The Emerging Global Labor Market

Joe lives in a small town in Southern Texas. His old job as an accounts clerk in a textile firm, where he had worked for many years, was not very secure. He earned $50 a day, but promises of promotion never came through, and the firm eventually went out of business as cheap imports from Mexico forced textile prices down. Joe went back to college to study business administration and was recently hired by one of the new banks in the area. He enjoys a more comfortable living even after making the monthly payments on his government-subsidized student loan.

Maria recently moved from her central Mexican village and now works in a U.S.-owned firm in Mexico's maquiladora sector. Her husband, Juan, runs a small car upholstery business and sometimes crosses the border during the harvest season to work illegally on farms in California. Maria, Juan, and their son have improved their standard of living since moving out of subsistence agriculture, but Maria's wage has not increased in years: she still earns about $10 a day, and her wage is likely to decline following the recent capital outflows.

Xiao Zhi is an industrial worker in Shenzhen, a Special Economic Zone in southern China. After three difficult years on the road as part of China's floating population, fleeing the poverty of nearby Sichuan Province, he has finally settled with a new firm from Hong Kong that produces garments for the U.S. market. He can now afford more than a bowl of rice for his daily meal. He makes $2 a day and is hopeful for the future.

Workers around the world are living increasingly intertwined lives. Most of the world's population now lives in countries that are either integrated into world markets for goods and finance, or rapidly becoming so. Not so long ago, in the late 1970s, only a few developing countries, led by some in East Asia, were opening their borders to flows of trade and investment capital. About a third of the world's labor force lived in countries with centrally planned economies, and at least another third lived in countries insulated from international markets by prohibitive trade barriers and capital controls. Today, three giant population blocs—China, the republics of the former Soviet Union, and India—with nearly half the world's labor force among them, are entering the global market, and many other countries from Mexico to Indonesia have already established deep linkages. By the year 2000 fewer than 10 percent of the world's workers are likely to be cut off from the economic mainstream.

But are workers better off as a result of these globalizing trends? Stories about losers from integration often make headlines: how Joe lost his job because of competition from poor Mexicans like Maria, and how her wage is held down by cheaper exports from China. But Joe now has a better job, and the U.S. economy has gained from expanding exports to Mexico. Maria's standard of living has improved, and her son can hope for a better future. The productivity of both workers is rising with increased investment, financed partly by the savings of workers in other countries, and Joe's pension fund is earning higher returns through diversification and new investment opportunities. Juan is looking forward to the day when he will no longer need to travel north—Xiao Zhi, meanwhile, would jump at the opportunity to make the wages Juan earns in California.

The complexity of these economic relationships would have been unthinkable just ten or twenty years ago. And as new opportunities for trade and interaction have grown, so too have attitudes shifted. In the 1950s and 1960s most developing countries regarded world market forces as a threat to their industrialization and development. Today they see them as a source of new opportunities. There is greater recognition that exports create good jobs, external capital flows spur accumulation and growth, and migration brings mutual gains.

But not everyone has benefited, and the international system has come under attack by some in industrial countries where rising unemployment and wage inequality are making people feel less secure about the future. Some workers in the industrial world are fearful of losing their jobs because of cheap exports from lower cost producers. Others worry about companies relocating abroad in search of low wages and lax standards, or fear that hordes of poor migrants will soon be at the door, offering to work for lower wages. The response has been a proliferation of protectionist demands, many of them under the guise of demands for fair trade and a level playing field.

Driving forces of global integration

Technological change and continually falling communications and transport costs have been a major factor behind global integration. Cross-border transport and trade are also easier today because of progress in resolving many of
the political conflicts that have divided the economic world for decades, such as the cold war, the apartheid system in South Africa, and the volatile situation in the Middle East. Most important, however, have been the actions of developing countries themselves. By rejecting the failed development strategies of the past based on insulation from world economic events, more countries than ever before have joined the economic mainstream.

Development strategies are changing fast all over the world. Central planning has been abandoned in the former Soviet Union and in Eastern Europe, and countries throughout Latin America, South Asia, and the Middle East are reversing policies of import substitution designed to prevent the need for trade. This development revolution is most apparent in the area of trade policies. Since 1986 more than sixty developing countries have reported unilateral liberalization measures to the General Agreement on Tariffs and Trade (GATT), twenty-four have joined GATT, and twenty are in the process of joining its successor the World Trade Organization. Barriers to trade should fall further now that the Uruguay Round is complete, and with the enlargement of the North American Free Trade Agreement (NAFTA) and the European Union.

Governments are increasingly seeking to improve the international competitiveness of their economies rather than shield them behind protective walls. Developing countries have made tremendous progress in education and steady improvements in physical capital and infrastructure, boosting their productive capacity and enabling them to compete in world markets. Between 1970 and 1992 the low- and middle-income countries’ share of the world’s work force rose from 79 percent to 83 percent, but their share of the world’s skilled work force (those workers with at least a secondary education) jumped from a third to nearly a half. Their share in total capital stocks also grew but remains small, rising from 9 percent to 13 percent of the world total.

This shift in development strategy has been reinforced by technological changes that have made the world easier to navigate—goods, capital, people, and ideas travel faster and cheaper today than ever before. Underlying these changes have been huge reductions in transport and communications costs. By 1960 maritime transport costs were less than a third of their 1920 level, and costs have continued to fall (Figure 7.1). Communications costs are falling even more dramatically—the cost of an international telephone call fell sixfold between 1940 and 1970 and tenfold between 1970 and 1990.

Channels of global interactions

International trade is the first avenue by which most countries feel the impact of economic integration. Volumes of goods and services traded across borders have grown tremendously in recent years, accounting for about 45 percent of world GDP in 1990, up from 25 percent in 1970 (Figure 7.2). In 1990, 17 percent of the labor force in developing and former centrally planned economies worked directly or indirectly in the export sector, with exports to the richer countries accounting for two-thirds of this employment effect. There was also a rapid shift to higher-value-added activities: the share of manufactures in developing countries’ exports tripled between 1970 and 1990, from 20 percent to 60 percent. This rise marks a radical change in the international division of labor since the 1960s, when developing countries exported primary commodities almost exclusively. With the expansion of labor-intensive exports of manufactures, trade has come of age.
International trade is booming—but it has not affected all regions evenly. The East Asian economies were the first to demonstrate the dynamic effects on economic growth when open trade is coupled with government expenditures directed at human and physical capital infrastructure and heavy imports of capital and technology. Several middle-income economies from Chile to Turkey followed suit in exploiting export-led growth. As the successful newly industrializing economies have climbed the quality ladder and moved out of products based on unskilled labor, poorer countries such as China and India have moved in. Trailing the other regions are Sub-Saharan Africa and the Middle East, which did not expand their exports of manufactures. Both regions remain producers of primary commodities, and their terms of trade have continued to fall.

Capital has also become increasingly mobile, ever in search of the best returns. Gross capital flows (inflows plus outflows), an admittedly imperfect measure of capital mobility, rose from 7 percent to 9 percent of GDP in developing and transitional economies during the past two decades (Figure 7.2). Capital controls have been relaxed and are easily evaded anyway. Today capital moves more readily into successful countries and out of those countries where returns on investment are outweighed by the risks.

But capital does not always flow toward poorer countries. Although overall capital flows have grown steadily, net flows (total inflows minus total outflows) have remained small and unstable. Net flows rose in the 1970s, fell sharply in the 1980s as the debt crisis brought rising debt service burdens and massive capital flight, and then started to rise again at the end of the decade. By 1992 net capital flows to developing countries had returned to earlier levels. Overall, the transfer of resources from rich to poor countries has played only a moderate role in complementing domestic saving in developing countries: under the extreme assumption that domestic saving rates have not been affected by these flows, about 11 percent of capital formation in developing countries during the 1970–90 period could be attributed to the cumulative effect of capital mobility (an amount equivalent to only about 2 percent of the combined capital stocks of the industrial countries).

Regions have fared unequally in attracting capital inflows. Latin America has long been an important participant in international capital markets. Countries there were hit hard by the 1980s debt crisis but witnessed major reflows after the debt reductions of late in that decade. The Mexican crisis of 1994–95 shows how fickle these flows can be when confidence in economic management disappears. In the past, capital flows played a less important role in Asia, but this asymmetry is fading fast with rising involvement of foreign capital in China and the progressive liberalization of capital markets in India and East Asia. Most of the capital going to Sub-Saharan Africa and the Middle

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**Figure 7.2 Trade, capital flows, and migration in industrial, developing, and transitional countries.**

Data are inflows plus outflows for all the countries in each group. Source: Migration data from Zlotnik 1993; all other data from the World Bank.
East is from official sources, but capital flight from these regions has been large.

International migration of people in search of work is the laggard in this story. Annual migratory flows from developing countries (total inflows and outflows) are no greater now, relative to population size, than in the early 1970s, at about one emigrant per thousand inhabitants (Figure 7.2). The overall effect of international migration is much smaller than that of capital or trade: only about 2 percent of people born in low- and middle-income countries do not live in their country of origin. Migrants send home about $75 billion a year, about one-third the volume of net capital flows. Some 2 million to 3 million new migrants now leave developing countries each year (both legally and illegally), about half of whom go to industrial countries. For the latter, migration from developing countries translates into 1.5 new immigrants per thousand inhabitants per year, the same as in 1970. Migration between industrial countries has fallen since 1970 from 2.5 migrants per thousand inhabitants in 1970 to 1.5 per thousand in 1990. The foreign-born share of the population in industrial countries—currently about 5 percent—has been rising, however, because of the slower growth of the native population.

Nor is international migration yet a global business. Most migrants still stay within their regions: African migrants most often go to other African countries, and those from Asia and the Middle East mainly to the Arab Gulf countries. Recently migration within Asia has picked up. In Europe migrants are typically from former colonies or neighboring countries. Migration to the United States differs from this pattern: its immigrants come not only from nearby Mexico but from a variety of far-flung countries including the Philippines, the Republic of Korea, Viet Nam, India, and China.

**Will a new golden age bring convergence?**

Most workers in poorer countries are only just beginning to feel the benefits—and costs—of global integration. Participation by developing countries in the earlier globalization of 1850 to 1900 was shallow and often based on unfavorable terms, especially in Asia and Africa. They exported exclusively primary products, and capital flowed in mainly to support such enterprises—to develop capacity in natural resource extraction and maintain the support of friendly governments. Today, developing countries have the opportunity to play a far more active role. The potential for large gains is enormous. Whether they are realized will depend on the policy choices made by developing country governments and on the reactions of industrial countries.

The combination of powerful, cost-reducing technological change, policy change, and political developments is forging ever-stronger links within the global labor market. But it would be foolish to predict that the differences between rich and poor countries will rapidly disappear through convergence, either upward (of poorer countries'...
wages and living standards toward those in the rich countries) or downward (the reverse). Convergence is a notion both dear to economists, who like its close fit with theory, and abhorred by populists in rich countries, who see it as a threat to their incomes. Past experience, however, supports neither the hopes of the former nor the fears of the latter (Box 7.1). Wages have converged within Europe and the United States, where integration has been deep and the initial conditions were not too different, but even there convergence has been slow and incomplete.

But while some poorer countries—most notably the East Asian stars—are catching up with the richer ones, just as many have failed to narrow the gap, and some are losing ground. Overall, divergence, not convergence, has been the rule: the ratio of income per capita in the richest countries to that in the poorest increased fivefold between 1870 and 1985, and global inequality rose slightly between 1960 and 1986 (the output share of the poorest 50 percent of the world population shrunk from 7.3 percent to 6.3 percent, while that of the richest 20 percent rose from 71.3 percent to 74.1 percent), before improving more recently as a result of faster growth in the poor countries of Asia.

Globalization is unavoidable—the welfare of Joe, Maria, and Xiao Zhi is now more closely linked than ever before. But growth prospects remain dominated by the effects of national economic policies. The forces of globalization increase both the benefits of good policies and the cost of failure. Although no group of workers can rely on the forces of convergence to raise their wages automatically, neither need they fear that such forces will inadvertently pull their wages down. Whether a new golden age arrives for all depends mostly on the responses of individual countries to the new opportunities offered by this increasingly global economy.

**CHAPTER 8**

**A Changing International Division of Labor**

**Trade increases most workers’ welfare**

International trade benefits most workers: because workers are also consumers, it brings them immediate gains through cheaper imports, and it enables most workers to become more productive as the goods they produce increase in value. One statistic powerfully makes the case for an export-led strategy: during the past two decades real wages rose at an average annual rate of 3 percent in those devel-