Core International Labor Standards and the World Trade Organization

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ABSTRACT

This class exercise can be used in undergraduate international business or economics classes to illustrate the economic effects of trade agreements on developed and developing economies.

LEARNING OBJECTIVES

Upon completion of this exercise, students should be able to explain: (1) how countries are truly part of a "global village" and their public policy decisions have impacts beyond their borders; (2) that countries are interdependent and therefore must exhibit an awareness and sensitivity about the international impacts their policies will have on their trading partners; (3) the economic impact of international labor standards on consumers, producers, and workers in all countries, developed and developing; (4) that international trade agreements require countries to make concessions to reach consensus in negotiations.

INTRODUCTION

The forces of globalization have sparked an ongoing debate between developed and developing countries regarding adherence to international labor standards in international trading agreements. Developed countries are proposing that all member countries of the World Trade Organization require minimal core labor standards in all trade agreements between member countries. Developing nations, on the other hand, realize that the adoption of such standards could negate the comparative advantage they have in trade with developed countries. Will these two opposing factions be able to reconcile their interests and reach a consensus to develop a uniform code of conduct to protect labor rights in international trade agreements?

THE WORLD TRADE ORGANIZATION

With headquarters in Geneva, Switzerland, the World Trade Organization (WTO) came into being on January 1, 1995, replacing the General Agreement on Tariffs and Trade (GATT). It is the only international organization dealing with the global rules of trade between nations. Its main function is to ensure that trade flows as smoothly, predictably, and freely as possible. At the heart of the system — known as the multilateral trading system — are the WTOs agreements, negotiated and signed by a large majority of the world's trading nations, and ratified in their parliaments. These agreements are the legal ground rules for international commerce. Essentially, they are contracts guaranteeing member countries important trade rights. They also bind governments to keep their trade policies within agreed limits to everybody's benefit. The agreements were negotiated and signed by governments. But their purpose is to help producers of goods and services, exporters, and importers conduct their business, while protecting the interests of consumers. The goal is to improve the welfare of the peoples of the member countries. Presently, over three-quarters of WTO members are developing countries.

One of the main accomplishments of the WTO is the dismantling of tariffs and other protectionist devices that have served to reduce the volume of world trade. Trade liberalization (the reduction of trade barriers) continues to be a central focus of the WTO. Unfortunately, the opening of trade between countries may cause unemployment in importing countries as cheaper imports replace the production of domestic goods. In this case, the affected import-competing industry may appeal for protection by petitioning the Government to impose tariffs or quotas on these imports. Such protectionist policies represent an affront to the free trade initiatives being promoted by the WTO. Specifically, there exists a tension within the WTO between developed countries and developing countries regarding trade in labor-intensive exports from developing to developed countries. The WTO is trying to resolve this conflict by establishing a Code of Conduct that would be agreeable to all sides and would establish trading rules and guidelines for the conduct of world trade.

Recognizing the widely divergent levels of economic development between the world's nations, the WTO has arbitrarily categorized and grouped countries according to their respective per capita income levels. The high income countries (HICs) are those with per capita incomes over $10,000 per year; the upper middle income countries (UMICs) are those with annual per capita incomes between $3,100 and $10,000; the lower middle income countries (LMICs) and lower income countries (LICs) are those with per capita incomes below $3,100 (see Table 1). It is common to refer to the HICs as "developed" countries and the other three country groupings as "developing" countries. The vast majority of the world's countries are in the latter category. Obviously the standard of living of the population and the well-being of laborers differ markedly in the three groupings.

TABLE 1: COUNTRY GROUPINGS

High Income Countries (HIC)	Upper Middle Income (UMIC)	Lower Middle Income (LMIC)	Lower Income (LIC)
GDP/Capita > $10,000	**GDP/Capita $3,100-10,000**	**GDP/Capita $800-3,100**	**GDP/Capita < $800**
Australia	Argentina	Bolivia	Ghana
Canada	Brazil	Bulgaria	India
France	Chile	China	Indonesia
Germany	Mexico	Costa Rica	Kenya
Greece	Poland	Ecuador	Nigeria
Ireland	South Korea	Egypt	Nigeria
Israel	Turkey	Iran	Vietnam
Italy		Morocco	Zambia
Japan		Peru	Zimbabwe
New Zealand		Philippines	
Portugal		Russia	
Saudi Arabia		South Africa	
Singapore		Thailand	
Spain			
Sweden			
U.K.			
U.S.A.			

Source: World Bank 2007

CODE OF CONDUCT ELEMENTS

A strong movement initiated by the HICs within the WTO has developed to establish a Code of Conduct that addresses labor rights. Once agreed upon, this Code of Conduct shall be universally applied. The recommendations are non-binding instruments which prescribe guidelines to be used in public policy (including trade policy) decisions. These decisions are intended to have significant impacts on working conditions and practices in all WTO member countries. When ratified, these guidelines will oblige countries to use means appropriate to national circumstances to promote these goals and to be able to demonstrate progress over time in achieving them. With this in mind, the WTO membership has agreed to enter into negotiations for the purpose of deriving a uniform set of rules that would be incorporated into a Code of Conduct for the promotion of labor rights. Failure to adhere to these standards may result in either boycotts or countervailing tariffs imposed on imports from the non-complying country. The final agreement, embodied in the Code of Conduct, will require a 75% approval rate from the voting members.

COUNTRY POSITIONS ON UNIVERSAL CORE LABOR STANDARDS

Labor rights activists, principally in developed countries, contend that it is highly immoral for countries to buy imported goods from countries using "sweatshop labor" working in substandard conditions at subsistence wages. The International Labor Organization estimates that of the 410 million children between the ages of 5 and 14 meeting these criteria, 250 million are employed in Asia (61% of the total), 131 million are employed in Africa (32%), and 29 million are employed in Latin America (7%). In addition to eliminating or curbing the use of child labor, labor rights activists insist that a country's laborers should have the right to join unions and engage in collective bargaining, should receive higher government mandated minimum wages and a guaranteed minimum level of health benefits. Countries that exploit their labor resources to produce low priced products for export should be required to meet minimum international labor standards that will improve the working conditions of their people and raise their standard of living. If these countries do not comply with these minimum labor standards within a reasonable period of time, the world community of nations should impose economic pressure by boycotting their exports, or at the very least, by imposing tariffs and quotas on their exports.

Representatives of the lower income countries (the UMICs, LMICs, and LICs), on the other hand, do not accept the proposition that poorer countries should have to enforce the labor standards of the rich countries in order to escape trade barriers which would cause a loss of jobs. Many in the developing world feel that bringing labor standards into trading relationships is a bid by the industrialized countries to undermine the comparative advantage that developing countries enjoy due to their lower wages. Workers in the factories of developing countries are there because this presents a better alternative than work in subsistence agriculture or other peasant trades. While by rich country standards conditions for labor may seem oppressive, workers employed on farms or in factories producing goods for export are better off than those employed in the production of goods for the local market. If a rich country were to restrict its imports from a developing country, the demand for labor in the developing country would fall, causing unemployment and depressing wages still further, an outcome that the supporters of better labor conditions would surely not want. In many of the very poorest countries, children are a major source of income for the family; barring child labor would make the whole family worse off.

It is important to point out that living conditions and wages are vastly different even within the three categories of the "developing" countries. The standard of living and level of wages in Argentina and Brazil are superior to LMICs Bulgaria and Peru and far superior to the standard of living of Nigeria and Zimbabwe. Not only wage disparities, but also large differences in literacy levels and infant mortality rates are clearly in evidence in each country grouping. Obviously labor standards cannot be made equal in all countries, but the intent is to improve significantly the labor conditions and standards in each country grouping. Many of the lower middle income countries (LMICs) and low income countries (LICs), while agreeing that some form of a conduct code should be adopted, feel that they will not be able to meet the standards required by the high and middle income countries and contend that these standards are a form of disguised protectionism. They claim that labor unions and farmers in these more developed countries want protection from imports that compete with the products they produce. Basically the dispute revolves around the industries in which the lower income countries have a comparative advantage, namely their exports of textiles, agricultural products, and raw materials. Their comparative advantage derives mainly from their low wages in these industries. For the most part, the LMICs and LICs concentrate on producing labor intensive products (textiles) and land intensive products (raw materials and agricultural products) and produce very little, if any, manufactured products that require skilled labor and machinery and equipment to produce. Therefore, workers and businesses in HICs and UMICs that produce such labor and land intensive products are adversely impacted by imports from the lower income countries; workers in HICs and UMICs suffer from lost jobs and lower wages and businesses suffer from lower profits due to the competition from lower priced imports. This sets up a possible alliance between HICs and UMICs whose primary exports are manufactured goods in contrast to the raw materials emphasis in the LMICs and LICs.

OTHER TRADE ISSUES: NEGOTIATION NUGGETS

Although the main focus in the current WTO negotiations is labor rights, there are other trade issues which are important to member countries. Specifically, the HICs would like the developing countries to take action on the following issues: (1) consider imposing environmental regulations on industries that pollute the air and water; (2) lower tariffs on imports of manufactured goods (the UMICs would also support this measure); (3) enforce intellectual property rights to reduce piracy of music and other computer software (the largest offender here is China); and (4) remove or reduce government regulations which limit access to financial services (e.g., banking, insurance). HICs may consider softening their insistence on the adoption of universal labor standards if the developing countries would offer concessions in one of these other trade categories. The HICs may also consider providing educational subsidies to the LMICs and LICs as a quid pro quo for adopting labor standards. In addition the HICs may offer low interest financing for loans to improve infrastructure in the LMICs and LICs.

Developing countries (to include UMICs, LMICs, and LICs) are interested in obtaining concessions from the HICs in the area of tariff reductions on agricultural products (and raw materials) and on the reduction of government subsidies in agriculture. The HICs agricultural sector is heavily subsidized by government, which means that consumers in the HICs pay above world prices for agricultural products, and in order to protect farmers from lower priced foreign imports the government imposes tariffs on agricultural imports. This HIC public policy decision clearly is not in the best interests of the developing countries who depend so heavily on agricultural exports to support their economies. Clearly, if the combination of government subsidies and import tariffs imposed by the HICs were abolished, the demand for agricultural products from developing countries would soar.

An interesting compromise that LMICs and LICs may consider to dampen the outrage in HICs about the use of child labor is the use of labeling to certify that child labor was not used in the production of a specific good for export.

The "Rugmark" label allows consumers in the importing country to discriminate in their purchases of goods from developing countries, in fact boycotting at their discretion those products without the "Rugmark" label and supporting those with the label. This policy decision by a LIC might be an alternative that HICs may accept in place of a wage increase.

REACTING TO THE HICS PROPOSAL

This section presents the HIC proposal and the initial reaction of the UMICs, LMICs, and LICs to the proposal. Hence all countries are aware of the initial reactions/positions taken by the members. Discussion and debate now opens to arrive at a consensus (75% majority) on the final elements to be included in the Code of Conduct.

HIC Proposal

1. ***Specific Terms***
    - Complete abolishment of the use of child labor, defined as below age 15
    - Establishment of a legally mandated minimum wage appropriate to living conditions in each country
    - The work week should not exceed 55 hours, and no single work day should exceed 14 hours
    - Mandatory two weeks paid vacation per year
    - Provision of minimal health benefits for the worker and his/her family, either payable by the firm or payable by the government, to include maternity coverage and infant care
    - Workers should have the right to join unions

2. ***Time Period for Compliance***
    - Within one year from the time of ratification

3. ***Non-Compliance Penalties***
    - WTO member countries that are importing goods from countries that are found in violation of items #1 and #2 above are encouraged to impose tariffs, quotas, or other restrictive measures as needed to reduce or terminate all imports from the offending countries
    - The normal appeals procedure is available to aggrieved countries

The reaction of country groups to the HICs proposal

1. ***Upper Middle Income Countries***
    - Complete abolishment of the use of child labor, defined as below age 14
    - Establish a legally mandated minimum wage consistent with minimal food, housing, and health requirements
    - Maximum limit for work week is 66 hours; maximum work limit for any single day is 15 hours; mandatory one day a week off work
    - Minimum health benefits only for the worker, not the family
    - Two years allowed for compliance
    - Non-compliance should first include a six month warning period to reach compliance; if this deadline is not met, full compliance penalties are imposed

2. ***Lower Middle Income Countries***
    - Children 11 years old and above may be used in the work place
    - Use of "labeling" ("Rugmark") encouraged by governments but not mandatory; revenue from "labeling" to be used for child education programs
    - No minimum wage requirement
    - Limit on work week to 72 hours
    - Compliance allowance of 2 years
    - If compliance is accomplished within the agreed upon period, the importing country will agree to provide government subsidized loans for child education programs; the amount of the subsidy will be prorated according to the per capita income of the importing country. No country in the LMIC or LIC

category will be required to provide subsidized loans

3. ***Low Income Countries***
   - Child labor use at the discretion of individual producers
   - "Labeling" ("Rugmark") at the discretion of individual firms; revenue from "labeling" to be used for child education programs
   - No minimum wage standard
   - No limits on hours of work per week; no mandatory paid vacations
   - Compliance period of 2 years
   - If compliance is accomplished within the agreed upon period, the importing country will agree to provide government subsidized loans for child education programs; the amount of the subsidy will be prorated according to the per capita income of the importing country. No country in the LMIC or LIC category will be required to provide subsidized loans.

DISCUSSION QUESTIONS

1. Why do the developing countries view these labor standards as a form of High Income Country (HIC) Protectionist Policy?
2. Specifically, how would the imposition of a minimum wage in developing countries affect their wages and employment?
3. How would the adoption of uniform labor standards affect foreign investment by HIC's in developing countries?
4. How would consumers and producers in developing countries and HIC's be affected by the proposed international labor standards?
5. When judging whether to support these international labor standards, what criteria or criterion should policy makers use?
6. What are the macroeconomic effects on developing countries and HIC's of adopting universal labor standards? Refer to the aggregate demand/aggregate supply analysis to illustrate your answer.
7. Make the argument that "free trade" (an absence of labor agreements) is the best solution for the High Income Countries.

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