

The Impact of the Global Financial and Economic Crisis on Developing Countries, in particular Africa, and the prospects for attaining the MDGs.

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I would like to thank, on behalf of Mr Juan Somavia, DG of the ILO, the invitation by Mr. Koichiro Matsuura, DG of UNESCO for the ILO to participate in this important event. This event is very timely as there is no doubt that the multilateral system and institutions need to rethink the way they do business in the wake of the financial crisis.

A. 2009 is a year in which labour markets around the world will be hit hard

The present crisis started as a full financial crisis in developed economies, then it hit product markets, consumer demand and trade. And 2009 is the year that the crisis will hit labour markets turning into a global jobs and unemployment crisis. The risk is that it also turns into a social and political crisis in a number of countries. Unfortunately, many indicators suggest that the crisis will be much deeper and broader, and will last much longer than initially thought.

Four weeks ago the ILO released our annual Global Employment Trends Report. We anticipate a dramatic increase in unemployment in developed countries and in working poverty and vulnerable employment in developing countries:

- The report estimates three scenarios. The results show that open unemployment can increase globally between 30 and 50 million people in comparison to 2007, reaching a total of 230 million, which corresponds to a global rate of unemployment of 7.1%.
- The number of people in extreme poverty is estimated to increase globally by 6.1 percentage points over the 2007 levels in the worst case scenario which represents an increase of more than 200 million additional people earning less than USD 1.25 a day. If this happens, this would take the world back to the poverty situation it had in 1997, wiping out the gains over the past decade. The crisis means that 2009 will be the first year since the MDGs were launched in which poverty at the global level will not be reduced but instead it will increase.

As the recession bites, poverty reduction unravels and the middle classes worldwide are weakened, the risk is that social and political tensions will multiply. Many governments around the world will be concerned in 2009 with how to avert explosions of social unrest.

Compared to previous crisis, this one has been characterized by the **speed** with which it has hit and spread globally, and the **synchronization** of its impacts in different countries. Developed countries are experiencing a **vicious circle** of negative interactions between financial markets, product markets, trade, and now labour markets. Job losses lead to lower consumption, which lowers industrial confidence, which leads to less investment, which results in more job losses, and so on. The global and synchronized nature of the crisis means that national tools are not enough, international and multilateral action is imperative, and how the multilateral system reacts is a key part of the solutions to the crisis.

B. Impacts and Prospects.

In March 2009 the downturn is unfortunately still deepening in and the risk is that a severe recession turns into depression. On January 28 the IMF released new growth estimates for 2009. World growth is expected to come to a virtual halt as it is estimated at only 0.5% for 2009.

Developed countries

Developed economies are expected to contract by -2.0%. The US by -1.6%; the Euro area by -2.0%, with the hardest hit being the UK -2.8% and Germany -2.5%; while Japan is expected to contract by -2.60%. The US economy shrank at its fastest pace in 26 years in the last quarter of 2008 and it is estimated that it could contract by another 6% in second quarter of 2009 before the impact of the stimulus package is felt, generating more unemployment. US unemployment now stands at 7.2%, and different sources predict it could hit 9% as the recession spreads.

In the Eurozone (EU16) the rate of unemployment climbed to 8% in December, which means that some 12.5 million people in the region are now seeking work. For the entire 27 nation EU, unemployment was 7.4 % in December, up from 7.3 a month earlier. (Eurostat) And recent figures reveal that the recession in the Eurozone is steeper than previously feared.

Indicators that the global recession is getting worse in developed economies include the fact that the financial markets continue under stress, asset values continue to fall, credit disruptions also continue constraining household spending and curtailing production and trade. The IMF World Economic Outlook points out that in January the world economy seems to have taken a sharp turn for the worse.¹ As bad news continue to come from the financial sector, impacts on the real economy are still percolating. Energetic action has been taken by governments but many economists agree that the economic situation will get worse in developed economies before it gets better.

Developing countries

The crisis has affected developing countries surprisingly quickly and strongly, through multiple channels: reduced trade flows, decline in commodity prices, reduced liquidity and tightening of credit markets affecting both the private and public sectors, reduced flows of remittances, a drop in Foreign Direct Investment (FDI), exchange rate depreciation and uncertainty, and declining flows of Official Development Assistance (ODA). Let me talk briefly about key regional developments and challenges.

Asia

The Newly Industrialized Asian economies (Asian Tigers) are expected to contract by -3.9%. Only the group of emerging and developing economies is expected to grow at positive rates with an average of 3.3%, led by China (6.7%) and India (5.1%). But China's growth was revised downward from the November 2008 estimate of 8.5% to 6.7%, and India's growth from 6.3% to 5.1%.

¹ Every day there are more bleak news: "More woe as 72.500 jobs axed in one day (FT, Jan 27); "Despair moves to the fore at Davos" (IHT, Jan 29); "Economic pain to be worst for 60 years" (FT, Jan 29). On 27th January leading corporations announced more than 70.000 job cuts: Caterpillar 20.000, ING 7.000, Pfizer 19.000, Philips 6.000, Sprint Nextel 8.000; Corus 3.500, Home Depot 7.000, General Motors 2.000.

In Asia, as The Economist has put it “The scale and speed of the downturn is breathtaking and broader in scope than in the financial crisis of 1997-98” (The Economist, Jan 31st-Feb 6th).²

Latin America

In Latin America, after six years of high growth, growth in 2009 will be considerable lower, and even negative in a number of countries, including Mexico. All engines of growth and all sources of financing in LAC are affected by the crisis: trade, tourism, FDI flows, remittance flows, and the prices of primary commodities. The conditions that propelled the region’s fast growth during the last six years are gone: the growth of exports, the high prices of commodities, abundant financing and low interest rates.³

The good news in Latin America is that the region is better prepared to face the crisis than in the 80s. First, inflation, the level of indebtedness and fiscal deficits are lower, providing fiscal space in several countries to respond to the crisis. The level of international reserves is also much higher. Second, most countries have implemented social programs: 85 million Latin-Americans are receiving a subsidy under Conditional Cash Transfer (CCT) schemes in at least 12 countries.

However, important weaknesses remain: a heavy dependence on commodity exports, and persistent inequality and poverty. Most important, social policy has not transitioned from a programme-based logic to an integrated view of inclusive-growth with social protection, that is, it has not transitioned to what in the ILO we call a decent work approach.⁴

ILO employment scenarios for Latin America indicate a possible increase in the unemployment rate to 8.3 percent for 2009 in comparison to 7.2% in 2007 which amounts to roughly 4 million additional unemployed in comparison to 2007 (worst case scenario). Extreme poverty in Latin America decreased from 22% in 1999 to less than 10% in 2007. However, in 2008-09 we estimate that extreme poverty will increase by around 2 percentage points. This increase compares favourably with other regions, which will see increases by 7 to 15 percentage points except in Central and South Eastern Europe (non EU) and CIS.

Africa

As for Africa, in the past ten years African economies have experienced faster and steadier economic growth than in the preceding two decades. Even a year ago Sub-Saharan African economies were, on average, growing at a similar pace to the rest of the world for the first time in three decades, and Africa seemed to have a bright growth outlook. Today the picture is quite different.

² China’s GDP, which expanded by 13% in 2007, scarcely grew in the last quarter of 2008 on a seasonally adjusted basis. In the same quarter Japan’s GDP is estimated to have fallen by 10%, Singapore’s at 17% and South Korea’s at 21%. Industrial production numbers have fallen even more dramatically.

³ UNDP, Regional Bureau for Latin America and the Caribbean, Crisis Update No. 2. The Global Financial Crisis: Social Implications for Latin America and the Caribbean, February 10, 2009.

⁴ Social security schemes and social protection still have low coverage in many countries and have inadequate benefits for large sectors of the population. This has not only social but also economic consequences, as the “transitory poverty” increases induced by crises tend to become “structural poverty” with long term consequences on the welfare of the next generation on issues such as maternal and infant mortality, malnutrition and dropout from schooling.

Like Latin America and many Asian countries, the main drivers of growth seem to be gone or seriously disrupted: commodity prices, capital inflows, and remittance flows are all in decline. The decline in remittances has direct negative effects on households given that they are directly used for covering basic needs such as food, education and health. Key sectors that have driven growth in the past decade, such as mining,⁵ tourism,⁶ and manufacturing,⁷ are being seriously affected and have been forced to decrease production and lay off workers. And promised increases in aid seem not to materialize. Throughout the region Stock Market Indexes are down significantly, numerous countries are suffering capital outflow risk. And African Banks are having difficulties securing lines of credit in international markets, thus tightening credit to the African private sector. Trade financing and financing of large infrastructure investment projects have been particularly affected.

The ILO's most recent labour market information for Sub-Saharan Africa confirms that the region stands out as a region with extremely harsh labour market conditions:

- The unemployment rate decreased slightly in the past five years but our unemployment scenarios for the region suggest that the unemployment rate could increase to 8.5 per cent this year, adding an additional 3 million people to the ranks of the unemployed.
- Vulnerable employment (defined as self employed plus contributing family workers) accounted for more than 3 out of every four persons employed in the region in 2007. This rate decreased by 3.5 percentage points between 1997 and 2007 in Sub-saharan Africa, however, our worst case scenario for 2009 suggests that the rate could increase from 77.4 per cent in 2007 to 82.6 in 2009 - a 5.2 percentage point increase. This would mean that an additional 28 million people could move into vulnerable employment in comparison with 2007.
- Similarly with working poverty, almost three fifths of the employed are classified as extreme working poor in Sub-Saharan Africa. For 2009 there could be an additional 36 million people earning less than USD 1.25 per day when compared to 2007. After a slight decline in the past decade, our worst case scenario suggests that the rate could increase from 58.3 per cent in 2007 to 67.2 per cent for 2009.⁸

⁵ In the DR Congo, about 300,000 jobs have been lost by now in the mining province of Katanga alone due to declining commodity prices. In South Africa job losses are expected or have been effected as companies scale down on production such as Petra Diamonds Ltd which plans to halt output at its Helam mine in South Africa and lay off more than half of its workers (350 jobs at the mine out of 669 employees) while in Simmer & Jack's Buffelsfontein Gold Mines, nearly 10 percent of the employees are expected to lose their jobs. In Zambia, a total of 3,072 copper miners have lost their jobs since December 2008 as leading copper miners announced closure with immediate effect.

⁶ The Tanzania Association of Tour Operators (TATO) has seen cancellations, from mainly American and European tourists, of between 30 and 50 per cent starting in January 2009 and June 2009. In Kenya, while the first two months of 2008 saw 80 per cent hotel bed occupancy, in the same period in 2009, occupancy has averaged between 50 and 60 per cent, with bookings headed downwards.

⁷ Volkswagen South Africa has announced plans to close all production areas in the last week of February 2009 and in the weeks before and after the Easter weekend. Separately the company will be retrenching some 400 employees through a voluntary separation package process.

⁸ About four fifths of the employed are classified as working poor when using the USD 2 per day rate, giving Sub-Saharan Africa the highest working poverty rate in the world. Our scenarios indicate that an additional 27 million people could earn less than USD 2 per day in 2009 compared to 2007. This is 4.4 percentage points higher- from 82.2 per cent in 2007 to 86.6 per cent in 2009.

Like in Latin America and Asia, the speed and nature of the impact of the crisis in Africa vary very significantly across countries depending on economic structure, policy constraints and other specificities. Some countries are more vulnerable than others. But clearly these figures suggest that it is very likely that the crisis will reverse the modest gains of many African countries in terms of growth, poverty reduction and job creation. These developmental impacts may be large and may outlast the crisis. Even less than in Latin America, in Africa social policy has not transitioned from a programme-based logic to a truly integrated view of inclusive-growth with social protection and decent work.

And, in contrast to Latin America, a number of African countries are highly vulnerable and have a more constrained fiscal policy space due to their high current account deficits, high debt levels and fiscal deficits. Unfortunately, many African countries can be classified as high risk countries on the basis of these macroeconomic balances considerations, as is done in a recent report by the African Development Bank.⁹

C. Solutions to the economic crisis and the role of the multilateral system

Let me now talk about the policy challenges, the need for international coordination and the role of the multilateral system. There are plenty of problems to solve and a lot that governments are already doing.

The multilateral system should have an active role in the search for solutions to the crisis for at least four fundamental reasons:

- First, because the crisis is global and it cannot be solved by using only national economic tools,
- Second, it was the policies of the past that got the world into this mess, so solutions to the crisis should not just try to apply the same prescriptions. The crisis is an opportunity for rethinking approaches and paradigms, and to re-balance policy packages, both nationally and internationally.
- Third, the crisis is affecting emerging and developing countries and the UN system is the guardian of the international development agenda.
- Fourth, the crisis is now a full jobs crisis and potentially a social crisis affecting **people**. The focus of the response cannot be only in the financial and macroeconomic level, it has to also include measures centred on people to cushion the labour market, welfare and poverty effects. And the multilateral system can be extremely helpful in all these respects.

The conclusion from this is that the solutions to the crisis need to be global and coordinated, development-oriented, people-centred, inclusive, and of course urgent.

The active role of the multilateral system should be based on a **broad vision** of what will be required for an effective response to the crisis and to the opportunities it represents and for this the multilateral system should agree on a number of **messages**, to help set the agenda and influence the formulation and implementation of solutions both globally and locally. What can these messages be?

There is first and foremost a message about the policy packages to frame the issues. Solutions to the crisis should have at least a four-track policy package.

⁹ ADB, Impact of the Financial Crisis on African Economies, Meeting of the Committee of Finance Ministers and Central Bank Governors, Cape Town, South Africa, 16 January, 2009.

First, fiscal and monetary policies to keep credit flowing and provide fiscal stimulus to the economy. There is an important debate on the nature of fiscal stimulus and how to make it more effective for job creation and lay the foundations for a more sustainable growth in the future. Although important to boost aggregate demand, fiscal stimulus is not the panacea. As Robert Zoellick, President of the World Bank has said “Pumping money into the economy through fiscal stimulus is not enough, governments need to fix the financial system.”

And this is the **second track: restoring health to the financial system** which involves dealing with the bad loans and toxic assets of banks, recapitalizing them, reshaping the financial sector regulations, avoiding financial nationalism. As Dominique Strauss-Kahn, Managing Director of the IMF has said “If the financial system is not restructured, all the money from the stimulus would go into a black hole”.

But there is a **third track** that the UN system must insist on and have key role in solving, this is **labour market and social policy responses to mitigate the blow on labour markets and on people**. Not enough is being done in this respect and to take care of the social and developmental dimensions of the crisis. This is important not only to promote recovery but to lay the foundations for a more sustainable and inclusive pattern of growth in the future. The labour market mitigation agenda should include measures such as the following:¹⁰

1. Strengthening income maintenance measures for the unemployed such as boosting unemployment benefits (duration, coverage), incentives to employers for work sharing and temporary worker retention, and complementary cash transfers programmes.
2. Expanding social protection measures and protecting pensions from the devastating decline of financial markets.
3. Strengthen active labour market policies to support employment and earnings such as introducing temporary payroll tax holidays or wage subsidies and expanding training programmes to the unemployed. Periods of slack labour demand are opportunities to invest in the development of worker skills.
4. Support to enterprises, particularly SMEs, to overcome cash-flow and access to credit problems.
5. A very important opportunity for employment generation is public investment in infrastructure, including community infrastructure through emergency public works with labour intensive techniques.¹¹
6. Targeted support to vulnerable groups and sectors, such as for instance, introducing temporary youth employment programmes.
7. Restructuring of enterprises and sectors and how to do it in a socially responsible way.
8. Strengthening of employment services, whose basic purpose is precisely to facilitate the adjustment of firms and individuals to changing labour market conditions. Employment services are more important than ever in times of crisis as workforce mobility increases.

¹⁰ See ILO “A Global Jobs Pact for a Sustainable Economy”, Paper for the Tripartite High Level meeting on the financial crisis, March, 2009.

¹¹ This includes: construction and rehabilitation of physical infrastructure, such as roads, bridges, schools, hospitals and clinics, social care and community social infrastructure upgrading, in particular through labour-based approaches. Labour-intensive approaches have become an important element of job creation strategies in many low-wage developing countries with considerable reserves of underutilized labour, and they can be applied in developed countries as well. While major capital-intensive new infrastructure projects take time to translate into increased employment, labour-based approaches can generate jobs and much-needed infrastructure quite quickly.

9. Incentives and investments in energy efficient technologies and “green jobs” can be an important contribution to job creation and recovery.
10. Social dialogue at enterprise, sectoral and national levels for all of these policies

Middle income countries with fiscal space and a better degree of institutional capacity are better positioned to introduce these types of policies, low-income countries have fewer options and need to rely on administratively less demanding programmes, such as public works and measures to increase productivity of informal economy activities, such as targeted micro-credit schemes.¹²

The UN should also be stressing the message that the present crisis is an opportunity to promote innovative patterns of growth. The type of growth dynamic experienced by many African and other developing countries in the past has been concentrated on a few export-led enclaves in mining or a few commodities. Agriculture more broadly and local industrialization has often been neglected. Also neglected has been investing in education, social services, science and knowledge, a point UNESCO has been stressing. The crisis is an opportunity to re-think and re-balance development agendas, not just to return to the policies of the past. For instance, by linking income support and employment services for workers to investments in skills development and promotion of the principles of lifelong learning during a global economic slowdown, there is an opportunity to raise future productivity of workers and enterprises while at the same time assist economically vulnerable members of society to remain or become connected to decent work. The ILO and UNESCO are engaged in conversations to strengthen our cooperation on these issues.

The fourth area is the need for **global coordination and cooperation** and the role of the multilateral system in this. The challenges of coordination include:

- Fiscal stimulus and global unbalances. Fiscal stimulus should not only be national but coordinated, as intended by the G20. The question is whether there will be enough political will to cooperate. As Dominique Strauss-Kahn, managing director of the IMF has said, not enough coordinated global action has been taken yet, and the G20 credibility is at stake.¹³
- Trade. The other area of cooperation is maintaining open trade and the flow of trade financing. In contrast to the 1930s, today the threat to keeping an open trading system seems to come more from subsidies and bailouts of troubled economic sectors or “strategic companies” than from tariff increases. Industrial bailout policy risks turning into a subsidy war.
- Aid. The third area is ensuring adequate flows of development aid. Substantial transfers of resources to developing countries will be needed to enable these countries to overcome their financing constraints in addressing this crisis that originated in the developed world and to be able to protect the most vulnerable from the worst consequences. It is important for donors to honour their commitments not just as a matter of principle but because reductions in aid will amplify the negative impacts of the crisis.

¹² How should labour market policy respond to the financial crisis? World Bank, HD and PREM Labour Market Teams, February, 2009.

¹³ The world needs to stimulate not only national demand but global aggregate demand. Surplus countries in the world economy have to stimulate their own economies and have to be willing to continue financing the deficit countries. It is in these surplus countries where the scope to increase aggregate demand in the world is the greatest. So the world economy needs a massive global rebalancing, particularly between US deficits and China surpluses.

- Labour market and social policy. It is not only in the traditional trade, aid and fiscal policy areas that coordination is needed. An essential ingredient in a balanced response to the crisis is cooperation on labour markets and social programmes including investments in basic education, technical and vocational education and social services. As I said, periods of slack labour demand are opportunities to invest in the development of worker skills.

Despite the enormity of the challenge the world seems to lack effective institutions to coordinate and mitigate the downturn and its impacts. Policy coordination should take place within an inclusive multilateral institutional setting, making use of the legitimate platform that the UN provides. The G-20 process could well pave the way for a broader consensus but engagement of the entire international community is required to provide legitimacy to the immediate policy actions needed as well as to the implementation of the necessary reforms of the international financial architecture and global economic governance structures.

The multilateral system should not only have the right messages with respect to the policy packages but it should also develop operational programmes of support to countries and globally in all these areas.

The UN needs to have a positive agenda and provide new, innovative ideas. In a paper we produced in the ILO to be presented to the Governing Body in two weeks time we are suggesting the idea of creating a “Global Recovery and Jobs Pact”. This Pact is about promoting social and income security as a global goal, it is about ways to address global asymmetries and imbalances, and about the need to mitigate labour market impacts of the crisis.

Finally, the multilateral system should have a clear message about the role of the private sector in confronting the crisis and operational programmes on a broad front with them. While business cannot eradicate poverty, poverty will never be eradicated without business, nor sufficient jobs created in a sustainable way. Confidence needs to be restored and new forms of partnership promoted. Business engagement around social and development issues and good corporate citizenship are more important than ever. There is a broad agenda here but let me stop at this point.

Thank you very much for your attention.