



**From the Crisis of Distribution to the  
Distribution of the Costs of the Crisis:  
What Can We Learn from  
Previous Crises about the  
Effects of the Financial Crisis  
on Labor Share?**

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**Abstract**

The paper analyzes the possible distributional consequences of the global crisis based on the lessons of the past crises experiences. The decline in the labor share across the globe has been a major factor that led to the current global crisis. What we are going through is a crisis of distribution, and similarly the policy reactions to the crisis are part of a distributional struggle. The paper presents the effects of the former crises in the developing countries and in Japan on income distribution, wages, and unemployment. This comparison is important not only because it compares developing vs. developed country cases, but also because it highlights the differences of the currency crises vs. domestic financial crises regarding the distributional consequences. However despite differences, the cumulative effect is in both cases a dramatic pro-capital redistribution. Building on these lessons, the paper discusses the possible different effects of the current global crisis in the developed countries, Eastern Europe, and developing countries, and concludes with policy alternatives to avoid the socialization of the costs of the crisis.

**Key words:** global crisis, labor share, unemployment, developing countries, Japan, developed countries, Eastern Europe

## **1. Introduction**

The aim of this paper is to analyze the possible distributional consequences of the global crisis based on the lessons of the past crises experiences. While public policy in the advanced capitalist countries concentrated on arresting the credit crash since the first onset of the crisis in summer 2007, the effects of the crisis on the real sector has attracted the attention of policy makers as late as 2008 winter. Although there is finally some concern about the possible employment effects, distributional consequences are still not on the agenda.

The failure to recognize the distributional aspects of the crisis by the policy reactions is no coincidence, when the mainstream analysis about the reasons of the crisis is kept in mind (e.g. IMF, 2008; OECD, 2008; ECB, 2008), which often portrayed the crisis as a banking and financial sector crisis with implications for the real sector. However this analysis misses the important structural reasons behind the crisis, which are related to the neoliberal macroeconomic policy choices of the post-1980s and the major redistribution of income at the expense of labor as a consequence. Even if the European Commission (2007) is finally pointing at the falling wage share in Europe and other advanced countries, it fails to connect this deterioration to the crisis, and handles the issue as a separate problem, mostly related to skill-biased technological change. Among the international institutions, ILO (2008) is the only exception to have built the link between the crisis and distribution. The neoliberal policies and the deterioration in labor share have created an important fertile ground to bury the seeds of a major global crisis together with the risky developments in the credit, housing, and security markets. Thus what we are going through is a crisis of distribution; and similarly the policy reactions to the crisis are part of a distributional struggle, even if it is not named. This also explains why the international as well as national institutions reacted to the accumulating risks only after they turned into a full-fledged crisis. Although the profits of this fragile growth regime were privatized, the losses and risks are now being socialized. What we understand from the socialization of the costs, is not only the use of the working peoples' tax money for generous rescue packages in a narrow sense, but also the broader consequences of the crisis on income distribution.

The following section discusses the distributional background of the crisis with a focus on the labor share and the functional distribution of income. Section three presents the effects of the former crises in the developing countries and in Japan on income distribution and unemployment. Building on these lessons, section four discusses the possible effects of the current global crisis in different countries. Section five concludes with policy implications.

## **2. The crisis of neoliberalism**

Since the 1980s, the world economy has been guided by neoliberal economic policies such as the dismantling of government regulations in financial markets as well as goods and labor markets, and increased openness to trade, foreign direct investment and financial capital flows. These policies have reduced the role for macroeconomic policy interventions with the claim that free market capitalism would increase efficiency and growth, and provide a fair distribution. The focus of macroeconomic policy has shifted away from full-employment towards mere price stability. The outcome was a secular deterioration in the labor share since the early 1980s.

Figure 1 shows the decline in the labor share in the major advanced capitalist countries, the Eastern European countries, and selected developing countries. There is a secular decline in the labor share across the globe ranging from developed countries to major emerging economies of Latin America, Asia, as well as Eastern Europe, who have all shared

similar neoliberal policy guidelines. As an exception, in the last years in the Baltic countries and Czech Republic the labor share is back to the former peaks at the starting of the transition, however data does not allow us to compare their current situation with the pre-transition phase; moreover it is well possible that the recovery will not be preserved during the current crisis. Although this global trend is very striking, these numbers are hiding another important fact: the very high wages of the CEOs or other top managerial income earners are also part of labor income, and the share of these high income groups in total labor income has increased dramatically at the expense of the rest of the wage earners in the last two decades (ILO, 2008). For example in the US, the real hourly compensation of the production and non-supervisory workers, which constitute 85% of the labor force, have been stagnating since the 1980s despite significant gains in productivity (Palley, 2008). Median real wages grew only by 0.3% per year during 2000-06, while labor productivity increased by 2.5% per year (ILO, 2008).

### Figure 1

The increase in globalization, in particular the mobility of capital, and the stagnation in aggregate demand have been the central powers behind this pro-capital redistribution of income (Onaran, 2008a, b). The stagnation in demand led to higher unemployment and eroded the bargaining power of labor against capital. In the mean time, the increase in the mobility of capital has not only contributed to this erosion in the bargaining power of labor, but also increased the fragility à la Minsky built in the capitalist system via increased financialization and speculation. There have been more crises in the post-1980s than in 1970s (Laeven and Valencia, 2008). This, coupled with the tight fiscal and monetary policies, and a decrease in the labor share in income, set the conditions for the vicious cycle of deficient aggregate demand, low growth, low employment, and a crisis prone global economy.

Here lie the two important long term contradictions of neoliberalism. Firstly, laissez-faire capitalism has generated higher profits for multinational firms, and especially for the financial sector. However, the high financial returns have replaced profits from real activity in many cases. As the finance dominated regime rose, the investment behavior of the firms were significantly affected by the rising shareholder value orientation. Lazonick and O'Sullivan (2000) argue that a shift in management behavior from 'retain and reinvest' to 'downsize and distribute' has occurred. Financial market-oriented remuneration schemes based on short-term profitability increased the orientation of management towards shareholders' objectives. The unregulated financial markets and the pressure of financial market investors have created a bias in favor of asset purchases as opposed to asset creation. At the same time most of the effort of macroeconomic policy makers has been going to policies to retain the confidence of volatile financial markets. Markets have been deregulated mainly to support the interests of the rentier-capitalists, who went on benefiting from investment subsidies, tax concessions and rescue operations during crises. The same process has limited the demands of workers. In a way, the loss in labor's share has prevented the profits in the real sector from being eroded by increased interest payments. Consequently the relationship between profits and investment has changed; the investment-profit ratio shows a clear declining trend, thus higher profits do not automatically lead to higher investment. Thus in spite of higher profit rates, not only in the USA, but also in the major advanced capitalist economies (Germany, France and the UK), as well as some developing countries (e.g. Latin America, Turkey), economic growth rates have been well below their historical trends.

Secondly from a macroeconomic perspective, the decline in the labor share has also been a problem for the micro level beneficiaries of these policies. Profit can only be realized if there is sufficient effective demand for the goods and services. But the decline in the

purchasing power of labor has a negative effect on consumption, given that the marginal propensity to consume out of profits as well as rentier income is lower than that out of wages. This affects investments negatively, which are already under the pressure of share holder value orientation.

Exactly at this point the financial innovations seemed to have offered a short-term solution to the crisis of neoliberalism in the 1990s: debt-led consumption growth. It is important to note that without the unequal income distribution the debt-led growth model would not have been necessary or possible. Particularly in the US, but also in UK, Ireland or even some continental European countries like Netherlands and Denmark the household debt increased dramatically in the last decade. The increase in housing credits and house prices fuelled each other; then the increased housing wealth thanks to the housing bubble served as collateral for further credit, and fuelled consumption. However, the wealth effect is based on notional wealth, which cannot be realized collectively but only serve as collateral for consumers to accumulate debt; and beyond a point the wealth effect may even turn negative due to increased interest payments, and increased risk of default (Bhaduri et al., 2006). Financialization leads to a debt-led growth by fueling consumption in the short-run, but debt has to be serviced in the future. The debt channel is a redistribution of income from indebted low-income households to rentier households. Thus the positive effects of the debt-led growth are destined to be partially offset by the negative effects of redistribution on consumption. Because of high debt levels, the fragility of the economy to the possible shocks in the credit market also increases.

This debt-led consumption model created a current account deficit in the US that exceeded 6% of the GDP. This deficit was financed by the surpluses of some other developed countries like Germany and Japan, developing countries like China and South Korea, and the oil rich Middle Eastern countries. In Germany and Japan current account surpluses and the consequent capital outflows to the US were made possible by wage moderation, which has suppressed domestic consumption and fuelled exports. Thus this is again an outcome of the crisis of distribution. On the side of the developing countries like China and South Korea, the experience of the Asian and Latin American crises stimulated a policy of accumulation of foreign reserves as a bail-out guarantee against the speculative capital outflows. Here the international dimension of inequality plays an important role: these countries, threatened by the free mobility and volatility of short term international financial flows, invested their current account surpluses in US government bonds instead of stimulating their domestic development plans.

The deregulation in the financial markets and the consequent innovations in mortgage backed securities, collateralized debt obligations and credit default swaps facilitated the debt-led growth model. These innovations and the “originate and distribute” model of banking have multiplied the amount of the credit that the banks could extend given the limits of their capital. The premiums earned by the bankers, the commissions of the banks, the high CEO incomes thanks to high bank profits, the commissions of the rating agencies all created a perverse mechanism of investments that led to short-termism and ignorance about the risks of this banking model. In the short-run in the sub-prime credit segment, even if the risk of default were known, this was not perceived as a major issue: first, most of these credits were anyway sold to other investors in the form of mortgage backed securities with high ratings. Second, when there is a credit default, the houses, which serve as collateral, could be taken over and as long as the house prices kept increasing this was a profitable business for the creditor. However this banking model led to a very risky economic model and a time bomb, which was destined to explode eventually. The bad news from the sub-prime markets

triggered the explosion eventually, and first the market for CDOs and then the interbank market, and finally the whole credit market collapsed at a global scale.

It is interesting to ask, why it took so long for the time bomb to explode. The reason is the endogenous evolution of the expectations: as the debt-led growth model produced high short-term growth and profits, optimism was stimulated via self-fulfilling prophecy, and risks were more and more underestimated even by those who were more conservative at the beginning. In Keynes' words, this resembles trying to bet on the winner of a "beauty contest", where what you think is unimportant; what matters is correctly guessing the opinion of the members of the jury, i.e. the other players in the market. In a world of coerced competition (Crotty, 1993) even those who see the risks are forced to take risky positions, if they are to keep their jobs as dealers, bankers, or CEOs, since the burst of the bubble is a matter of time, and it can take longer than the short-term evaluation of the profits by the share holders, who fail to value more secure investment behavior. Just a couple of weeks before the big collapse in July 2007, the ex-CEO of Citibank, Chuck Prince, had said "when the music stops, in terms of liquidity, things will be complicated. But as long as the music is playing, you've got to get up and dance" (Elliott, 2007). An example of a bank analyst, who lost his job because of "conservatism" is Michael Mayo, who "said in 1999 to sell banks stocks and has not wavered from that call, which cost him his job at Credit Suisse and friends on the Street. That year he said banks relied too much on asset-backed securities, and that if home prices fell we would see a self-fulfilling prophecy of lower home prices and lower collateral, not to mention unique political fallout" (Fortune, 2008). In the coerced competition environment the banks as well as the credit customers increased their leverage. This has increased the fragility of the economy and created a systemic risk; and when the shock came, credit crunch and the collapse of the debt-led growth model was inevitable.

Although it was not possible to say when and how deep the crisis would be, it was always clear that the crisis would hit as suggested by a number of political economists (e.g. Brenner, 2003; Palley, 2004; 2006; Baker, 2006, 2007; Crotty, 2007; Papadimitriou et al, 2007; Godley et al, 2007; Whalen, 2007; Becker, 2007 Onaran, 2007; Stockhammer, 2008), and several prominent New Keynesian economists (e.g. Stiglitz, 2008; Shiller, 2000, 2008; Roubini 2006). In the mainstream camp, there were also warnings about the problem of US current account sustainability and its consequences for the global economy (Goldstein, 2005; Mussa, 2005; Edward, 2006; Obstfeld and Rogoff, 2001, 2005). The mainstream economic institutions like the FED, IMF, OECD, or ECB as well as many mainstream economists nevertheless ignored the risks. The IMF (2006) was still defending that the new financial instruments were distributing the risks and creating a more "resilient" financial system. In the US policy makers also failed badly in foreseeing the problems. In Fortune's words "Greenspan's legacy is tarnished by his decision to keep interest rates low while watching the housing bubble expand. Bernanke predicted this February that the economy and markets would be fine, after saying in 2005 that housing prices would see 'a moderate cooling', but not a collapse. And just days before recommending radical measures to get money to Fannie Mae and Freddie Mac, Paulson said they were adequately capitalized." (Fortune, August, 2008). It is interesting that Bernanke, who was very aware of the Great Depression as well as the deflationary experience of Japan in the 1990s (see his speech in 2002 at the Fed), was nevertheless not alert enough to prevent the risk of a great crash. UNCTAD (e.g. World Economic Situation, 2006) and Bank of International Settlements (BIS, 2006) were the only exceptions among the international institutions to warn about the imbalances in the global economy. Given that BIS is the umbrella body for central banks, the ignorance of FED and the ECB is all the more striking (Elliott and Atkinson, 2008). While the "beauty competition" argument can partly explain the indifference of the mainstream international institutions to risks, a more important explanation is the distributional aspect behind this risky model: the

prevention of the crisis required the solution of the distributional problems behind the debt-led growth model, i.e. redistribution of income and wealth; however the powerful global elite, which has influence over global policy making through their nation states would not agree with this solution. Therefore the policy institutes hoped for a “soft-lending” that would correct the bubbles without effectively touching the distributional conflict. Only in 2007 mainstream economic institutions began to publicly express worries about the possibility of a financial crisis (IMF, 2007; ECB, 2007). On the other hand if we consider that the German Finance Minister Steinbrück had named the crisis as an Anglo-Saxon crisis just a few days before the bad news about the German banks’ balance sheets regarding their write-downs due to the CDOs, it is also clear that the supervision and signaling mechanisms were not properly working.

### **3. Learning from the past: crisis, unemployment, and distribution**

This part analyses the effects of some previous financial crises on the distribution of income, wages, and unemployment. Past crisis experiences show that the episodes of crisis intensify the distributional struggle and the question on who will carry the burden of adjustment becomes part of the struggle. In that respect we will focus on the experiences of developing countries as well as the Japanese slump of the 1990s as a developed country case. This comparison is important, because it highlights the differences of the currency crises vs. domestic financial crises regarding the distributional consequences.<sup>1</sup> There are two important aspects related with this comparison: while the currency crises of the developing countries come with inflationary effects, the issue in Japan’s crisis was deflation. The other important difference is the duration and the size of the shock: in most of the developing country crises, the recession is a very deep, but one year long phenomenon, whereas during the Japanese slump, the initial shock to growth was moderate, however the recovery took more than a decade. As a consequence, the developing country crises lead to sharp declines in real wages, whereas the deflationary environment creates moderate real wage declines or even some minor increases particularly in years of deflation. However strikingly, the cumulative effect is in both cases a dramatic pro-capital redistribution.

#### **3.1 Empirical evidence: developing countries**

##### **3.1.1 Wage share and crisis**

Despite former policy differences many developing countries have experienced in the past similar outcomes as a consequence of financial crises that followed the liberalization of capital flows. The effects of the crises in the developing countries worked through three channels: 1. the decline in growth and thereby labor demand, 2. the increase in unemployment, and thereby the decline in the bargaining power of workers, 3. inflationary shocks during currency crises, 4. path dependency effect, i.e. lagged effects. The outcome in the developing countries has been a radical deterioration in the real wage, and consequently wage share, which has persisted years after the crisis. Similarly unemployment rates, which hike during the crises, have not been back to pre-crisis levels for years after the crises.

We first focus on three developing countries; Mexico, Turkey, and Korea, for which detailed data are available (see Figure 1.c).<sup>2</sup> The differences in economic policy are reflected

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<sup>1</sup> Although in recent papers Claessens et al (2008) and Eichengreen and Bordo (2001) compare different crises and their macroeconomic consequences, the differences regarding the distributional effects are not discussed in this literature.

<sup>2</sup> This part is using material published in Onaran (2009). We restrict our analysis to the manufacturing industry due to the lack of nationwide wage data for Turkey and Mexico prior to late 1980s. The data source for Korea



to the distributional outcomes of the countries. Mexico and Turkey, which based their international competitiveness on low wages during the era of liberalization, experienced a significant decline in the manufacturing wage share since the 1980s, whereas Korea, which had not adopted the standard orthodox structural adjustment programs in the early 1980s, and had relied on the industrial policy-investment-growth nexus, experienced an increase in the wage share. Nevertheless, the crises following capital account liberalization have had very similar effects on the wage share in all three countries leading to a sharp and long lasting decline.

During the currency crises the decline in growth and bargaining power of workers, and the inflationary shocks have set the stage for the decline in the wage share. Due to the import dependency of these countries, depreciation of the local currency has a pass-through effect on prices due to an increase in the price of the imported goods, which generates an important increase in overall input costs, and thus dramatic increases in inflation. The depreciation rates had reached up to 90.2% in Mexico in 1994, and 169.5% and 96.0% in Turkey in 1994 and 2001 respectively, 47.3% in Korea in 1998. The outcome is a radical deterioration in the real wage, and consequently wage share. Indeed similar episodes were also experienced during the early phases of opening up in the Latin American countries and Turkey, which were accompanied by huge devaluations. Be it due to the official devaluations of the early stages of liberalization or the market made depreciations after the financial crises following the nominal anchor based anti-inflationist stabilization programs, there is a clear trade-off between the rate of depreciation and the wage share. Not only are these inflationary shocks unexpected, but also it is hard for the workers to ask for wage increases in line with inflation due to the magnitude of the shock. Depending on the balance of power relations, the firms try to compensate the increase in input costs by a decline in labor costs. Similarly, the reverse has also been true during episodes of capital inflow, and appreciation of the currency, when employers become more accommodative towards wage demands. However, these episodes have been sooner or later disturbed by the increased current account deficits and fragility in the economy, which is followed by the currency crises. The negative effect of depreciation also depends on the extent of the dollarization of the economy, which determines the destructive dimensions of a currency crisis.

Table 1 summarizes the developments in the exchange rate and growth during these crisis episodes, and decomposes the sources of the decline in the wage share to its sources: i.e. changes in real wages and labor productivity; the latter is also decomposed as changes in value added and employment.

Table 1

The initial crisis year is always associated with a decline in the wage share, which by far exceeds the rate of decline in production. During a crisis, employers push labor unions to accept dramatic wage cuts or compulsory unpaid leaves to avoid job losses. The crisis also creates a hysteresis effect that destroys the bargaining power of labor for a long period afterwards. Diwan (2001) defines crises as episodes of distributional fights, which leave "distributional scars". In all countries, a strong economic recovery took place the year after the crisis, however the fall in the wage share usually continued for two or even three years. In Mexico the wage share declined 27.7% as of 1996 compared to 1993, and indeed has still not returned to its pre-crisis level ten years after the crisis based on the latest available data for

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and Mexico is the OECD Industrial Structural Analysis Database (STAN), which report labor compensation data. For Turkey we extend the labor compensation share in the National Accounts Database backwards using the percentage change in the wage share in manufacturing industry surveys.

2004. The post 2001 recession in Mexico has triggered a new declining trend in the wage share. In Turkey the cumulative decline in the wage share has been 24.8% and 30.2% following the 1994 and 2001 crises with the decline continuing for two and six years respectively. Given the latest available data for 2006, the wage share is still not back to its pre-crisis level after the 2001 crisis. The wage share as of 2006 is even lower than its level in 1994. In Korea, the wage share has continued to decline for three years following the 1997 crisis, and was 21.6% lower in 1999 compared to 1996. Also in Korea the wage share has not returned back to its pre-crisis level in 10 years after the crisis. In that respect, crisis has brought Korea closer to the cases of Mexico and Turkey, reversing the increasing trend.

The major source of the decline in the wage share during the crisis year is the decline in the real wage. Real wages continue to decline for two more years after the crisis in both Mexico and Turkey (except for the 1981 recovery in wages after the military coup of 1980). Employment declines also in all crisis years, except for 1980 in Turkey, when the crisis was associated with a military coup, which also banned lay-offs. In both Mexico and Turkey during all crisis years the decline in the real wage is much higher than the change in employment. Thus wages adjust rather flexibly to changes in the labor market conditions. On the contrary during the Korean crisis, the adjustment in employment exceeds that in real wages quite significantly. In Korea the decline in employment also exceeded that in value added, leading to productivity increases. In Mexico both 1982 and 1995 are episodes of stagnant productivity (comparable declines in employment and value added), thus the decline in the wage share is solely resulting from real wage declines. In the cases of crises of Turkey, both productivity and real wages decline, with the decline in the latter being significantly higher. The recovery that had started in 2004 in real wages was so minor compared to productivity increases that the wage share continued to decline during the 2004-2008 recovery period as well. As of 2008 the real wages were still 19.9% lower than in 2000.

Figures 1d and 1e show further evidence about the declining wage share in manufacturing industry in six more major South-East Asian and Latin American countries with a crisis experience.<sup>3</sup> The wage share is lower in the post-1980s compared to 1970s in all countries with usually significant margins other than in Philippines and Thailand. In Argentina, Brazil, Indonesia, Malaysia, the wage share is also lower in the 1990s than that in the 1980s. The crises also hit the wage share strongly in all these countries.

Finally, the broad numbers about real wages deflated based on a general consumer price index hide an important information about how different income groups are affected as inflation accelerates after the crisis. Given that food consumption forms a significant proportion of the consumption budget of working class households, higher food price inflation will affect them more adversely than others and decrease real wages even more than what we observe based on average consumer price inflation rates. Food price inflation has exceeded average consumer price inflation rates in Turkey in 1994 and 1995 by 3.7 and 9 points respectively, in Mexico in 1995 and 1996 by 4.2 and 7.2 points respectively, in Indonesia from 1997 to 1999 by values ranging between 2.1 and 34.7 percentage points, in Korea in 1998 and 1999 by 1.2 and 2.0 points respectively, in Malaysia from 1997 to 1999 by values ranging between 1.5 and 3.6 points, in Argentina in 2002 by 8.8 percentage points.

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<sup>3</sup> For labor share calculations for Brazil, Philippines, and Thailand, the UN manufacturing data is combined with the World Development Indicators (WDI) database of 1993, which report manufacturing wages and employment, and for Argentina, Indonesia, and Malaysia WDI data is combined with the Economic Intelligence (EIU) database based on percentage changes.

Onaran (2008b and 2009) presents econometric evidence about the effect of the currency crises on the wage share in developing countries estimating the percentage change in the wage share in manufacturing as a function of growth (current and lagged), nominal depreciation rate of the currency (current and lagged), and its own lag.<sup>4</sup> To test whether there is a break in the cyclical behavior of labor's share during the crisis periods, the normal years vs. recession years are separated<sup>5</sup>. During normal years wage share is not pro-cyclical in most of the cases, but it is pro-cyclical during a recession in Argentina, Indonesia, Malaysia, Mexico, and Turkey, with the decline in the wage share ranging between 1.4% (Malaysia) and 7.8% (Turkey) as a response to a 1% decline in growth. When the nominal depreciation is not controlled for, wage share is pro-cyclical during a crisis in Korea as well. Only in Philippines the wage share has a counter-cyclical character during a recession. Nominal depreciation has a negative significant effect on wage share in six out of ten countries (Argentina, Chile, Indonesia, Korea, Mexico, Turkey). The economic significance of the negative effect of depreciation is ranging between -0.003 in Argentina and -0.22 in the case of Turkey. If we interpret these results for a crisis year, the cause of the decline in the wage share during a crisis is explained by mostly the dramatic rates of nominal depreciation. In five countries the contraction of growth has a simultaneous negative effect as well. The persistence of the decline in the wage share is mostly related to the lagged effect from either growth or past year's decline in the wage share.

### 3.1.2 Unemployment

Figure 2 shows the pre and post-crisis trends in unemployment for selected developing countries, which have experienced a crisis in the post-1980s. Among the South-East Asian countries, in Indonesia, and Philippines, there had already been an increasing trend since 1980s in unemployment, which had further worsened after the crises. In both countries unemployment went on increasing for 7 years after 1998 (by 6.8%-points in Indonesia and 3.1%-points in Philippines) and started to recover only in 2005-06. In Philippines it finally reached its pre-crisis level in 2005, whereas in Indonesia unemployment remains still at a level of 9.1%, which is much higher than the pre-crisis level of 4.4% in 1996. In Korea, Malaysia, and Thailand unemployment rates had declined to quite low rates during the post-1980s (in Korea and Thailand since late 1980s and in Malaysia since 1992) due to the powerful employment creation capacity of the economy, which only lasted until the crisis of 1997, and unemployment rates increased after the crisis in these cases as well. In Korea unemployment rate has increased from 2.6% in 1997 to 7.0% in 1998, and despite the recovery that already started in 1999, it is still higher than its pre-crisis level as of 2007 (3.2%). In Turkey, the unemployment rate had been stable albeit at a high rate during the era of liberalization, but increased significantly since the recent crisis of 2001, reaching to 10.5% in 2003 from a level of 6.5% in 2000, where it stabilized at a rate of 10.0% as of 2007. In Argentina the partial recovery since 1997 was completely reversed after the 2001 crisis with unemployment increasing from 14.1% in 2000 to 19.6% in 2003; the recovery since 2004 finally took unemployment back, but it is still at a high level of 9.5% as of 2006. In Mexico, unemployment rate increased from 4.2% to 6.9% in one year after the 1994 crisis, returned back to pre-crisis level only after three years, and is again increasing since 2002. In Brazil there was an increasing trend since 1980s in unemployment, which went on after the crisis of

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<sup>4</sup> This equation to be estimated here is a reduced form derived from a model, where distribution is jointly determined via wage bargaining by workers, price setting by firms, and improvements in productivity. The price setting behavior also includes the imported inputs, where the pass through effect of the depreciation of the local currency also becomes important.

<sup>5</sup> The variable "contraction of GDP during a recession" is growth of GDP multiplied by a dummy variable for recession years, which is defined as a decline in manufacturing value added, which in all cases also correspond to a decline in GDP or per capita GDP.

1998. Overall in six out of these nine countries (Indonesia, Korea, Thailand, Malaysia, Turkey, Brazil) unemployment rates are still higher than the pre-crisis levels. During the crisis episodes the increases in unemployment goes along with the decline in the wage share. Furthermore as high unemployment rates suppress real wages, the decline in the share of wages contributes to the aggregate demand deficiency, making it worse for the recovery and job creation capacity of the economy.

Figure 2

### **3.1.3 Economic policy and their effects on distribution**

The changes in monetary as well as fiscal policy have important effects on the wage share as well. The currency crises in particular have resulted in hikes in the real interest rates, which usually do not return to the previous levels for a long time –in some cases up to six to seven years later (Onaran, 2008b). The hikes in interest rates also have spillover effects on other countries. Even when the crisis does not directly affect the country, as in the case of Chile, Mexico and Turkey during the Asian crisis, interest rates still increase for a while. Connected with that, the composition of the budget expenditures of the government reflect clearly how the state is involved in the process of income distribution during the crisis. As the share of wages in government expenses contract, the share of interest payments increases in most cases (Onaran, 2008b). While the demands of international and domestic borrowers are met, wages and social expenditures and investment have to take their shares of budget cuts. Right after the crisis, the conditions of the IMF are usually accepted, and the initial bail out credit to save international firms arrives. Public debt increases as guarantees to the financial systems and large firms are satisfied and running primary surpluses becomes the major duty of nation states. Privatization, mostly in the form of a cheap sell out to foreign capital supplies the additional resources for the country to pay back its ever growing debt. The ideological discourse about the so-called inefficiency of the state is supporting this process and further arresting the social expenditures and state investments. Since governments choose or are obliged to choose not to raise taxes or default on their creditors sufficiently, public deficits end up being paid by labor. Public wages are adjusted. Declines in private sector wages follow as the fear of job loss grows due to possible downsizing or bankruptcies. Eventually, the growth potential of the economies is deteriorated due to increased fragility, higher interest rates, volatility, and lower investment, with further adverse effects on labor. Onaran (2008b) estimates the change in the wage share in the economy as a function of the share of interest payments in total budget expenditures or the real interest rate (current and lagged) for the post-1980 period, and finds a negative effect in seven out of ten countries (Argentina, Indonesia, Korea, Malaysia, Mexico, Thailand, and Turkey).

It is also interesting to note that government expenditures do not play a counter-cyclical role during the crisis years, and in some cases continue to contract for two years or more after a crisis. Fiscal contraction creates further negative effects on wages, apart from its direct effects through reduced demand. Government expenditures in health and education have the effect of decreasing the costs of the consumption bundle of the workers to the extent these services are provided free or at a low price. The budget cuts mostly target these items of expenditure, eroding the bargaining power of labor further by increasing its dependency purely on wage income. Estimation results in Onaran (2008b) show that the ratio of the government final consumption expenditure to GDP has a positive effect on the wage share in seven out of ten countries (Brazil, Chile, Malaysia, Mexico, Philippines, Thailand, Turkey).

The proper response to the crises would have been to repair the damage by financial liberalization by reconstituting capital controls and creating an effective system of financial

regulation, while being responsive to the needs of the people, as opposed to the domestic and international capital. However, quite contrary to that as we have observed during the Asian crisis, the IMF conditionality credit imposed high interest rates and restrictive fiscal policy, which led to a severe recession, unemployment, and credit crunch. The IMF policies turned a liquidity crisis into a solvency crisis, as the nation state was denied any intervention (Taylor, 1998). This created the ground for foreigners to buy Asian firms and banks at rock bottom prices (Crotty and Lee, 2002). In the meantime, the crisis not only prepared the ground for opening Asia to the interests of foreign investors to full extent, but also resolved the accumulated conflicts between domestic capital and labor. Crotty and Lee (2004) emphasize the importance of the crisis episodes for facilitating the radical neoliberal restructuring which could not be achieved through democratic process under normal economic times. In a country like Korea, which has been reasonably prosperous, only during the times of crisis, the panicked public can be led to believe that failure to accept IMF dictates would be even more disastrous than their implementation, and a new labor law can be passed without too extensive mobilizations. The same story has been true in most other developing countries, e.g. Turkey. At best not daring to upset the domestic and international investors, or mostly being in close ties to the big corporations via either ownership or financing of their election campaigns, the politicians in power are taking active steps for a pro-capital redistribution of income via taxation and expenditure policies. The need to run high primary surpluses is being presented as the objective truth, although it in reality is just the obvious tool to continue the payments of the interest on debt. The only exception to this generalization has been Argentina in 2001, where the extent of the popular unrest and self-organization of the masses has managed to pressurize the government to be disobedient to further austerity packages, and consequently default on debt, and increase the focus on social policy, although without any fundamental shift in economic strategy.

### **3.2 Empirical evidence: Japan**

The wage share was declining since late 1970s in Japan, and with the crisis the first stage was just a stagnation or slight decline in the wage share as can be seen in Figure 1b. This is quite different from the emerging markets. A general property of the post-war Japanese economy related to the job security of core workers played a role in this development: “labor hoarding” during contractions and “increasing returns to scale” during expansions (Uemura, 2008). During the recession in the 1990s the real wage declined moderately (in 1992-93, 1997-99), but also there has been slight recoveries in between (in 1994-96) as can be seen in Figure 3. The nominal wage increases as well as the deflation of 1994-96 contributed to this process. Nevertheless, except for 1994 and 1998 the difference between the wage and productivity changes was always negative (Figure 3), leading to a continuous decline in the wage share. Starting from 1998, we also observe nominal wage declines in the deflationary environment (1998-99, 2002-04, 2007) as well as wage freezes (2000, 2005-06, 2008). The firing of many workers in the first half of the 2000s has been influential in this process. After the recession, the institutionalized wage co-ordination mechanism was also almost broken down (Uemura, 2008). The employment system has also evolved in the Japanese economy since the recession. As a measure against labor hoarding in large Japanese firms, the number of non-regular workers increased dramatically; there has also been a shift towards unstable service jobs (Uemura, 2008). All these developments have led to a weakening in the bargaining position of unions and the suppression of nominal wage growth. Overall the wage share decreased by 10.6% as of 2007 compared to 1998, and 8.9% compared to 1992. The decline in the wage share contributed to a decline in domestic demand, and exports became an important source of demand again in Japan, which also increased the pressure of international competition with the other Asian countries and the increasing number of foreign affiliates of the Japanese multinational firms (Uemura, 2008).

Figure 3

In the meantime employment in the total economy first stagnated during 1992-95 and after a slight recovery decreased in absolute terms during 1997-2003 (see Figure 4a). The recovery since 2004 barely brought employment to the level of 2001 as of 2007. The decline in employment led to a strong and continuous increase in unemployment from a level of 2.1% in 1991 to 5.4% in 2002 (see Figure 4b). Despite the recovery since 2003, unemployment as of 2007 is still higher than in 1997. Although the unemployment rate in Japan in its peak point is still lower than in most other advanced countries, it is important to realize that drastic increases in unemployment can radically change the industrial relations and wage bargaining process in a persistent way. In the meantime, the unemployment rate of elderly male increased much more, but the most dramatic increase has been in male youth unemployment (aged 15-24) increasing from 4.5% in 1990 to 11.6% in 2003 (see Figure 4b). Long term unemployment also increased from 0.3% in 1992 to 1.7% in 2003 with the incidence of unemployment (persons unemployed for a period of one year or beyond as a percentage of the total unemployed) increasing to 33.7% in 2004. These adverse developments in unemployment took place despite a strong decline in male as well as female labor force participation rate, which declined from 64.1% in 1992 to 59.6% in 2007 (see Figure 4c). It is also worrying that the decline in the labor force participation rate is persistent despite the recovery in employment and unemployment; it can be argued that the discouraging effect of the crisis and the deterioration in the working conditions have had a permanent effect.

Figure 4

#### **4. Possible effects of the recent global crisis**

The current global crisis forms the biggest policy challenge since the Great Depression given that this is a global not a regional crisis; it originates from the core and spreads to the periphery. There is now a global credit crash, and more innovative financial system means more risk and a wider contagion. Export market contraction will make recovery harder. As the previous imbalances of debt-led growth is now being corrected, it is unclear where the recovery will come from. What will be the effects of the current global crisis in different countries? We need to distinguish four different groups of countries:

1. The *developed countries* seem to be experiencing the crisis different from the former cases of crises in the developing countries thanks to their fiscal capacity to somewhat weather the shock. The immediate decline in interest rates, credit lines to domestic banks, counter-cyclical fiscal policy (albeit at a lower degree than the financial rescue packages) are measures that were formerly denied to the developing countries by the IMF as well as the advanced countries of the core. Indeed in the developing countries the conditionality credits of the IMF had made use of the crisis to impose further measures of liberalization. However despite this crisis management, the real effects in the developed countries are much stronger than the previous stock market or banking crises of the 1980s. The size of the future effects depends on the size of the fiscal stimulus plans, but some patterns emerge. The effects of the credit crash, particularly in countries with high household debt (e.g. US and UK), will be severe. The multiplier effects of the credit crash as well as the decline in consumption have already started to affect investments. The pessimistic expectations will amplify the decline of both consumption and investments. In countries like Germany or Japan with a high degree of dependence on export markets the contraction will also be severe, and the reliance on low wages to expand export markets will prove to be a curse. In some EU countries' the ability to respond to the shocks will also be constrained by their fiscal capacity. Furthermore there are strong real and nominal divergences within the EU15 as well as EU27, which are now

becoming even more major problems in the face of the crisis. These differences are also being priced by the financial investors, who demand higher interest rates on the government bonds of the countries like Italy, Greece, Spain, and Ireland compared to the interest rates on German bonds. Austria is also belonging to this camp with high spreads on government bonds due to its “Eastern European” exposure.

Broadly speaking the negative effects of the crisis on labor in the developed countries will work through demand, bargaining power, and path dependency channels. The decline in the wages in the emerging markets, which will suffer from the global crisis, will also add further international competition pressures. Other additional channels of negative effects will be through the housing debt, which will have strong distributional consequences for the indebted households. Differences with respect to skill levels and further dispersion of within labor distribution are also to be expected, e.g. the temporary workers losing their jobs first, and the more qualified workers are being hoarded; however some skilled workers in the automotive or metal industry or finance have already been the first to be affected. Furthermore the future cuts in governments’ social expenditures, if they are faced by financing pressures, will also asymmetrically affect labor. Two differences to the former crisis in the developing countries can be expected: a) the dimension of the initial recession might be more moderate, but given that we are facing a global recession, the recovery in economic activity can last much longer, bringing in worries about an “L” type of recession, but much stronger than the Japanese experience of the 1990s, given the global dimension of the crisis. Thus the negative labor market effects could be less severe at the beginning, but might persist and deteriorate further. b) An inflationary shock will not accompany the credit crisis in the developed countries, which may offset the other negative effects on real wages in the first year. Dramatic increases in inflation in the case of the developing countries had been due to the collapse of currencies. Nevertheless, in case the recession persists longer, the pressure on real wages and the bargaining power of labor will intensify. The worst case scenario of deflation can bring further major risks to these economies as can be seen from the case of Japan in the 1990s and 2000s.

2. During this global crisis, many *developing countries* with a former crisis history are once again experiencing a crisis led by speculative capital outflows, despite significant differences in the fragility of their economies. Speculators seem to fail to distinguish between countries like South Korea and Argentina, which do not have significant current account deficits or even have current account surpluses, vs. countries like Turkey with a high current account deficit, and dependency on capital flows. While the former developing country group is suffering from a crisis, which they have not created, the countries with current account deficits (e.g. Turkey, South Africa) might suffer through a deeper bust, due to the accumulated fragilities during the speculation-led boom cycle. The dependency on export markets, which are now shrinking, is adding another dimension to the fragility. If the capital outflows triggers another currency crisis in the countries with high current account deficits, the effects on wages, employment, and labor share can be expected to be quite similar to the previous experiences summarized in section 3. Although with alternative policies, this destiny can be reversed, as of now in those countries with current account deficits (e.g. Turkey), which apply for IMF credit, the IMF policies are again much more restrictive than what IMF finds appropriate for e.g. Germany. Capital controls to avoid speculative outflows are not even mentioned.

3. The emerging markets of *Eastern Europe* are also being threatened by credit crash and capital outflows, and possible currency crisis accompanying the banking crisis. After the initial transition shock and a decade of restructuring, these countries will once again face the costs of integration to unregulated global markets. For these countries learning from the

experience and the policy mistakes of the former crises is extremely important. It is also important to learn from the crisis management techniques of countries like Malaysia through capital controls. The degree of accumulated imbalances including current account deficits, exchange rate appreciation, and foreign-currency denominated private debt will determine the differences in the depth of the effects among these countries. Hungary, Bulgaria, Romania, Serbia, Croatia, Baltic Countries, Ukraine, and Russia are more exposed than Poland, Czech Republic, Slovenia, and Slovakia. But even the latter group might suffer from the contagion effects, the slowdown in global demand, the decline in FDI inflows, and the contraction in remittances. Excessive dependence on export markets and as in the case of Slovakia a dangerous specialization in the automobile industry will turn out to be a major risk. In the more fragile case of Hungary it is yet to be seen whether the huge international rescue package will remain in the country, or whether it will in the future turn into bailing out the international investors. The problematic pegs of the Baltic States and Bulgaria require even larger international rescue packages in comparison to the size of the economy, which might not be possible if the EU funds contract due to problems in the core countries. The results for non-EU countries like Ukraine, Russia, or the South-Eastern Europe can be more devastating. Russia, also with a former crisis record and a more intense reliance on market-based finance, is already under the pressure of further devaluation. When capital outflows accompany a financial crisis, the distributional effects are also expected to be heavier, as was the case during the Asian or Latin American crises. The contagion effects in the region would also be dangerous. The ability of parent banks to maintain the credit booms in the region is exhausted, and even without further capital outflows, the region will suffer from a deeper recession than in the West. The spillovers from currency depreciations, and increases in non-performing loans will further affect the parent banks' approach to the Eastern affiliates.

4. In the case of other developing countries like *China, India, and Brazil*, although the contagion effects and the slow-down in global demand will be an important problem, and the myth of decoupling of demand in these countries proved to be a case of wishful thinking, these countries could manage the crisis based on their large domestic markets, if they could make a policy shift away from pure dependence on export orientation based on low labor costs. The recent state expenditure program in China is an indicator of its ability to intervene, but the results are yet to be seen. The recent mass layoffs in China are creating doubts about the responsiveness of the government to make the issue of inequality a part of crisis management.

A common question for all country groups is how the asset price deflation will affect the wealth distribution. A usual optimistic expectation is to hope for a more equal wealth distribution; however this point misses the coming process of concentration of wealth. Moreover the power of the wealthy is not being disturbed so far with the policy reactions; quite on the contrary the makers of the crisis have been the first to be saved without any serious penalties or conditions, and the state is operating as an economic partner for them.

## **5. Policy implications**

The answer to Hyman Minsky's question on whether a crisis like the Great Depression can happen again in an unregulated financial economy, proved to be yes; and the only reason why it may not reach the dimensions of the Great Depression is that the states have been called into action with rescue packages of unforeseen amounts. The neoliberal economic thinking and policy making is going through a deep legitimacy crisis. Indeed the generous bank rescue packages are the confession about the failure of the neoliberal economic policy. Even the CEO of the Deutsche Bank, Ackermann, declared that he has lost trust in „the self-healing abilities of the financial system”. Greenspan, ex-chief of the FED has said „I have



made a mistake in presuming that the self-interests of organizations, specifically banks and others, were such that they were best capable of protecting their own shareholders' and their equity in the firms". As the dimension of the crisis becomes obvious, the call for a more relevant fiscal policy response is also getting stronger, e.g. by Bernanke as well as IMF President Strauss-Kahn. The current insistence of Germany on the requirements of the Stability and Growth Pact about budgetary discipline is now being criticized even by the IMF (Schrörs and Pache, 2009). However other than some concern about the CEO pays, and bonus structures, nothing is being said about the solution of the distributional dimension of the problem. In order to formulate the correct policy response to the crisis, it is again important to remember the big picture behind the crisis: This is not just a crisis of improperly regulated markets, but also a crisis of unequal distribution, and it should be asked why labor should go on paying the costs of this crisis further. The major crisis calls for a major policy restructuring:

a) First fiscal policy has to incorporate a public employment program, and a distributional policy to reverse the negative demand effects of the crisis. Public expenditures in labor intensive services like education, child care, nursing homes, health, as well as in public infrastructure and green investments are important areas of target.<sup>6</sup> These are also areas to redirect the economy towards a sustainable as well as solidarity-oriented development. Gender aspect of the public employment programs should also be carefully designed in order to not only avoid disadvantages for women but also increase the female employment share. Otherwise a typical outcome of crises is either declining labor force participation by discouraged women or high female unemployment rates due to the increased need to work as a secondary breadwinner in the household in a period of low job chances.

As part of the employment programs it is important to avoid the "socialization of the costs", i.e. to prevent that the working people and the unemployed pay the costs of the irresponsible behavior of the global capital. Particularly some firms might be making use of the crisis to implement their long-term downsizing strategies. Other firms are using the "short work" regulations to preserve their profits, while the workers suffer from loss of income because of the shorter work hours and public sector pays part of the lost income as a transfer to the workers. The prevention of the "socialization of the costs" requires strict measures to avoid lay-offs: in firms that are in a position to distribute dividends, the logical thing would be to ban lay-offs. Furthermore "no lay-offs without a public restructuring and employment plan" should be imposed as a condition to banks that enjoy the funds of the bank rescue packages. Also such banks should be obliged to extend credits to priority sectors and firms under conditions set by the government through transparent and participatory mechanisms. Such firms that receive credits through conditionality channels should be demanded to stop lay-offs as well. In cases of sectors that are under the threat of mass layoffs, like the auto industry, socialization of the firms should be considered. In such sectors, if it is clear that there is an overcapacity, restructuring of these public firms as part of a medium-term plan should be considered, e.g. in the auto industry a shift of focus towards the production of public transport vehicles in the existing firms, and a gradual transfer of the human capacity towards new innovative sectors.

The tax rebates/subsidies on low income groups or extension of unemployment benefits to those workers who are unable to access unemployment benefits are important short-run solutions. However this is not a substitute for the requirement to correct the overall deterioration in the labor share. This is not only an egalitarian but also macroeconomic concern. The usual wage moderation of the European macroeconomic policy mix can indeed

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<sup>6</sup> See Pollin (2008) for a detailed outline of the employment program for the case of US.

only worsen the demand deficiency problem now. The risk is not the excessive budget deficits but rather the persistence in the low wages in some countries like Germany.

For the finance of an extensive stimulus package budget deficits are in the short run reasonable. But more progressive income and wealth taxes, higher corporate tax rates, inheritance tax, tax on financial transactions are the only way to make the responsible pay for the costs of crisis. This is also the only way to avoid future budget cuts in social expenditures, education, health, child and elderly care.

b) In order to fundamentally solve the problems of this crisis, economic policy must most of all solve the distributional crisis. A new socio-economic and political paradigm is required focusing on full-employment, productivity led wage growth, and a shortening of work-time. This process should also decide on critical sectors for the society, in which the ownership rights cannot be left to the private sector and private profit motive. The crisis has indicated that the finance and the housing sectors are clear candidates for public ownership enhanced with democratic and transparent control mechanisms of all the stakeholders. The energy crisis is indicating that the energy sector and alternative energy investments also require public ownership. The problems with the private pension funds as well as private supplies of education, health, and infrastructure are showing that social services are also too critical to be ruled by private profit motives. A creative and participatory public discussion should question, in which other sectors public ownership would produce more egalitarian as well as more efficient outcomes. This does not mean to praise the public sector as such, but calls for the participation and control of the stakeholders (the workers, consumers, regional representatives etc.) in the decision making mechanisms within a public and transparent economic model. Such a shift in decision making also facilitates economy wide coordination of important decisions for a sustainable and planned development based on solidarity.

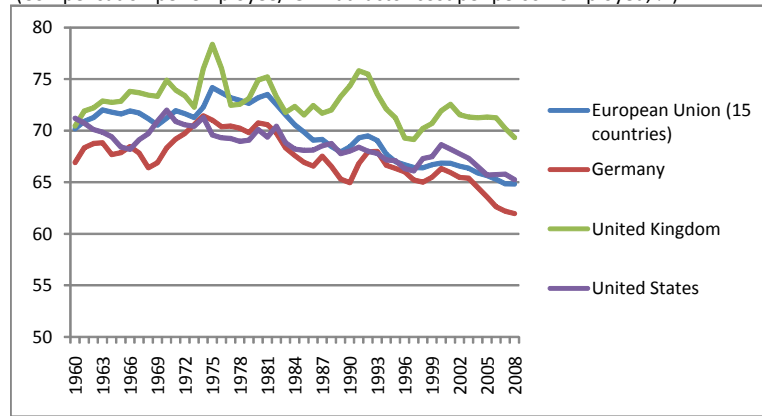
c) Next the redesign of the financial sector is urgent, on which most of the alternative literature is also focusing. However regulation is important but not enough; the financial institutions have an amazing capacity to avoid regulations through new innovations. Thus there is need for a large public finance sector to foster stable growth.<sup>7</sup> The crisis has shown us that large private banks are exploiting their advantage of being “too big to fail”. The large private banks should be broken down and converted into publicly useful units. The financing of the activities through the capital markets should be limited. But these are not enough; the challenge is the finance of socially desirable large new investments, e.g. in the energy sector. This requires a detailed historical analysis of the benefits that had been received from large development and investment banks as well as regional, cooperative banks. Again here it is important to emphasize that state ownership alone is not the solution; the participation of the workers and other stakeholders to decision making, and the transparency of the accounts are important. Only based on this structure, the following financial regulations can be pursued further to deliver socially desirable outcomes: full regulatory over-sight for all financial institutions, full accountability of the decision makers, counter-cyclical capital requirements, a public auditing agency to monitor also the release of new financial products; the elimination of off-balance sheet instruments (see e.g. Crotty and Epstein, 2008; ATTAC, 2008 for details of an alternative regulatory framework).

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<sup>7</sup> See Euromemorandum Group (2008) as an exception in the literature on policy alternatives, which also emphasizes the nationalization and democratic control of a relevant part of the banking sector, and not only for the already “nationalized” part of the sector during the crisis, but in principle. Epstein’s (2009) proposal of a “good bank” in public hands as opposed to the “bad bank” solution is also opening the way for a large national financial sector. He suggests that the government should buy the good assets, and not the bad assets from the banks. If the banks do not want to sell the good assets to the government, and if later they are unable to survive alone, then the government could “take the bank over for much less, or for nothing at all” (Epstein, 2009).

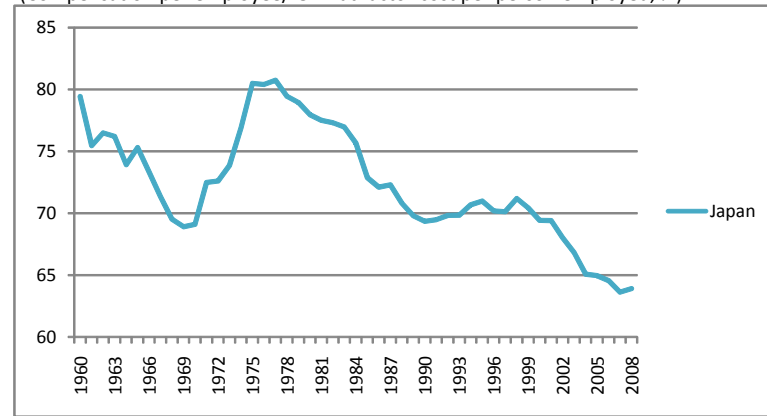
d) Last, but not least the crisis has important policy implications for the global dimension. Labor in the North and the South (or the East and the West) has more common ground than they currently exploit. Thus redefining the rules of the game, coordinating the institutional setting of the global economy is the only alternative to readjust the playground to create conditions that are fairer to labor. Nevertheless creating a consensus around these targets in the North as well as the South also requires a systematic global policy on international redistribution and development. How or whether the North supports the South in weathering the current global crisis will also be important in creating positive signals for global cooperation. This defines new roles and tasks for the trade unions in each country, since they are the political agents who have interest and the potential to push for such a shift in policy at the global level. The main cornerstones of a new solidarity oriented global economy are trade and industrial policy consistent with development, a new global monetary regime with fixed exchange rates, and controls on capital flows. The latter is not only about the shutting-down of off-shore tax heavens, but also includes a tax on all financial transactions as well as quantity controls on capital flows. The tax revenues from financial transactions can also serve to build up a fund for the global investments for facilitating convergence.

Figure 1a: Adjusted wage share, total economy, EU & US (1960-2008)  
 (Compensation per employee/ GDP at factor cost per person employed, %)



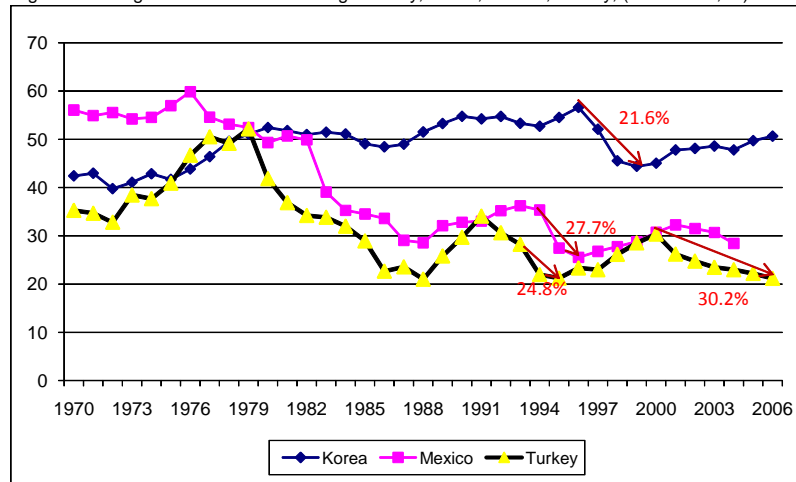
Source: AMECO, online macro-economic database of the European Commission's Directorate General for Economic and Financial Affairs

Figure 1b: Adjusted wage share, total economy, Japan (1960-2008)  
 (Compensation per employee/ GDP at factor cost per person employed, %)



Source: AMECO, online macro-economic database of the European Commission's Directorate General for Economic and Financial Affairs

Figure 1 c: Wage Share in Manufacturing Industry, Korea, Mexico, Turkey, (1970-2006, %)



Source: OECD STAN for Korea and Mexico, and for Turkey Annual Survey of Employment, Payments, Production and Tendencies in Manufacturing Industry by the Turkey Institute of Statistics

Figure 1 d: Wage Share in Manufacturing Industry, Indonesia, Malaysia, Philippines (1970-2003, %)

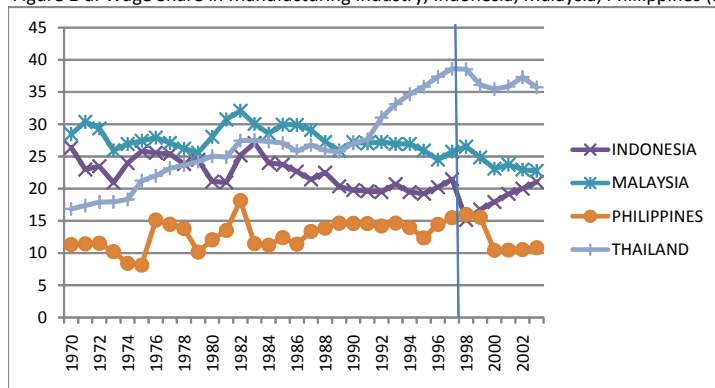
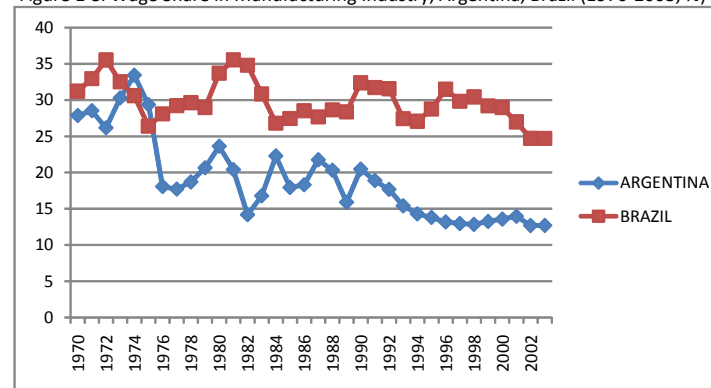
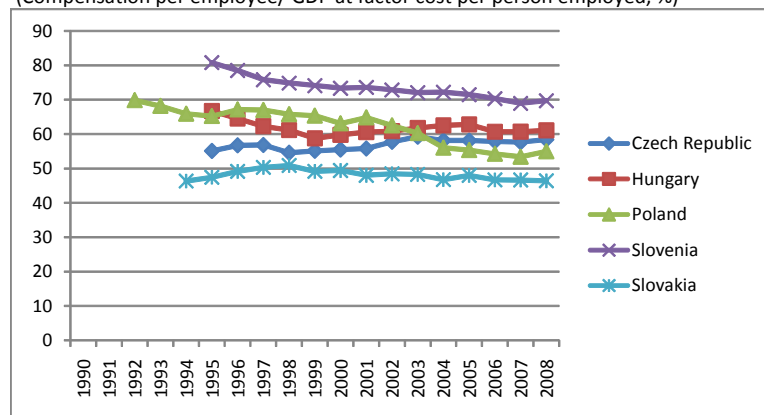


Figure 1 e: Wage Share in Manufacturing Industry, Argentina, Brazil (1970-2003, %)



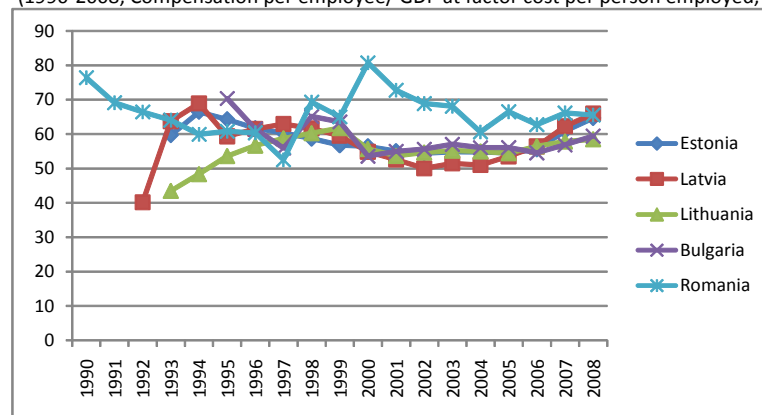
Source for Figure 1d&e: For Brazil, Philippines, and Thailand, the UN manufacturing data is combined with the World Development Indicator (WDI) database of 1993, which report manufacturing wages and employment, and for Argentina, Indonesia, and Malaysia WDI data is combined with the Economic Intelligence (EIU) database based on percentage changes.

Figure 1f: Adjusted wage share, total economy, Eastern Europe (1990-2008)  
 (Compensation per employee/ GDP at factor cost per person employed, %)



Source: AMECO, online macro-economic database of the European Commission's Directorate General for Economic and Financial Affairs

Figure 1g: Adjusted wage share, total economy, South-Eastern Europe and Baltic Countries (1990-2008, Compensation per employee/ GDP at factor cost per person employed, %)



Source: AMECO, online macro-economic database of the European Commission's Directorate General for Economic and Financial Affairs

Figure 2a: Unemployment rate, Selected Countries in South-East Asia (1980-2007)

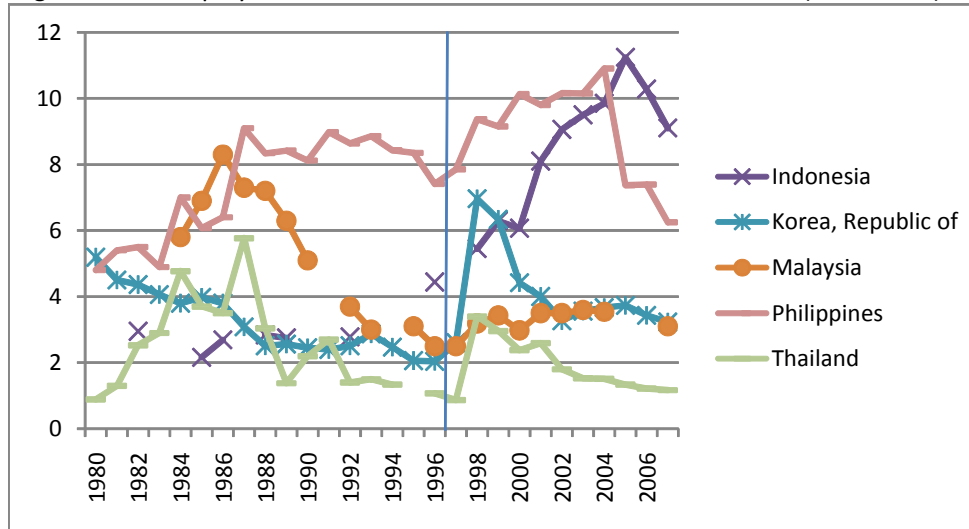
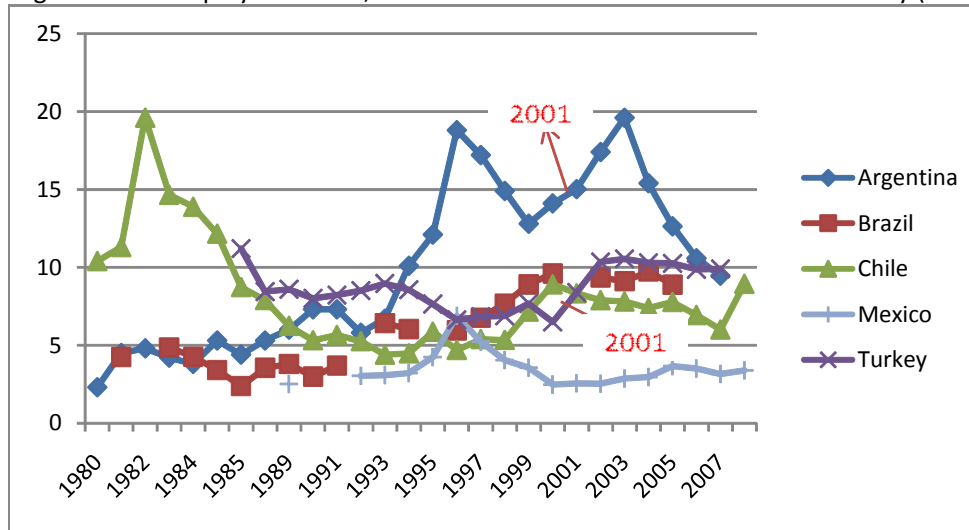
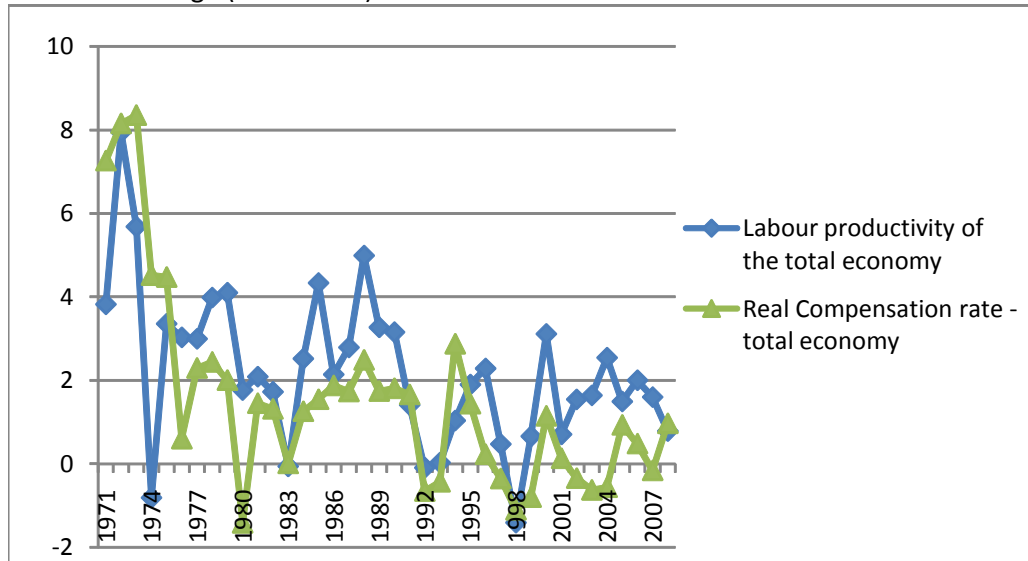


Figure 2b: Unemployment rate, Selected Countries in Latin America and Turkey (1980-2007)



Source: ILO online database on the Key Indicators of the Labour Market (KILM)

Figure 3: Labour productivity and real compensation rate, total economy, Japan  
Annual % change (1971-2008)



Source: OECD Economic Outlook



Figure 4a: Employment, Japan (in thousands, 1980-2007)

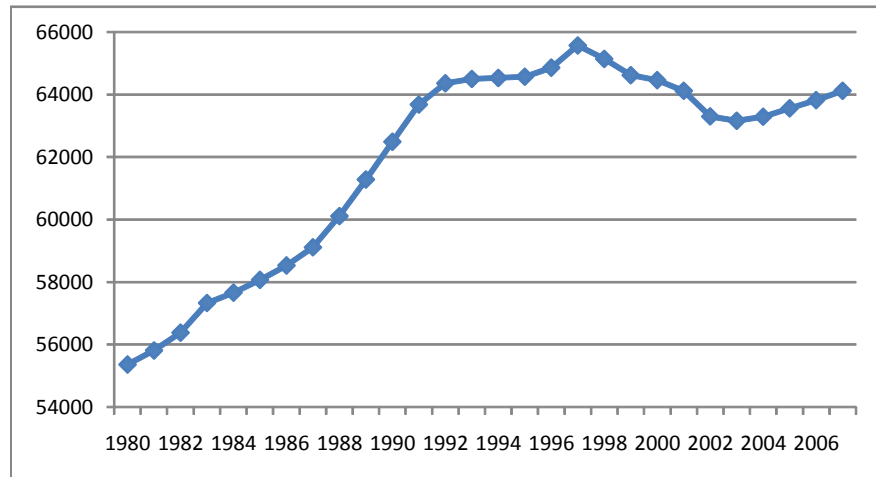


Figure 4a: Employment, Japan (% , 1980-2007)

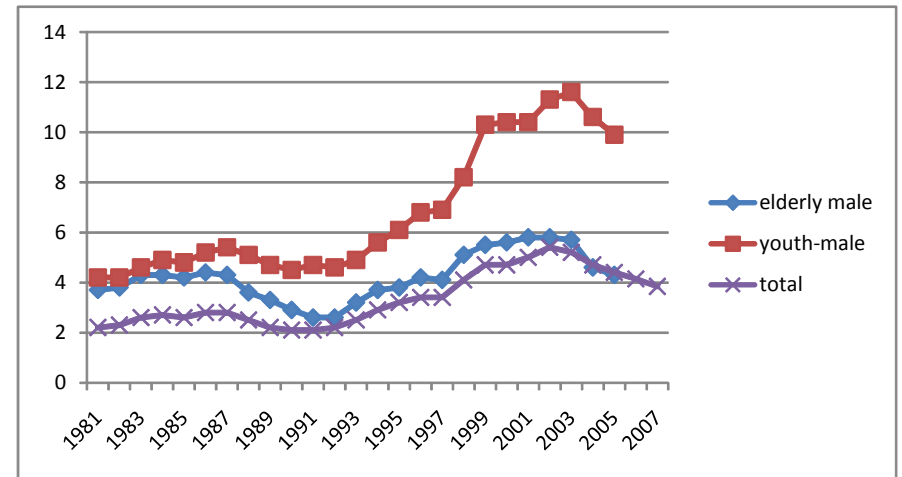
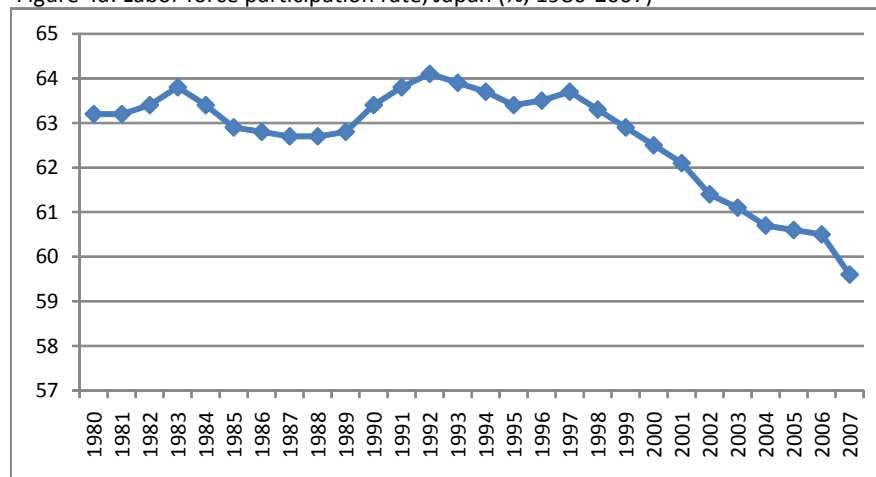


Figure 4a: Labor force participation rate, Japan (% , 1980-2007)



Source: ILO online database on the Key Indicators of the Labour Market (KILM)

**Table 1: The sources of the change in the wage share in manufacturing industry during a crisis**  
Annual % change in

	Exchange rate (local currency/\$)	Real exchange rate (local currency/\$)	Real value added	Wage share (Wage bill / value added)	Real wage per worker (deflated by CPI)	Employment	Productivity (Real value added / employment)
<b>Korea</b>							
1998	47.32	37.02	-7.90	-12.58	-2.10	-13.74	6.78
1999	-15.17	-15.86	21.77	-2.48	4.92	2.24	19.11
2000	-4.87	-6.97	16.98	1.45	5.65	6.80	9.53
<b>Mexico</b>							
1982	130.07	44.77	-2.74	-1.60	-3.16	-2.04	-0.72
1983	112.93	5.53	-7.84	-21.74	-22.46	-7.13	-0.76
1984	39.75	-15.58	5.01	-9.63	-6.15	2.07	2.89
1995	90.20	40.89	-4.94	-22.25	-13.07	-5.31	0.39
1996	18.38	-11.90	10.83	-7.07	-8.62	6.88	3.70
1997	4.20	-13.62	9.94	4.89	-0.52	8.79	1.06
<b>Turkey</b>							
1980	144.67	16.41	-6.21	-19.76	-38.50	1.17	-7.29
1981	46.27	7.10	10.33	-11.88	11.05	1.42	8.78
1982	46.16	11.71	6.36	-7.19	-2.17	3.76	2.50
1994	169.55	30.68	-5.60	-22.22	-14.14	-4.27	-1.39
1995	54.84	-17.69	11.80	-3.31	-0.15	4.08	7.42
1996	77.57	-1.54	7.50	9.98	-5.14	6.82	0.65
2001	96.03	26.96	-8.05	-24.27	-27.60	-2.94	-5.26
2002	22.98	-15.17	8.20	-5.51	-11.39	0.61	7.54
2003	0.42	-19.85	8.44	-5.23	-10.08	1.82	6.50

Note: The real wage is deflated by CPI, whereas productivity is calculated based on real value added deflated by PPI. Thus the difference in the % change in the wage share and the % change in the real wage-% change in productivity is the differences in inflation rates in CPI and PPI.

Source: See Onaran (2009) for details. Own calculations based on OECD STAN for Mexico and Korea, and Annual Survey of Employment, Payments, Production and Tendencies in Manufacturing Industry for Turkey.

Source for the exchange rate and CPI is World Bank World Development Indicators. Real exchange rate is deflated by CPI.

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