December 2007

ILR Impact Brief - Economic Development, Labor Markets, and Poverty Reduction

Gary S. Fields
Cornell University, gsf2@cornell.edu

ILR Impact Brief - Economic Development, Labor Markets, and Poverty Reduction

Abstract

[Excerpt] Economic development is generally understood to involve improvements in economic well-being for a society and its members. Despite the generalized unfolding of economic opportunity that accompanies economic growth, the specific goal of poverty reduction should be the most pressing component of a development agenda. Labor market policies that foster the creation of “good” jobs and prepare the population to hold these jobs will alleviate individual economic privation.

Keywords

poverty, labor markets, economic development, economic growth, public policy

Comments

Suggested Citation

Fields, G. (2007). *Economic development, labor markets, and poverty reduction* (Impact Brief #24). Ithaca, NY: School of Industrial and Labor Relations, Cornell University. http://digitalcommons.ilr.cornell.edu/briefs/38

For a more in-depth analysis, please see: Fields, G. (2006). “Labor Markets and Economic Development”. *Journal of Eastern Caribbean Studies, 31*(2), 72-84.

The ILR Impact Brief series highlights the research and project based work conducted by ILR faculty that is relevant to workplace issues and public policy. The Briefs are prepared by Maralyn Edid, Senior Extension Associate, ILR School.

IMPACT BRIEF

Brief #24 / December 2007 / ILR School / www.ilr.cornell.edu

Economic Development, Labor Markets, and Poverty Reduction

Research question: What is the most critical aspect of economic development beyond macro-level economic growth?

Conclusion: Economic development is generally understood to involve improvements in economic well-being for a society and its members. Despite the generalized unfolding of economic opportunity that accompanies economic growth, the specific goal of poverty reduction should be the most pressing component of a development agenda. Labor market policies that foster the creation of "good" jobs and prepare the population to hold these jobs will alleviate individual economic privation.

Policy implications: The choices governments make regarding development goals and the policies that result largely determine whether the outcomes are more or less favorable for businesses, individuals and groups of individuals, and governments and non-governmental organizations (NGOs). A government's choices also influence how effectively the labor market contributes to economic growth and conveys to participants the gains from growth. Economic development encompasses more than increases in economic activity and is unlikely to evolve from free, unfettered markets. National governments should intervene with country-specific policies to promote outcomes that yield widely dispersed benefits.

Abstract: Economic development entails the relaxation of constraints on choice, those limitations being the hallmark of economic underdevelopment. As opportunities open up for workers, businesses, and government, policy makers should not lose sight of the importance of poverty reduction. Hard-core privation is prevalent in many parts of the world, where nearly three billion people are living on the equivalent of less than two U.S. dollars a day. The International Labour Organisation (ILO), a specialized agency of the United Nations, estimates that the "working poor" are seven times more numerous than those without any work at all.

Realistic and pragmatic policies may improve the chances that economic development will be win-win-win. In such a scenario, businesses sell more products in more markets, individuals earn more money and enjoy enhanced benefits and services, and governments and NGOs collect more taxes and contributions, respectively, enabling them to deliver better services and programs. The decision taken by many East Asian countries during the past few decades to produce for world markets generated this type of broad-based economic success. Although economists concede that development helps some individuals more than others, assertions that export-oriented growth strategies benefit a few at the expense of the many lack supporting evidence. Public policies that protect and potentially enhance incomes, such as worker retraining and trade adjustment assistance, may mitigate whatever inequities do arise.

The central role played by labor markets in distributing the gains from growth make them potentially effective

instruments of poverty reduction. In the traditional supply and demand model, where wages are set by the market—that is, by the intersection of the demand for, and supply of, labor—employment and output are both maximized. During periods of economic growth, demand for labor increases and wages rise accordingly. But if the government inhibits the market by artificially setting wages, say, or by limiting employers' ability to hire and fire, the rate of economic growth suffers along with individuals' earning opportunities.

Crafting the growth strategy that suits the reality of any given country is the primary challenge facing policy makers. Both Africa and the Caribbean, for example, have long been characterized by what economists term "dualistic" labor markets; i.e., two distinct segments, each with its own supply and demand structure and institutions: formal and informal in the Caribbean, rural and urban in Africa. Take Kenya, where prior to the 1970s high-wage jobs were located in the cities and the resulting out-migration from low-wage rural areas caused urban unemployment to rise. Ultimately, the government implemented a rural development strategy that drew migrants home from the cities; over time, urban unemployment fell.

This paper argues that labor market policies intended to foster economic development should target job quality rather than maximum levels of employment. Aiming at the latter only ensures unacceptably low wages and overlooks terms and conditions of employment, such as health and safety, workers' rights, and job security. The ILO has formulated a set of core labor standards that prohibit forced labor, child labor, and discriminatory hiring and that also guarantee freedom of association and collective bargaining; it has urged all member states, now numbering 175, to adopt and enforce these standards.

Poverty reduction through the creation of more and better jobs requires government intervention. To increase the demand for labor, governments could i) implement employment-friendly labor market policies, such as avoiding onerous regulations against dismissals, and ii) maintain a sound business environment, wherein property rights are secure, contracts are enforced, foreign investment is welcome, domestic capital is retained, and corporations are properly governed. To augment the supply of labor, governments should focus on the quality of human capital by supporting education, training programs, and other initiatives that develop the skills demanded by a globalized economy; provision of health care and child care would encourage individuals to supply more of their labor. And finally, governments could tweak the workings of the labor market by providing abundant information about job openings and devising laws and institutions that create realistic possibilities for occupational and/or geographic mobility.

Greater savings, investment, and capital formation may be the standard tools of economic growth, but labor markets are the most effective mechanism for spreading the wealth.

Methodology: Decades of research, including field work in Africa, Asia, and Latin America, by the author informed this document.

Source publication: "Labor Markets and Economic Development" appeared in *Journal of Eastern Caribbean Studies*, 31(2): 72-84, June, 2006.

---

by Gary Fields
Professor of Labor Economics and International and Comparative Labor (ILR)