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The Road to Exclusion in Latin America

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Introduction

The emergence of crises is one of the main characteristics of the capitalist system. These crises range from over-accumulation to over–production. They have different impacts upon countries, groups of individuals, eras, etc.; but they always affect the composition of accumulation and the pattern of development in societies.

Latin America has not been an exception. Nowadays, after a period of religious belief in market forces and trickle down effects, the gaps (expressed in terms of social costs) are evident.

Globalization emerged as an alternative with the oil crisis of the 70's, but enforced its position when the debt crisis struck most of Latin America. It found its support in the multilateral institutions that conformed to the so-called Washington Consensus.

This document will investigate the process of disarticulation in Latin American economies as a result of the orthodox structural adjustments associated with globalization; and propose a different alternative that sets full-employment and poverty alleviation at the center of macroeconomic policy, with the state playing the role of Employer of Last Result.

Historical perspective

The crisis after the recession of the 30's induced a model of import substitution industrialization (ISI), which found the theoretical support of Raul Prebisch, and later the Economic Commission for Latin American and the Caribbean (ECLAC), among others. This strategy, which pinpointed the secular deterioration of terms of trade as the main limitation to economic development, shaped the pattern of accumulation during four decades in the region and the world.

The ISI was characterized by the use of the tools developed by Keynesian theory, within the institutional framework of the welfare state in the broad sense.
ISI was successful in several aspects, but the struggle for income among different economic actors (workers vs. industrial capitalists; exporters vs. domestic market; domestic firms vs. foreign ones) accelerated its exhaustion.

ISI, however, had some characteristics that were optimal for the implementation of macro policies focusing on full employment and an improving income distribution, since both were compatible and synergetic with the implemented schema.

As a result of the multiple articulations and linkages in its base, ISI configured a growth path that was self-centered and self–sustained. These articulations can be summarized in three basic dimensions: social, sectoral, and spatial (or local).

Social Articulations

Social articulations emerged in the interaction between capital and labor. Wages were more than a mere cost of production. They provided the main source of demand fueling investment, and therefore, profits to the firms. Class struggle was postponed and limited to episodes at the firm or sector level.

Workers' representation and negotiation was centralized by national unions, with a global bargaining capacity that spread the results to all workers.
Within this institutional framework a generalized wage increase would imply a rise in the general economic activity that rapidly would absorb the climb of production costs, at least maintaining the rate of profits.

Wage and salary increases did not affect significantly the systemic competitiveness of sectors due to the way in which they were inserted at international level. They would raise aggregate demand (consumption and investment) and its contribution to GDP.

The State played an important role here; not only by regulating the relations between capital and labor in order to reduce conflict, but also as an employer of last resource with an anti-cyclical behavior.

Sectoral Articulation

From a sectoral perspective, the articulation emerged from the forward and backward linkages among sectors and sub-sectors of the economy helping to diffuse the effects of economic growth to the rest of the economy.

The rise of one sector would start a multiplier process, fueling not only consumption, but also intermediate demand and investment; and linking the production of goods, connected services, and reinforcing the social articulations stated before.

The state would intervene by setting maximum and minimum prices, production quotas, and subsidizing crucial sectors; but mainly, by investing in basic industries and infrastructure not covered by the private sector.

Spatial Articulation

The two levels of articulations stated above, were reproduced at the regional level. By a type of comparative advantage framework, each region, mainly large countries, specialized in the production of a certain product, thereby developing similar social and sectoral articulations as at local level. Sometimes this process was linked to natural resources, and at other times to patterns of production induced via state subsidies.
The regions also constituted centers of demand of goods and services, generating to their interior, multipliers at the local level.

The state regulated employment in the region, in the same manner as at the national level, boosting or maintaining the aggregate demand at local level.
The debate of regional planning at that time was how to close the gap between rich and poor regions of a country, by finding ways to induce investment in the poorer areas.

Internal contradictions

This schematic process was not exempt of contradictions and limitations.
One of them was the on external front. The provision of foreign exchange limited the possibilities to develop in certain areas industries that were capital-intensive or dependant on high/medium levels of technology.

In this sense, the deterioration of terms of trade and the recurrent crises of raw materials prices, plus the limitations imposed by central countries on the access to those markets, developed. These events induced devaluations with the aim of reducing domestic absorption via incomes and a cycle of stop and go, as very well depicted by several prestigious scholars.

The second restriction was the monopolistic structure of certain domestic markets. The industries in these markets behaved in a sort of rent-seeking way and heavily lobbied governments in order to maintain their dominant position.
This structure fed inflation via the struggle for advantageous income distribution at certain points of time and induced instability both at the economic and political level.
The schema was finally exhausted as a result of internal inefficiencies and distribution struggles, the failure of the state to be an engine of economic growth, and the influence of the neo-classical discourse promoted by multilateral institutions (transformed in the auditing agencies of the financial sector after the debt crisis).

Disarticulations

The central characteristic of the new (or perhaps not so new) regime of accumulation, in contrast with the ISI, is the way in which the articulations are dismantled (i.e. disarticulation), by aiming for a new set of economic relations locally and worldwide.

With the opening of the economy, especially the linkage to international capital markets, the deregulation and withdrawal of the state, and the resulting social polarization emerging from the crisis; firms are forced to target international markets or segments of high income that survived the successive orthodox structural adjustment programs.

The first consequence is social disarticulation. Wages are no longer a factor that dynamizes demand, but a mere cost of production to firms, that should be maintained as low as possible. The new goal of the economy is to maintain profits and the external competitiveness of domestic firms. Although productivity per employed worker increased significantly, and was sometimes accompanied by wage increases, the skyrocketing of unemployment shows very little social efficiency.

The process of deregulation of markets, via privatization and removal of subsidies, plus the reduction of import barriers and tariffs, enlarges and turns inelastic other components of production costs. Wages become the only adjusting variable in the productive structure of the firm, breaking the temporary social alliance of the other stages. The interest of workers and capitalists collide. To firms, the purchasing power of workers in other countries becomes more important than that of local ones. As soon as a downturn in the economy appears, more pressures for flexible labor markets arise.

This result goes hand-in-hand with the seeking of competitiveness, integrating an increasing amount of foreign inputs into the productive process and inducing disarticulation at the sector level. These changes imply the closing of industries and sectors that lost "micro efficiency" as the economic censuses of the Latin-American region show. It becomes more convenient to import from other countries, even though this has dramatic implications at the country level.

As such, the regions lose importance. Whole populations are marginalized within the economy as a result of the closing of factories around which the town developed. First, the linked activities disappear, followed by the services provided to the local population.

This process can be sustained since, at the beginning, the deterioration strikes "individuals": individual firms, individual households, and individual regions; thus, enlarging the idea of the role of externalities in the change: frictional unemployment (losers due to a lag in the adaptation to the new scenario) or artificially developed regions. But after a while, the deterioration in income distribution, the reduction of domestic markets, and the lack of counter-cyclical policies show that the problem is more structural than a withdrawal of foreign flows at a certain juncture.

The pattern of development changed from relatively homogeneous growth to a mushroom-like pattern, with reasonable growth on average, but only in clusters, while the rest are excluded.

Summarizing, the explosive cocktail of indiscriminate processes in the opening of the economy (e.g. deregulation of domestic markets and desertion of the state as indicative or imperative planner) tear apart the multiple articulations that characterized the ISI strategy pursued by the region for almost 50 years. The ultimate result consolidates a process of polarization and heterogeneity in the society, with fewer rich, each time richer and more linked to foreign markets, and more and more people left outside.

Social heterogeneity, within a process of increasing poverty, reduces efficiency of social policies, and induces, with the support of multilateral institutions, the implementation of targeted strategies, that do not achieve their goals.

As an agenda

Although not clearly mentioned in these pages, globalization cannot be understood as a natural disaster. It is the oeuvre of humans, imposed upon the whole world, striking deeply the most vulnerable. When nobody regulates the markets, the powerful are the ones that impose the plan. In addition, some of its unbeneficial effects for third world countries are impossible to withdraw, unless serious steps are taken in that direction.

First and foremost, there should be a restitution of the linkages inside countries between different groups of the population struck by the effects of globalization. This restitution should occur through the implementation of social policies aimed at restoring some of the articulations stated before. The best social policy is that of full employment, re-establishing the role of the state as employer of last resource.

Although unemployment is not the main cause of poverty, a high proportion of the poor, have no job at all, or have to find their living in low quality, low paid, episodic jobs. This situation must reversed, not only by supply side policies such as training and education, but also by the means of active labor market policies that reduce the vulnerability generated by the deregulation and flexibilization of labor markets, as imposed by the IMF and World Bank.

Full employment as the center of macro policies

With financial liberalization most orthodox macroeconomists take financial flows as the main variable to be taken into account when evaluating the results of certain policies. In contrast, the suggestion here is to have full employment as the goal of every country's economic policy, and not merely as an externality of "sound economic policies," of which the orthodox theory advocates.

With such an objective function, the rest of the variables should be adjusted to achieve full employment. Monetary policies, trade, subsidies, fiscal policies, taxing regimes, would have to adjust in each country in order to reach full employment, thereby reducing the negative effects of globalization. Each country will try to preserve the working posts by adjusting its policies domestically and internationally to obtain full employment.

This strategy also implies the provision of an income to every household in the country, as well as the support to maintain children and youngsters attending school, thereby disrupting the inter-generational reproduction of poverty, with its perverse effects on the human capital of the country.

The goal of poverty alleviation will add other quantitative indicators to the economic performance and allow the rapid correction of the direction assumed. Within such a framework, employment generation, economic sustainability and the social impact of the policies will direct the definition of long-term strategies.

The state as the employer of last resort

Within this framework of analysis, the state playing the role of employer of last resort (ELR) is a must.

Most of the unemployment in the periphery can be targeted with such programs that present the characteristics of the so-called Keynesian unemployment, mainly explained by the shortage of aggregate demand; rather than the more Marxian unemployment that results from a capital accumulation shortage and is present in countries that faced a long duration of stagnation, recession or capital stock destruction.

The strategy of this type of program is to induce aggregate demand by giving a job to any unemployed person that is willing to work in a certain social service or activity at a politically determined wage or salary.

By this method, unemployment, and at the same time poverty and indigence, will be reduced, boosting aggregate demand in order to restore the three levels of articulations and tending to stabilize the economy.

As the private sector´s demand for workers increases, the buffer stock determined by the pool of workers in the ELR program will be reduced, thus operating as a counter-cyclical strategy.

<u>The ELR and its advantages</u>

An ELR program has a number of advantages at the political, social and local level, beyond the ones at macro level and in line with the process stated in the paragraph above.

<u>Political advantages of the ELR</u>

It should be clear that an ELR is a program that needs a certain degree of political will and autonomy, and in that sense, presents some advantages to the policymaker that help in the implementation of such a program.

- **Constitutes a global strategy against exclusion and poverty:** An ELR program is global, in the sense that it addresses the problem of exclusion and poverty, by centering on the employment condition of the individual and restoring the citizenship status absent during the period of structural adjustment programs. It helps to show figures in terms of poverty and indigence reduction as goals of the administration.

- **It a clear schema of social protection, not charity:** Since an ELR program involves a social service by the individual, it cannot be considered a mere charity strategy, and should be envisioned as a social protection schema by the overall community, enhancing the political and social acceptability of the plan.

- **Reduces unemployment:** Unemployment is one of the crucial variables that help in the appraisal of a political administration; and since the ELR reduces the involuntary unemployed to almost zero, it can be presented as an achievement.

- **Integrates excluded groups:** It helps excluded collectives to extend nets and linkages via equality of opportunities, at least at the level of the program. It has a high level of self-targeting, thus making it superior to other type of social programs.

- **Allows the identification of problems for further interventions:** Since poverty is multidimensional, the program helps to identify other problems that are hiding at the household level, under the sign of unemployment, and aids in the design of complementary interventions.

Social advantages of the ELR

The ELR is meant to reduce the exclusion that characterized the structural adjustment strategy implemented during the 80-90s in most of the countries of the region, generating what was called social disarticulation.

- **Solves basic needs insufficiency at the household level:** A large number of households present unsatisfied basic needs, most of them due to the insufficiency of income, thus, leading to an increase in school drop-out rates, infant mortality, poor housing, dependency rate, etc. The provision of a basic income via employment helps to solve that facet of the problem.

- **Improves human capital at individual, local, and national level:** It is well known that the chances of an unemployed individual is lower the longer the unemployment period is; thus, the reinsertion into an employment schema that involves training is a very efficient way of avoiding this process of human capital deterioration.

- **Involves beneficiaries in collective plans and projects:** The beneficiaries of the program, some of them with years of unemployment, can be involved in collective plans, many of them designed at the grass roots level, restoring the social links and networks locally. Overall, it enhances the feeling of participation at local level.

- **Reduces pressures on the unprotected informal labor markets:** In countries with high informal or non-registered labor markets, the vulnerability of workers is immense. If all individuals have the opportunity to get a reasonably paid job, it will induce wage increases and better working conditions in those markets, some of which are at the fringe of legality.

Local and regional advantages of the ELR

- **It is basically counter-cyclical:** As was stated above, the ELR has an important role in reducing the negative impact of the business cycle, as well as other effects, such as: climatic problems, external shocks, etc. at the local level, and avoiding the transfer of those negative effects to other sectors linked to the main employers in the region.

- **Improves infrastructure and proximity services:** Since the beneficiaries will be involved mainly in local community projects, it provides an improvement on the local infrastructure (sanitation, housing, better side-walks, irrigation schemas, road maintenance, schools and hospital maintenance, etc.), as well as services appropriated by the same local community and small scale business and inhabitants, such as: day care, school support, health support, etc.

• **Generates multiplying and accelerating effects:** Since the pattern of development and accumulation has changed from a homogeneous one to one with the behavior of "mushrooms," it is very important to induce demand at local level in order to recover local activities that were impacted by the disarticulation process. With an ELR, the injection of local demand can restore part of those linkages destroyed by the institutional change.

• **It is able to articulate with the productive sectors in order to create stable, good quality jobs:** If the domestic demand is induced and some of the activities developed within the ELR program can be directed to foster the productive infrastructure of the region, it is more likely that the business community will take advantage of that potential. This does not mean that the beneficiaries should play the role of the subsidized labor force for the private sector, since this has proven to be harmful (due to several factors that reduce the effectiveness of the ELR).

• **Barely distorts local labor markets:** Although this is not a major point in economies that have unemployment rates of two digits, labor market distortion is one of the arguments stated by those that defend free markets. Alternatives to subsidizing private employment, however, result in the piling up of people in the queue, and not generating enough jobs. On top of that some pervasive effects tend to occur, such as fictitious turn-over, massive lay-offs at the end of the program, etc.

Silver Bullet. One size fits all?

Although the ELR is an excellent alternative for most of the countries that face high unemployment, stagnation of the economy, and uneven regional development, further analysis on the labor market and its linkages to the overall economy should be taken into account.

In economies that rely on self-consumption and where poverty is more linked to the lack of access to assets and resources such as land or water, an ELR program will have a different impact upon them.

The same happens to economies where there is a high unregistered or informal sector, where small-scale firms are an important source of incomes for the population, or where underemployment is widespread.

In these instances, it is important to have a sand table where simulations of the impact of the ELR and the diffusion of its effects can be traced. The State can thus optimize the program, and not only reduce unemployment - the most obvious goal, but also reduce poverty or indigence - the most desirable achievement of the program. Also at issue is how to define the wage level of the ELR and its impact at national and local levels, how it will affect local salaries and local productions, and how seasonal activities can be abandoned by beneficiaries of the ELR.

Managing the ELR

A massive program in order to provide employment to large sectors of the population involves significant managerial capabilities that are not always present, not only in the administrative structure needed to pay a monthly salary to millions, but also in the assumption of a portfolio of projects and activities that can be utilized by the beneficiaries in order to achieve the objectives of the program.

Some of the projects may require qualifications for workers that are not present. The support of certain structures from the state or civil society should be organized. Fraud and stigmatization are additional problems that will arise for sure and should be confronted. More than acceptable levels of fraud reduce the social acceptability and legitimacy of the program, especially in the eyes of taxpayers who may stigmatize the beneficiaries by talking about their dependency on the program. Only the clear consciousness of the social benefits of the program, can prevent this type of behavior.

Conclusion

Only a massive state intervention can stop the implosive spiral that induces unemployment, poverty, bankruptcy of small-scale firms, local government crisis, and its inter-temporal reproduction. Targeted interventions, aimed at the signs of the problem, rather than the causes, have proven ineffective and inefficient. The ELR is an alternative that will restore the linkages and articulations at different levels, promote development, and above all, reduce poverty and unemployment - the most disrupting factors in a society.