowered, more jobs would be created.

The process of expanding employment was expected to have an additional benefit of improving Latin America's notoriously unequal distribution of income.[3] The most obvious link was through the creation of new low-skill jobs. Insofar as many of these new jobs were created in rural areas, they would help alleviate the greatest pockets of poverty, which were located there. It was also anticipated that the greater demand for unskilled labor would have a positive impact on the relative wages of those who were already employed. That is, the wage differential between skilled and unskilled workers would shrink, thus improving the distribution of income. The gap between profits and wages was also expected to decrease, given some evidence that protection had increased the former at the expense of the latter. Finally, reducing the productive role of the state would free up funds that could be devoted to social expenditure in benefit of poorer groups.

More recently there has been a second wave of literature on the reforms, this time to ask whether the expectations have been fulfilled.[4] A surprising degree of consensus has emerged. The dominant conclusion is that while growth in the 1990s obviously improved in comparison with the "lost decade" of the 1980s, it was quite modest. Moreover, the empirical analyses have generally found that the reforms had a negative impact on employment generation and perhaps on equity. Data indicate that the growth rate of employment was lower in the 1990s than in the last half of the 1980s, unemployment rose, informality increased, and improvement in real wages mainly benefited skilled workers. With respect to the impact of the reforms on equity, there is more controversy. While some argue that the reforms have had a negative impact on income distribution, others find little relationship; none find the positive effect that had been expected.

Why this discrepancy between expectations and reality, especially with respect to employment? Our own previous research suggests several reasons. First, the slower than expected growth rates in the 1990s meant that employment also lagged. Second, the sectoral patterns of investment and growth were such that labor-intensive sectors and firms were among the least dynamic, further depressing the chances for employment growth. Third, participation rates increased in many cases, thus making it harder to keep unemployment under control. And, fourth, the assumption that Latin America's comparative advantage lies in unskilled labor was at least partially wrong. As we will see later, this may have been true for part of the region, but not for all.

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3 While there is no doubt that the proponents believed the reforms would benefit employment, there is more disagreement about whether better income distribution was an explicit goal of the reformers. Balassa and others clearly said that it was (1986, pp. 93-94), as did Krueger (1983, pp.186-87). Williamson specifically excluded it from the Washington Consensus measures, saying that the Washington of the Reagan-Bush years had no interest in the subject (1990, pp. 413-14; 1993, p. 1329). Perhaps Bulmer-Thomas's conclusion that the new economic model was "not primarily adopted" to reduce poverty and improve distribution is the best summary (1996, p. 310).

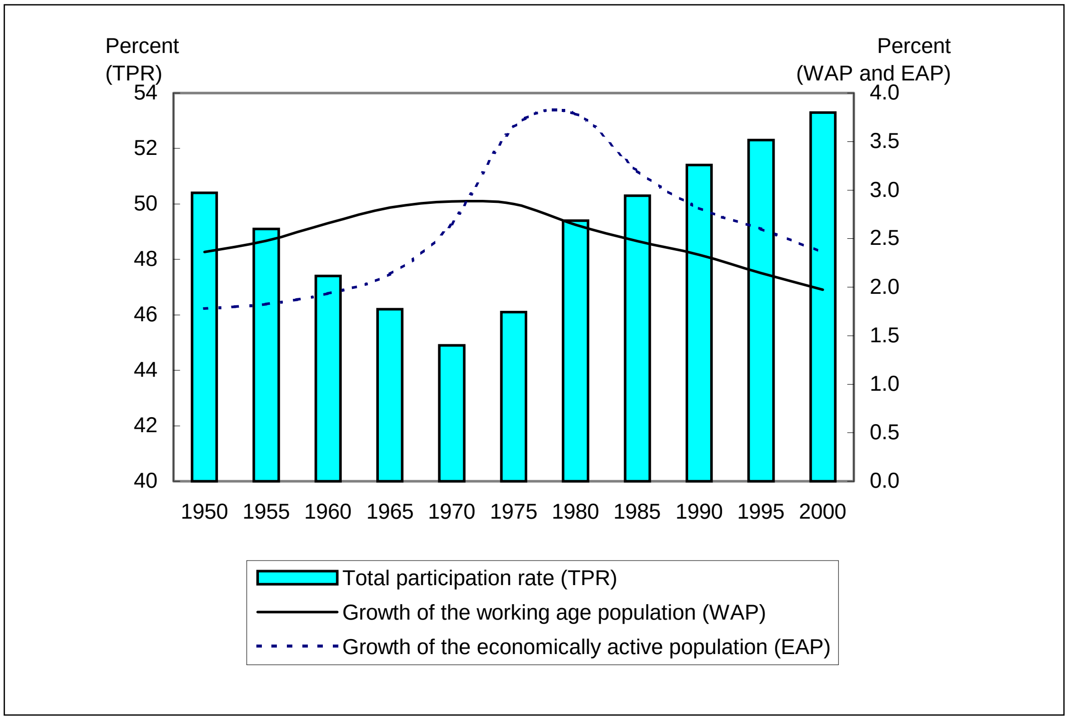
4 We have been involved in a large multi-year project to evaluate the impact of the reforms; see Stallings and Peres (2000), Weller (2000), and Morley (2000). Other important sources include Edwards (1995), Bulmer-Thomas (1996), IDB (1996, 1997), Lora and Barrera (1997), Fernández Arias and Montiel (1997), Londoño and Székely (1997), Burki and Perry (1997), and Berry (1998). Sources particularly concerned with employment are Tardanico and Menjívar (1997), Funkhouser and Pérez Sáinz (1998), Lora and Olivera (1998), Weeks (1999), and various issues of the ILO, *Labor Overview*. For a review of the literature on reforms and employment, see Tuman (2000).

III. Regional Trends in Labor Markets

Labor market performance in Latin America in the 1990s was affected by the reforms as well as by long-term trends in the economies. We expand on the diagnosis sketched out in the previous section by examining labor supply variables, as reflected in participation rates, and then moving to the changing demand for labor as represented by aggregate and sectoral employment creation and by job creation by size of firm. Unemployment trends can be seen as the outcome of these supply and demand pressures. Wage data focus on aggregate trends and the wage differential between skilled and unskilled workers.

Experts agree that long-term trends in employment are determined by changes in the labor supply. Changes in the economically active population (EAP) are explained by changes in the size of the working-age population (WAP) and the extent to which that population decides to participate in the labor market (the total participation rate, or TPR). The latter two variables have followed different trends in Latin America in the postwar period. On the one hand, as the demographic transition proceeded, the annual growth rate of the WAP fell, reducing pressure on the labor market. On the other hand, the degree of labor force participation, which is the outcome of both long-term processes and temporary fluctuations, is still increasing, mainly because of greater female participation. At the same time, other processes worked to reduce participation rates, including urbanization, growth in the education system, and increased coverage of the pension system. This second group of factors meant that people entered the labor force later and retired earlier. As a consequence, the TPR in the region as a whole grew by 0.2 percentage points per year during the 1990s, maintaining the trend of the previous decade. Figure 1 combines the effects of demographic and participation changes to show their impact on the growth of the economically active population, which fell from 2.9 percent in the 1980s to 2.5 percent in the 1990s.[5]

Figure 1
CHANGES IN LABOR SUPPLY, 1950-2000[a]



Source: Weller (2000, p.45).

[a] Based on weighted averages for 20 countries.

The strong correlation between the labor supply and the generation of total employment causes difficulties for the analysis of labor demand and its possible relation to changes brought about by the reforms. To minimize this problem, we concentrate on trends among wage earners, a category more closely related to labor demand. Table 1 illustrates the differences between total employment and wage earners, as well as changes over time; it shows economic growth by decade in the postwar period, creation of total and wage employment, and the respective elasticities. Leaving aside the 1980s, which were clearly atypical,[6] elasticities did not differ significantly in the 1990s from the 1950-80 period. Insofar as the 1990s reflected the impact of the reforms, it can be inferred that the reforms did not affect –either positively or negatively– the quantitative relationship between GDP growth and employment creation. Rather, what stands out in the table for the last decade are lower growth rates, which led to more sluggish employment creation, especially for wage earners.

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5 A complex interplay between demand and supply factors leads to short-term fluctuations around the long-term trend. For instance, increasing unemployment tends to provoke a higher TPR growth rate, as households try to compensate for earning losses by having more family member work. Eventually, however, persisting high unemployment may lead to withdrawal from the labor market by people who lose hope of finding a job, and thus a decreasing participation rate.

6 Especially high elasticities in the 1980s resulted from an increasing labor supply in the face of very slow growth; nonetheless, the EAP was growing more slowly than in the 1970s.

Table 1
EMPLOYMENT GROWTH AND ELASTICITIES, 1950-99[a]
(Annual weighted average)

Period	GDP growth	Growth of employment	Employment elasticity re: output	Growth of wage employment	Wage employment elasticity re: output
1950s	5.1	1.9	0.4	2.5	0.5
1960s	5.7	2.3	0.4	2.7	0.5
1970s	5.6	3.8	0.7	4.7	0.8
1980s	1.2	2.9	2.6	2.4	2.0
1990s	3.2	2.2	0.7	2.0	0.6
1950-99	**4.2**	**2.6**	**0.6**	**2.9**	**0.7**

Source: Authors' calculations, on the basis of official country statistics.

[a] For the 1950s to 1970s, employment growth corresponds to growth of the labor force. From the 1950s through the 1980s, 20 countries are included; for 1990-97, the number is 17.

Below the aggregate level, there were vast differences in the employment trends at the sectoral level during the last decade as seen in table 2. Some represented processes long underway. Thus, the long-term trend of falling employment in agriculture and expanding employment in services accelerated in the 1990s. Likewise, the strong expansion of employment in the manufacturing sector, which came to a halt in the early 1980s and then resumed later in the decade, appears to have come to an end. At the same time, the reforms reinforced many of these trends.

Table 2
EMPLOYMENT GROWTH BY SECTOR, 1990-99[a]
(Percent)

Sector	Employment growth	Contribution to total
Agriculture	-0.4	-4.3
Manufacturing industry	1.2	8.3
Construction	2.8	8.0
Commerce, restaurants, and hotels	4.0	32.7
Electricity, gas and water, transportation, storage, and communications	4.4	10.9
Financial services, insurance, real estate, and business services	6.0	12.3
Social, communal, and personal services	2.7	34.8
Other	-2.3	-2.7
Total	**2.2**	**100.0**

Source: Authors' calculations, on the basis of official country statistics.

[a] Weighted averages for 17 countries.

Between 1990 and 1999, agricultural employment fell by an annual average of 0.4 percent, as demand for labor in the more dynamic activities (generally export agriculture) was not strong enough to offset the loss of employment in the less dynamic ones (especially family farming). The reforms contributed to this process in several ways. Lower import tariffs meant greater competition, at the same time that subsidized credit lines were eliminated. As the cost of agricultural machinery fell, employers substituted equipment for labor.

Manufacturing employment increased in Latin America as a whole in the 1990s, but with an annual growth rate of only 1.2 percent. At the subsectoral level, data for employment in medium-size and large firms show that two simultaneous processes were at work. On the one hand, labor-intensive subsectors lost share relative to more capital-intensive ones. Highly labor-intensive activities such as textiles, garments, leather products, and footwear continued to lose ground within manufacturing in the 1990s, while capital-intensive production of natural resource-based commodities kept the share it had won in the 1970s and 1980s. On the other hand, within subsectors, incorporation of new technologies resulted in layoffs or less employment creation than usual, even in sectors with strong increases in output (e.g., automobiles).

The most dynamic employers were in the services, which explain about 90 percent of new net job creation (see the second column in table 2). The service sector is highly heterogeneous, but two general situations can be identified. First, commerce, restaurants, and hotels, together with social, community and personal services, accounted for 67 percent of all jobs created in the region. Second, financial services, insurance, real estate and business services experienced even faster growth, as did electricity, gas and water, in addition to transportation, storage, and communications. Their small share in total employment, however, meant that these categories contributed only 23 percent of new service-sector jobs.

The economic reforms played an important role in the growth of employment in services, as well as in the polarization that took place within the sector. Although the privatization of electricity and telecommunications was immediately followed by significant layoffs in most countries, it led to the modernization and expansion of those services, which account for their job creation. Similarly, trade liberalization led to the expansion of services related to export-import processes, while financial liberalization led to the introduction of new financial services and to new employment. Finally, pressures to reduce costs led to the outsourcing of service activities previously undertaken within manufacturing firms, which accounts for the strong development of business services. At the same time, however, the low end of the services sector also expanded since this was the main source of jobs for those who could not find work elsewhere.

In addition to sectoral differences, there were also important differences in employment creation by size of firm. According to ILO data, the increase in the number of wage earners in the private sector in the 1990s was concentrated in microenterprises (units with fewer than six workers) and small firms (between six and twenty workers). Jobs in these two categories grew at 3.7 percent between 1990 and 1998 in comparison to 2.3 percent in medium-size and large firms and only 0.7 percent in the public sector (see table 3).

Table 3

GROWTH OF URBAN EMPLOYMENT BY SIZE OF FIRMS, 1990-98[a]

(Percent)

Sector	Annual employment growth rate	Contribution to growth Total	Contribution to growth Formal/Informal
Total	2.9	100.0	
Informal sector	3.9	61.0	100.0
Self employed	3.6	29.0	48.0
Domestic service	5.2	11.0	18.0
Microfirm[b]	3.8	21.0	34.0
Formal Sector	2.1	3.9	100.0
Public sector	0.7		
Private firms	2.6	39.0	100.0
Small[c]	3.6	9.5	25.0
Medium[d]	2.2	12.7	32.0
Large[e]	2.4	16.8	43.0

Source: ILO (1999, p.47).

[a] Weighted average of 12 countries; [b] Less than 6 workers; [c] 6-20 workers; [d] 21-100 workers; [e] More than 100 workers.

The ILO's concept of the informal sector, which has permeated the literature on employment, combines jobs in the microfirm and the non-wage categories.[7] Although the definition of the concept centers on the productivity level of firms, in practice it has been measured by a proxy that groups microenterprises, the self-employed, domestic service, and non-remunerated family members. On this basis, as indicated in table 3, about 60 percent of new jobs in the region were in the informal sector. The idea behind the concept of the informal sector is that this type of job is of low quality, with poor working conditions, low salaries and productivity, and a lack of legal and social protection. Clearly this is not completely true, since both the self-employed and some microenterprises include good jobs. The concept continues to be used, however, because of lack of information on the characteristics of such occupations and the assumption that the majority are indeed precarious.

More precarious yet is the situation of the unemployed, whose presence in Latin America increased, despite higher growth of GDP in the 1990s in comparison to the 1980s. Average unemployment in 1980-90 was 6.6 percent, rising to 7.2 percent between 1991 and 2000.[8] Table 4 shows that with the generalized fall in GDP growth rates in South America in the late 1990s, unemployment reached historic highs in that subregion, surpassing the levels of the debt crisis of the early 1980s. Especially serious problems with unemployment were found in Argentina, Colombia, Uruguay, and Venezuela, where unemployment rose to double-digit rates by 1999.

Table 4

UNEMPLOYMENT RATES, 1980-2000

(Percent)

	1980-90	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000[a]
Latin America	**6.6**	**5.7**	**6.1**	**6.2**	**6.3**	**7.2**	**7.7**	**7.3**	**7.9**	**8.7**	**8.4**
Argentina[b]	5.5	6.5	7.0	9.6	11.5	17.5	17.2	14.9	12.9	14.3	15.1
Bolivia[b]	7.8	5.8	5.4	5.8	3.1	3.6	3.8	4.4	6.1	8.0	7.6
Brazil[b]	5.3	4.8	5.8	5.4	5.1	4.6	5.4	5.7	7.6	7.6	7.1
Chile[c]	11.9	8.2	6.7	6.5	7.8	7.4	6.4	6.1	6.4	9.8	9.2
Colombia[b d]	11.2	10.2	10.2	8.6	8.9	8.8	11.2	12.4	15.3	19.4	20.2
Costa Rica[b]	6.8	6.0	4.3	4.0	4.3	5.7	6.6	5.9	5.4	6.2	5.3
Dominican Republic[c d]	...	19.6	20.3	19.9	16.0	15.8	16.5	15.9	14.3	13.8	13.9
El Salvador[b]	9.3	7.9	8.2	8.1	7.0	7.0	7.5	7.5	7.6	6.9	6.7
Guatemala[c]	8.0	4.2	1.6	2.6	3.5	3.9	5.2	5.1	3.8	...	...
Honduras[b]	9.7	7.4	6.0	7.0	4.0	5.6	6.5	5.8	5.2	5.3	...
Mexico[b]	4.3	2.7	2.8	3.4	3.7	6.2	5.5	3.7	3.2	2.5	2.2
Nicaragua[c]	5.3	11.5	14.4	17.8	17.1	16.9	16.0	14.3	13.2	10.7	9.8
Panama[b d]	14.5	19.3	17.5	15.6	16.0	16.6	16.9	15.5	15.2	14.0	15.2
Paraguay[b]	5.6	5.1	5.3	5.1	4.4	5.3	8.2	7.1	6.6	9.4	8.6
Peru[b]	7.4	5.9	9.4	9.9	8.8	8.2	8.0	9.2	8.5	9.2	8.5
Uruguay[b]	8.9	8.9	9.0	8.3	9.2	10.3	11.9	11.5	10.1	11.3	13.6
Venezuela[c]	9.3	9.5	7.8	6.6	8.7	10.3	11.8	11.4	11.3	14.9	13.9

Source: ECLAC, on the basis of official country statistics.

[a] Preliminary figures; [b] Urban areas; [c] Total nationwide; [d] Includes hidden unemployment.

The other side of the labor market equation involves remunerations. Average real wages in the formal sector in Latin America as a whole improved during the 1990s or at least held their own. Nevertheless, in some countries, including Argentina, Mexico, Nicaragua, Peru and Venezuela, wages in the year 2000 were lower than in 1980 (see table 5). In many countries real wages were quite volatile. In some cases (for example, Bolivia, Colombia and Costa Rica), real wages fell at the beginning of the 1990s but then recovered. Mexico and Peru experienced the opposite trend, with an early increase followed by declines; in the Mexican case, this trend was clearly the result of the 1994-95 financial crisis. Only Chile had continuous increases throughout the decade.

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7 See Mezzera (1990) on the informal sector as seen by the ILO.
8 This numbers refer to the weighted average of 17 countries. The simple average rose from 8.3 to 8.6 percent.

Table 5

AVERAGE REAL WAGES IN THE FORMAL SECTOR, 1980-2000

(1990=100)

	1980	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000[a]
Argentina[b]	128.8	99.1	100.4	101.7	100.4	101.1	100.0	99.9	99.3	99.0	100.1	101.6
Bolivia[c]	57.6	87.6	82.1	85.5	91.2	98.5	100.0	100.5	106.6	110.1	117.0	118.0
Brazil[d]	94.6	104.4	88.9	87.0	95.5	96.3	100.0	107.9	110.7	110.8	105.9	104.8
Chile[e]	77.2	80.9	84.9	88.7	91.8	96.1	100.0	104.1	106.6	109.5	112.1	113.7
Colombia[f]	80.7	94.9	92.4	93.5	97.9	98.8	100.0	101.5	104.2	102.8	105.9	110.0
Costa Rica[g]	104.0	89.8	85.6	89.2	98.3	102.0	100.0	97.9	98.7	104.3	109.2	110.1
Ecuador[h]	88.3	65.4	68.4	74.2	83.5	90.9	100.0	105.4	103.0	98.9	90.7	86.4
Guatemala[g]	88.7	77.1	72.1	82.9	88.8	89.3	100.0	109.7	112.7	116.8	123.5	128.2
Mexico[b]	113.1	88.1	93.8	100.7	109.7	114.9	100.0	90.1	89.1	91.5	92.4	98.0
Nicaragua[i]	390.8	81.8	84.5	100.5	93.3	98.2	100.0	97.9	97.7	104.9	109.6	111.3
Paraguay[j]	89.5	87.7	91.8	90.9	91.7	93.0	100.0	103.1	102.6	100.7	98.6	99.9
Peru[k]	265.0	85.7	98.7	95.2	94.4	109.2	100.0	95.2	94.5	92.7	90.7	91.8
Uruguay	99.5	91.7	95.2	97.3	102.0	102.9	100.0	100.6	100.8	102.7	104.3	102.9
Venezuela[l]	302.4	138.1	130.1	136.5	124.4	104.8	100.0	76.7	96.3	101.5	96.8	90.5

Source: ECLAC, on the basis of official country figures.

[a] Preliminary figures; [b] Manufacturing industry; [c] Private sector in La Paz. The figure shown in the column for 1980 refers to 1985; [d] Workers covered by social and labor legislation in six metropolitan areas. Average for 1980 for Rio de Janeiro and São Paulo; [e] Until April 1993, non-agricultural wage earners. Since May 1993, the general hourly wage index is used; [f] Workers in the manufacturing sector; [g] Average declared wages of workers covered by the social security system; [h] Non-agricultural enterprises with 10 or more employees. The figures shown in the column for 1980 refers to 1985; [i] Averages wages, not including payment in kind or other benefits; [j] Asuncion; [k] Private sector workers in Lima; [l] Urban non-manual and manual workers; second half of each year. The figure shown in the column for 1980 refers to 1982.

Theory tells us that there should be a tradeoff between wages and volume of employment created. On the surface, this does not appear to have occurred during the 1990s. That is, wages rose nearly everywhere, but both employment and unemployment behavior varied widely across countries.[9] One hypothesis is that regional labor markets are far from equilibrium, but a proper analysis of this topic would require better data than are currently available. Sectoral-level data are particularly important, since labor markets in Latin America tend to be heavily segmented by sectors as well as by other characteristics.

In addition to average wages, it is also important to analyze what happened to the remunerations of different categories of workers. The literature suggests the wage differential is a key link between labor markets and income distribution.[10] The aim is to study the divergence (if any) in trends between the wages of high- and low-skill workers. This can be operationalized in several ways; the most common is by educational level. Table 6 compares two versions of an education-based wage gap for eight countries during the 1990s: (1) the difference between wages for workers with university education and those with the average remuneration level of the sample, and (2) university graduates versus those with 7-9 years of schooling (the equivalent of complete primary education, or perhaps a bit more depending on the educational structure of each country). The second method generally resulted in a larger differential. An increase in the differential is found in all cases except Costa Rica, although it is small in Argentina and negligible in Brazil.

9 Econometric analysis in Weller (2000, chps. 4 and 5) shows a negative relationship between employment creation and real wages, but the coefficient is not significant.

10 Bulmer-Thomas (1996); ECLAC (1997); IDB (1998); Morley (2000).

Table 6
WAGE DIFFERENTIALS BY EDUCATION LEVEL, 1990s[a]
(Percent)

Country (period)	University graduates vs. average wage: Initial year[b]	Final year[b]	University graduates vs. 7–9 years of education: Initial year[b]	Final year[b]
Argentina (1991–97)	164.3	169.6	218.3	227.9
Bolivia (1989– 96)	235.0	292.9	251.8	506.4
Brazil (1992–97)	380.2	383.5	553.2	553.3
Chile (1990–96)	231.6	247.9	366.1	448.6
Colombia (1988–95)	222.2	261.6	276.7	327.2
Costa Rica (1990–96)	285.0	273.2	323.1	316.7
Mexico (1991–97)	182.1	232.1	160.1	302.2
Peru (1991–97)	220.7	275.0	321.0	403.1
Median	**226.9**	**267.4**	**298.9**	**365.2**

Source: Weller (2000, p. 167).

[a] Ratio of average wages of specified groups; [b] Initial and final year of period indicated for each country.

Another way to operationalize the wage differential is to compare results for white-collar and blue-collar workers. Data are available for a number of countries including Chile, Colombia, Costa Rica, Mexico, and Peru. Almost all cases show the same pattern as that embodied in the educational comparisons: white-collar workers received larger wage increases than have blue-collar workers, again with the exception of Costa Rica.[11] Finally, there is a gap between the wages of workers in large and small firms, whereby the latter have risen more slowly than the former.[12] While more difficult to interpret, this third gap may also include some elements of a skill differential.

A widening gap in wages based on skill level is the opposite of what proponents of the reforms expected. Theoretical analysis would point to relative prices favoring cheaper capital over more expensive labor as the main cause of the phenomenon. This change in relative prices would lead to a substitution of labor by capital and thus a higher capital-labor ratio. According to data gathered by Morley for nine countries, however, relative price trends did not manifest themselves in any consistent pattern with respect to the capital-labor ratio. The ratio rose in the 1990s in Brazil, Chile, Costa Rica, and Mexico, fell in Argentina, Bolivia, and Peru, and remained about the same in Colombia and Jamaica.[13]

If relative prices do not explain the widening wage gap, one alternative is firm restructuring. For example, restructuring that involved increased use of outsourcing for services could lead to the concentration of skilled employment in the firm itself, while less skilled occupations, such as catering, cleaning, and security services, are contracted out. This could explain why the wage gap between small and large firms increased during the 1990s.[14] Another explanatory factor is the expansion of tertiary activities, which are on average more intensive in skilled labor, and the reduction in the weight of the primary and secondary sectors, which are relatively more intensive in unskilled labor. Even more important than sectoral restructuring, the strong relative demand for highly skilled labor was caused by processes of internal upgrading of the service sector, especially in community and social services, as well as in finance and business services. Finally, the political economy of the labor market provides another explanation: the declining strength of unions probably played a role in some countries, since less-skilled workers were less likely to be represented by labor unions, as did policy with respect to the minimum wage, which has frequently been allowed to lag with respect to the average wage.

11 García-Huidobro (1999); Ramírez and Núñez (1999); Montiel (1999); López (1999); Saavedra and Díaz (1999).
12 Weller (2000, p. 181).
13 Morley (2000, pp.99-102).
14 Of course, there is also outsourcing of skilled jobs.

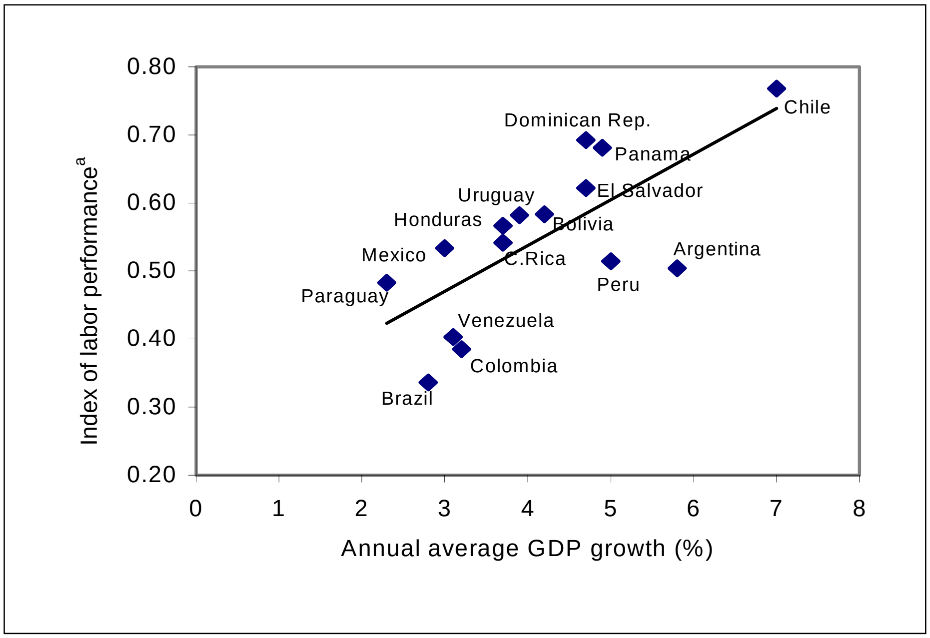
IV. Divergences between North and South

While overall employment trends in Latin America and the Caribbean were problematic during the 1990s, it is clear from the tables in the previous section that there were important differences among countries. To some extent, these differences were due to economic performance, as countries with higher growth rates generally also saw a better performance on the labor markets. Figure 2 shows the relationship between GDP growth rates and an index for labor market performance for 15 Latin American countries during the period 1990-98.[15] Strong growth performers generally showed better results in terms of employment, unemployment, and wages.

Chile was the country with the highest economic growth rate, which had a positive impact on all four variables in the index, such that the country showed the best labor market performance. At the other extreme, the worst labor market performer was Brazil, the country with the second lowest annual growth rate. The employment rate in Brazil fell sharply, which led to growing unemployment despite a decline in labor supply. Argentina was an outlier insofar as a high economic growth rate did not lead to an improvement of the labor market situation. Although the number of wage jobs increased, the overall employment rate fell – especially after the Mexican financial crisis began to affect Argentina– and, exacerbated by a higher labor supply, unemployment rates at the end of the 1990s greatly exceeded those at the beginning of the decade.

[15] The index is an average of four subindexes that summarize the countries' performance in terms of unemployment, real wages, employment generation, and the growth of wage jobs compared to general job growth (as an indicator of labor demand). The best and worst performers on each variable are assigned the value of 1 and 0 points, respectively.

Figure 2
ECONOMIC GROWTH AND LABOR MARKET PERFORMANCE, 1990-98



Source: Authors' calculations.

[a] See text for construction of index.

Beyond growth differentials, however, it has been suggested that another phenomenon is also at work. ECLAC has put forward the hypothesis that a structural difference is beginning to emerge in the region, whereby the northern tier of countries (Mexico, Central America, and perhaps the Caribbean) are tied into the United States economic area through production of traditional industrial goods (especially textiles) and more high-technology items (electronic products and autos). In the case of the smaller countries of the subregion, these ties have been fostered through assembly firms (*maquiladoras*); in Mexico there is greater diversity of production relations. In South America, by contrast, the main source of economic dynamism has come from the sectors based on processing natural resources for Europe and other markets. Major examples include steel, petrochemicals, paper and pulp, and processed food items. Other industrial products have been centered on the subregional market, especially Mercosur.[16]

Categorizing the types of products that are involved in the two subregions according to their dynamism in the world market, another difference appears such that the products of the northern group are more dynamic, while those produced by the southern group are less so. This difference can be demonstrated by using a software program developed by ECLAC, which sorts countries into four groups according to their export performance: those whose main exports gain market share in dynamic sectors (rising stars), gain share in lagging sectors (falling stars), lose share in dynamic sectors (lost opportunities), or lose share in lagging sectors (retreat). Table 7 uses these categories to characterize Latin American and Caribbean countries. While Mexico and the Central American group are mainly in the "rising star" quadrant, the South American countries are mostly "falling stars."

[16] ECLAC (2000b, vol. 1, chp. 1; vol. 3, chp. 3); see also Katz (2000).

Table 7

CHARACTERISTICS OF COUNTRIES' EXPORTS TO THE OECD, 1980-96[ab]

	Increasing market share	Decreasing market share
Dynamic products	**"Rising stars"** Dominican Republic (76.0%) Mexico (71.8%) Honduras (62.3%) Salvador (54.5%) Costa Rica (46.1%) Guatemala (42.5%)	**"Lost opportunities"** Haiti (68.2%)
Non-dynamic products	**"Falling stars"** Paraguay (71.6%) Venezuela (62.0%) Ecuador (58.6%) Chile (54.9%) Uruguay (52.9%) Argentina (48.2%) Colombia (44.4%) Bolivia (43.0%) Brazil (37.7%)	**"Declining competitiveness"** Suriname (64.5%) Nicaragua (48.8%) Guyana (47.3%) Peru (46.0%) Panama (44.7%)

Source: ECLAC (2001b, p.135).

[a] The countries are located in the quadrants that correspond to over 40% of the total value of their merchandise exports to the OECD; [b] The figures in parenthesis are the percentage of the sales of the products indicated in the quadrant with respect to total exports to the OECD.

Important for our purposes is an additional aspect of this alleged dichotomy: the *maquila*-based production is said to be very labor-intensive, while the production of nature resource-based “commodities” is more capital intensive. These different factor proportions have obvious implications for job creation. We want to begin an explore this idea of differential job creation. Since the data at hand are quite limited, both in terms of quantity and quality, the analysis that follows should only be considered as an initial step.

Table 8 presents some basic data on the relative performance of the two subregions. While certain commonalties characterize both north and south –especially the dominance of services as a source of job creation– two difference emerge very clearly. First, aggregate employment grew nearly twice as fast in the northern tier countries as in the south (3.6 percent and 1.9 percent, respectively). Employment growth was also stronger in the north, or declines less severe, in every individual sector. These differences are linked to the positive relationship between job growth and labor supply dynamics, i.e., the higher growth rate of the working age population in the northern tier. A second difference emerging from the table is more relevant to labor demand. That is, employment in manufacturing in the northern countries grew at an annual average rate of 4.3 percent, faster than employment as a whole, and accounted for 13 percent of all jobs created in those countries. In the southern tier, by contrast, the manufacturing sector was shedding jobs (an average annual contraction rate of 0.1 percent).

Of course, there was also variation among countries; not all conformed to this pattern. In the southern hemisphere, for example, Bolivia and Paraguay saw rapid employment creation, both in the aggregate and in manufacturing. As we will see below, however, these jobs tended to be in the self-employment category rather than as wage earners. Within the northern group, Costa Rica lagged its neighbors in job creation. Nonetheless, the subregional differences are significant and pose important problems for the southern countries. A net loss of industrial jobs occurred in five of nine cases (Argentina, Brazil, Colombia, Peru, and Uruguay), while most saw aggregate employment trends that were clearly unsatisfactory, even in quantitative terms.

Table 8

GROWTH AND CONTRIBUTION OF EMPLOYMENT BY SECTOR, 1990s[a]

(Percent)

Country/ period	Agric-ulture	Manufac-turing	Construc-tion	Com-merce[b]	Basic services[c]	Financial services[d]	Social services[e]	Other	Total
Argentina	…	-3.1	1.0	0.3	4.0	4.9	3.0	…	1.4
1991-99	…	-46.6	5.5	4.7	36.5	37.1	62.9	…	100.0
Bolivia	…	8.8	10.2	9.9	7.2	12.8	-0.3	-7.0	5.4
1990-97	…	29.4	14.7	47.5	11.8	9.1	-1.5	-7.4	100.0
Brazil	-0.9	-0.2	2.4	2.8	3.0	5.6	2.6	-1.4	1.3
1992-99	-18.0	-1.6	11.5	26.8	8.4	14.0	62.4	-3.6	100.0
Chile	-1.5	0.4	3.1	3.0	3.0	7.7	2.5	-3.4	1.9
1990-99	-12.9	3.2	11.4	29.1	12.8	24.1	35.7	-3.5	100.0
Colombia	-0.5	-1.4	0.7	2.1	2.3	5.0	2.8	-6.6	1.1
1991-99	-11.8	-17.4	3.0	40.7	12.1	18.7	61.0	-6.2	100.0
Costa Rica	-0.3	1.2	2.5	6.0	5.9	7.6	3.0	0.0	2.8
1990-99	-2.6	7.4	5.9	38.6	12.5	11.1	27.0	0.0	100.0
Dom. Republic	1.6	3.1	14.4	6.3	6.0	-5.4	1.1	-17.0	3.5
1991-99	8.9	15.6	19.5	42.7	12.1	-2.9	7.6	-3.6	100.0
El Salvador	-2.3	5.0	7.2	9.1	6.0	21.0	3.4	7.1	3.9
1992-99	-8.1	10.7	4.4	23.0	3.2	5.4	8.0	0.1	100.0
Honduras	2.5	7.3	4.9	7.8	3.6	10.9	5.2	-2.7	4.9
1990-99	19.9	22.3	4.9	29.5	2.0	3.7	17.9	-0.2	100.0
Mexico	0.0	5.1	1.8	4.3	5.1	5.6	3.8	-0.6	3.1
1991-99	0.2	28.8	3.4	26.4	7.5	6.0	28.1	-0.4	100.0
Panama	-1.6	3.7	15.4	5.6	4.0	9.7	3.1	12.2	3.7
1991-99	-9.6	9.6	20.8	32.4	9.0	13.6	23.4	0.8	100.0
Paraguay	2.8	4.9	0.5	10.4	7.8	…	8.4	-32.7	5.2
1992-99	17.6	11.7	0.6	35.3	6.5	…	37.2	-8.9	100.0
Peru	…	-0.1	7.4	5.7	10.8	12.3	0.2	…	3.8
1990-97	…	-0.6	9.9	44.1	16.5	16.5	1.7	…	100.0
Uruguay	…	-4.0	1.8	0.4	1.0	2.9	-0.7	1.1	-0.5
1990-99	…	-138.3	23.7	12.2	12.0	29.6	-29.6	11.5	100.0
Venezuela	1.0	2.0	3.9	6.0	4.2	2.3	3.4	-0.8	3.5
1990-99	3.2	8.4	8.5	39.8	8.8	3.8	27.7	-0.2	100.0
Latin America	**-0.3**	**1.2**	**2.8**	**4.0**	**4.4**	**6.0**	**2.8**	**-2.1**	**2.2**
(weighted avg.)	**-4.1**	**8.3**	**7.8**	**32.7**	**10.8**	**12.3**	**34.8**	**-2.4**	**100.0**
Latin America	**-0.1**	**1.6**	**2.8**	**5.8**	**4.1**	**6.6**	**3.0**	**-1.1**	**3.5**
(median)	**-1.2**	**9.6**	**5.9**	**32.4**	**8.8**	**8.6**	**33.4**	**-0.3**	**100.0**
Northern tier	**-0.1**	**4.3**	**6.0**	**6.1**	**5.5**	**8.6**	**3.3**	**-0.3**	**3.6**
(median)	**-1.2**	**13.2**	**5.4**	**30.9**	**8.2**	**5.7**	**27.6**	**-0.1**	**100.0**
Southern tier	**-0.5**	**-0.1**	**3.1**	**5.7**	**4.2**	**6.7**	**3.3**	**-3.4**	**1.9**
(median)	**-11.8**	**-0.6**	**9.9**	**35.3**	**12.1**	**17.6**	**48.3**	**-3.5**	**100.0**

Source: Authors' calculations, based on official country statistics.

[a] The first line for each country refers to the annual growth of employment during the period indicated. The second line shows the contribution of each sector to total employment generated during the period. The data refer to the national total, except for Argentina (urban areas), Bolivia (departmental capitals and El Alto), Peru (Metropolitan Lima) and Uruguay (urban area). Note that the rows for Latin America, Northern tier, and Southern tier do not sum to the totals because they represent the medians of the columns; [b] Includes restaurants and hotels; [c] Electricity, gas and water, and transport, storage and communications; [d] Includes insurance, business services and real estate; [e] Includes community and personal services.

Another way that job creation has differed in the two subregions is according to type of employment. That is, table 9 breaks down total employment creation into five categories: wage earners, self-employed, domestic service, non-remunerated family workers, and others.[17] For the northern countries, the fastest growing job category was wage earners (an annual average rate of

[17] Note that tables 8 and 9 have different totals for some countries, given different data sources and thus time periods.

4.2 percent), which accounted for two thirds of all new jobs. In the south, wage jobs grew by only 1.8 percent per year, representing less than half of new employment. The alternative was self-employment, which increased faster in the south than the north (4.0 percent and 3.6 percent, respectively), despite the overall faster employment growth in the latter. As a share of total employment creation, self employment represented 27 percent in the north compared to 37 percent in the south. Referring back to the discussion in the previous section, the difference in the importance of wage jobs is associated with differences in labor demand, which was increasing more rapidly in the north.

Table 9

GROWTH AND CONTRIBUTION OF EMPLOYMENT BY TYPE OF JOB, 1990s[a]

(Percent)

Country/ period	Wage earners	Self employed	Domestic service	Unpaid family workers	Others	Total
Argentina	1.8	-1.0	2.3	…	0.9	1.1
1991-97	100.7	-20.0	14.7		4.5	100.0
Bolivia	4.7	5.5	-2.9	11.6	16.1	5.5
1990-97	41.4	34.7	-2.8	12.3	14.4	100.0
Brazil	1.1	1.5	3.8	-1.9	3.1	1.2
1992-97	49.0	34.2	22.5	-15.7	10.0	100.0
Chile	3.3	2.4	-0.6	-1.9	0.2	2.5
1990-1997	84.1	22.4	-1.4	-15.7	0.3	100.0
Colombia	1.1	4.0	0.1	-7.5	-1.4	1.4
1991-97	43.8	92.3	0.2	-31.3	-5.0	100.0
Costa Rica	2.7	2.8	2.8	-4.4	7.8	2.7
1990-97	64.6	20.0	4.4	-6.7	17.7	100.0
Dom. Republic	3.6	0.8	…	8.0	-2.0	1.9
1991-96	79.3	14.5		12.7	-6.4	100.0
El Salvador	5.8	3.1	3.5	-1.9	-4.4	3.4
1992-97	83.6	26.3	4.4	-5.1	-9.2	100.0
Honduras	4.4	4.9	4.2	3.8	15.8	4.8
1990-97	40.6	38.1	3.5	9.9	7.9	100.0
Mexico	4.0	4.0	8.4	3.0	-5.9	3.4
1991-97	62.7	28.2	9.1	11.3	-11.2	100.0
Panama	5.0	5.0	4.0	-2.3	-13.1	4.0
1991-97	70.8	36.6	5.8	-2.4	-10.7	100.0
Paraguay	2.9	6.3	8.5	20.4	11.5	6.3
1992-97/98	19.6	37.2	8.9	25.5	8.8	100.0
Peru	1.7	5.3	1.7	…	…	3.8
1991-97	18.4	81.0	0.6			100.0
Uruguay	0.8	1.6	…	-0.3	-2.0	0.8
1991-97	77.0	37.8		-0.5	-14.3	100.0
Venezuela	2.7	8.2	…	-10.0	0.2	3.8
1990-97	46.8	57.5		-4.6	0.3	100.0
Latin America	**2.2**	**2.2**	**3.0**	**3.8**	**0.2**	**2.2**
(weighted avg.)	**52.7**	**38.2**	**9.1**	**-0.4**	**0.4**	**100.0**
Latin America	**2.7**	**4.0**	**3.2**	**-1.9**	**0.2**	**3.4**
(median)	**62.1**	**34.7**	**3.5**	**-1.5**	**0.3**	**100.0**
Northern tier	**4.2**	**3.6**	**4.0**	**0.6**	**-3.2**	**3.4**
(median)	**67.7**	**27.5**	**4.4**	**3.7**	**-7.8**	**100.0**
Southern tier	**1.8**	**4.0**	**1.7**	**-1.9**	**0.6**	**2.5**
(median)	**46.8**	**37.2**	**0.2**	**-2.6**	**2.4**	**100.0**

Source: Authors' calculations, on the basis of official country statistics.

[a] The first line for each country refers to annual employment growth during the period indicated; the second line shoes the contribution of each category to the total employment generated during the period. Note that the rows for Latin America, Northern tier, and Southern tier do not sum to the totals because they represents the medians of the columns.

The differences in labor demand brings us back to the relationship between GDP growth and growth of employment. Figure 2 showed that labor market performance was positively correlated with GDP growth rates, but the southern countries as a whole did less well than would have been predicted by expansion of GDP. Thus, most (but not all) of the southern countries are below the regression line in figure 2, while all of the northern countries are above.

Another way of exploring the relationship between growth and employment creation in the various countries and subregions is to calculate employment elasticities. Table 10 presents the data for the region in the 1990s, which provide additional support for the hypothesis about a structural difference in north and south. While the median elasticity for the 15 countries as a whole is 0.79 (meaning that for every 1 percent increase in output, employment grows by 0.79 percent), the figure is 0.52 for the southern countries compared to 0.83 in the north. The message is that growth appears to have been more labor intensive in the northern tier. This helped to create jobs above and beyond the fact that growth itself was more rapid in the north during the 1990s.

Table 10

GDP GROWTH RATES AND EMPLOYMENT ELASTICITIES, 1990s

Country	**GDP growth rate**	**Employment elasticity**[a]
Argentina	4.7%	0.30
Bolivia	4.0	1.35
Brazil	2.5	0.52
Chile	6.2	0.31
Colombia	2.6	0.42
Costa Rica	5.2	0.54
Dominican Republic	5.0	0.70
El Salvador	4.5	0.87
Honduras	3.0	1.63
Mexico	3.2	0.97
Panama	4.7	0.79
Paraguay	2.1	2.48
Peru	4.6	0.83
Uruguay	5.0	-0.17
Venezuela	2.0	1.75
Latin America (median)	**4.5**	**0.79**
Northern tier (median)	**4.6**	**0.83**
Southern tier (median)	**2.9**	**0.52**

Source: ECLAC (2000a, p.66) for GDP growth rates; Table 8 of this chapter for employment growth.

[a] Elasticities are calculated as employment growth rate divided by GDP growth rate.

The meaning of these elasticities, however, must be interpreted with care. As can be seen in the table, some (in both north and south) are very high. In particular, Bolivia, Honduras, Paraguay, and Venezuela all have elasticities above 1.00. With the partial exception of Bolivia, these cases represent situations where supply pressures have outstripped the economies' capacity to create jobs in the face of low GDP growth rates. As a consequence, work was "created" through self employment and other informal sector activities, rather than the economic models being especially labor-intensive.

Since we showed earlier that manufacturing was central to the difference in employment creation across the two subregions, and since the *maquila* is hypothesized to play an important role in explaining the differences within industry, we close this section by looking at the *maquila* per se. Table 11 shows just how important this type of firm has been. Indeed, during the 1990s, it was the only type of manufacturing with noteworthy employment growth.[18] In some countries, especially Mexico and the Dominican Republic, there were already an important number of jobs in these plants at the beginning of the 1990s, but the main expansion took place during that decade. By 1999, *maquila* jobs represented from 10 to 40 percent of total manufacturing jobs in the sample of northern countries shown in the table. Likewise, they accounted for up to 48 percent of formal-sector manufacturing jobs. Since these jobs depend on exports to the United States, the recent dynamism of the U.S. market was a crucial factor in the *maquilas'* growth, and it remains to be seen how they will fare under less favorable circumstances.

Table 11

EMPLOYMENT IN THE *MAQUILA* SECTOR, 1990-99

	Employment in *maquila* (in thousands)			Employment in *maquila* as % of employment in manufacturing (1999)	
Country	**1990**	**1996**	**1999**	**Total**	**Formal**
Costa Rica	33	48	…	25[a]	36[a]
Dominican Republic	130	164	191	37	…
El Salvador	2	38	45	11	
Guatemala	45	62	…	…	48[a]
Haiti	…	20	…	…	…
Honduras	18	76	120	32	…
Mexico	446	779	1197	16	28
Nicaragua	0	8	20	16	36

Source: Authors' calculations, on the basis of official country statistics.

[a] 1996.

The dynamic job generation in the *maquila* sector did not mean that the northern subregion's traditional industries were exempt from the strong impact that trade liberalization and modernization had on manufacturing employment in the southern part of the region. In Mexico, just as in countries like Argentina and Brazil, labor intensive industries such as textiles and leather products were hurt by growing imports, and the number of jobs in non-*maquila* industries declined more than 10 percent between 1990 and 2000, in spite of a certain reactivation since 1997.[19] Given these common tendencies, the *maquila* industries are the main reason that manufacturing jobs rose in the northern subregion, while they shrank in the south.

Maquila industries have frequently been accused of non-compliance with basic labor standards, such as the right to organize, and of bad working conditions, as well as of a low impact on social and economic development.[20] There is, however, an important differentiation going on among *maquila* enterprises, and no generalizations can easily be made. We will return to the *maquila* and the critiques that have been made in the final section of the chapter.

18 See ECLAC (1997, p. 93; 2001a, chp. 3).
19 Weller (2000, chp. 5); ECLAC (2001a, chp.3).
20 See, for example, ILO (1996, pp. 34-35). For a more extensive discussion of the *maquila*, including both their advantages and disadvantages, see Buitelaar, Padilla, and Urrutia (1999) and Buitelaar and Padilla (2000).

V. Policy Recommendations

Important problems remain with respect to growth, investment, and productivity in Latin America, but progress was made in these areas in the 1990s compared to the 1980s. Problems involving employment and equity, in contrast, were exacerbated. Employment creation was slow, and job quality deteriorated. Inequality probably increased. Governments need to develop policies specifically aimed at these areas. The evidence presented about differences in employment generation in the northern and southern parts of the region suggests that –to some extent– policies need to be tailored to match specific subregional characteristics.[21]

For the region as a whole, a general policy consideration concerns the need for more robust growth as part of a strategy to speed up job creation. Indeed, achieving high, stable growth rates is a necessary prerequisite for lowering both unemployment and inequality. The type of growth is also important. With the new development model in place in Latin America, the private sector must take the lead in investment, but governments can offer incentives to increase the labor intensity of growth. For example, an emphasis should be given to infrastructure construction, which has the double advantage of improving countries' competitiveness and creating a substantial number of jobs. The use of concessions, as an extension of the privatization process, is a useful instrument in this regard.

[21] This section is drawn from Stallings and Peres (2000, chp. 7) and Altenburg, Qualmann, and Weller (2001). Other policy recommendations with respect to improving the employment situation are found in IDB (1996), Edwards and Lustig (1997), and Tokman and Martínez (1999).

With respect to the situation of the northern subregion, the *maquila* has an important potential to improve the performance of the labor market in both quantitative and qualitative terms. Already important differences can be observed among *maquila* plants, concerning technology, human capital requirements, labor code compliance, and so on. These differences show that there are possibilities for development with positive consequences for labor.

A broad acknowledgement of this potential would help to overcome the sterile confrontation between critics of prevailing bad working conditions in the *maquila* sector and advocates who insist that most *maquila* workers do not have a satisfactory alternative to their present jobs. It is true that, since the *maquila* plants are formal-sector jobs, they are likely to offer some benefits when compared to informal activities. At the same time, poor working conditions and the denial of the right to organize are frequent characteristics of these plants. A combination of external pressure concerning the compliance of basic standards (e.g., the commitment to codes of conduct and the establishment of seals of social quality), and internal actions to guarantee the right to organize and the compliance of national labor laws could lead to an upgrading of working conditions without endangering the competitiveness of *maquila* plants.

The labor performance of the *maquila* sector could also be improved by a process that gradually transforms the basis of its competitive advantage from low factor costs to knowledge, a tendency already observable in some productive networks, especially across the U.S.-Mexican border and in Costa Rica. Another improvement would involve stronger integration into the national production structure, by establishing links with small and medium-size enterprises. In addition to legal reforms, this obviously requires an increase of the competitiveness of national suppliers.

In South America, the *maquila* is less relevant; more important is support for small firms to complement the capital-intensive production structure that currently dominates. In thinking about employment policies for these units, it is important to distinguish small and medium-sized enterprises from microfirms. The former usually have economic potential, so the question becomes how to improve their competitiveness. While the same is also true for some microfirms, most of them are more a reflection of the basis needs of survival rather than undertakings with a potential for improving labor conditions. Therefore, in the long run the workers in the large majority of these units need to receive more educational preparation and training so that they can find more attractive job opportunities elsewhere in the economy.

Two approaches to improving conditions for small firms have been tried in other world regions that may provide useful insights for policy makers in Latin America. First is the idea of economic “clusters” that are geared toward lowering the costs of services for small firms. Among the most successful examples are the cases in northern Italy. Credit operations are particularly costly when negotiations must be carried out with a great many small units; a collective approach to credit has proved viable, even for microenterprises (for example, the Banco del Sol in Bolivia or the Grameen Bank in Bangladesh). This approach has also proved useful for small agricultural producers. In addition to credit, clusters can be useful for lowering the cost of other inputs as well as for marketing.

A second approach to the creation of productive jobs in small and medium enterprises is the establishment of supplier relations with larger firms. These links create a situation where it is in the interest of the larger firms to help raise the competitiveness of their small-scale suppliers, especially in the areas of information, technology, training, and finance. In several Asian countries, including Japan, supplier relations have substantially improved the viability of small firms, although the latter tend to bear the brunt of adjustment when times are bad. A variant of this approach is the contracting model, whereby international marketing companies obtain their products from firms that produce to their specifications. Latin America has many examples of these arrangements, some of which are more successful than others.

An alternative proposal put forth by some experts on how to increase job opportunities throughout the region is through flexibilization of the labor market more generally.[22] Our view is that labor markets are already much more flexible than usually perceived. We are also concerned about jumping into drastic reform without adequate information on the likely consequences, with respect to both new jobs and the quality of existing jobs. A generic solution is particularly inappropriate given the extreme differences among labor markets in the region.

Policymakers would be better advised to think about ways to improve the functioning of labor markets rather than to concentrate exclusively on flexibilization. However, if a particular government decides that it wants to move forward on flexibilization per se, it would be essential to simultaneously guarantee access to unemployment insurance and to make benefits portable to smooth the transition between jobs. An additional policy that would make labor markets function better is to increase information available to workers and firms in order to reduce search periods and frictional unemployment. Clearly these measures will not eliminate structural unemployment, so they need to be combined with job creation policies as mentioned earlier.

Efforts to stimulate employment are certainly not a substitute for other social policies; rather, the two are highly complementary. Two kinds of complementarities can be identified, although there is overlap between them. One has to do with improving the ability of the work force to adapt to the new demands of the labor markets, especially in view of the region's greater involvement in the world economy. Here education and training are the key issues, but others such as health and housing are also relevant. The other centers on safety nets, aimed to assist vulnerable groups: those who cannot access the labor market or whose incomes do not enable them to maintain their families. Both require an increase in social expenditure.

A positive step in this direction is that, after the contraction of social spending during the crisis years of the 1980s, all countries in the region increased such outlays in the 1990s and some did so dramatically.[23] The funds for increased social spending come from one or more of three sources: faster GDP growth, an increase in public expenditure as a percentage of GDP, or an increase in the share of social spending in total public expenditure. For countries with a low share of public expenditure in GDP, it would be desirable to raise the share to increase social services further. Others will likely need to rely on one of the other two mechanisms. With respect to the share of social spending in total public expenditure, however, a number of countries are close to the maximum that is politically viable. This leaves three alternatives: more efficient use of existing resources, an increase in total public expenditure, which would require an increase in revenues, or greater participation by the private sector. All three have their problems; which alternative is more attractive would vary from country to country, depending on local circumstances and public preferences.

Increasing and improving social expenditure will not do much good if it is then cut when a crisis arises. This was the prevalent pattern in the 1980s, and since social expenditure is strongly procyclical, the threat of future cuts remains. Governments should make sure that social spending is protected when hard times come. The long-term social losses through crises are often never recovered. Children who leave school may never return; workers who lose their jobs may lose invaluable experience if they have trouble returning to work later; families who lose their homes may have difficulties for many years. Those who benefit from the later economic recovery are unlikely to be the same ones who lost as a result of the crisis.

[22] See, for example, Guasch (1996), Burki and Perry (1997), Márquez and Pagés (1998), and Heckman and Pagés (2000).
[23] See ECLAC (1999, chp. 4).

Among social services, improving and expanding access to education must receive high priority. Education expenditure has the double advantage of simultaneously contributing to competitiveness and greater equality, although this is a relatively long-run process. An important share of Latin America's distribution problems, as well as of its productivity problems, comes from its large stock of unskilled labor, which in turn derives from many years of inadequate education. It will be extremely important to work to overcome the legacy of this education gap. This subject has been widely studied, but many controversies and implementation issues remain. How to improve quality is the main issue for primary education. At the secondary level, the issue is expansion of coverage and access, while at the university level, access and the relevance of areas of specialization are paramount. Dramatically increasing the share of entrants to the labor market who have secondary education would simultaneously contribute to the solution of both economic and social problems in the region.

In summary, Latin American countries urgently need to seek solutions to employment problems as the key link between economic and social development. Moreover, festering employment problems also pose a threat to the region's democracies as can be seen in a number of cases. Such solutions will necessarily be multifaceted. In the economic sphere, they involve higher growth and thus investment rates. In the social area, they require special emphasis on education. But these two alone will not suffice. Policies to promote employment per se, with particular attention to the problems of small and even microenterprises, must also be sought.

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