RESEARCH SEMINAR IN INTERNATIONAL ECONOMICS

School of Public Policy
University of Michigan
Ann Arbor, Michigan 48109-1220

Discussion Paper No. 387

Issues of Trade and International Labor Standards in the WTO System

Robert M. Stern
University of Michigan

September 11, 1996

Recent RSIE Discussion Papers are available on the World Wide Web
at: http://www.spp.umich.edu/rsie/workingpapers/wp.html

ISSUES OF TRADE AND INTERNATIONAL LABOR STANDARDS IN THE WTO SYSTEM

Robert M. Stern
University of Michigan

Presented At
Seventh U.S.-Korean Academic Symposium

The Emerging WTO System and Perspectives from East Asia

University of Michigan
Ann Arbor, MI

August 28-30, 1996

Revised
September 11, 1996

Address Correspondence To:

Robert M. Stern
School of Public Policy
University of Michigan
Ann Arbor, MI 48109-1220

Tel. 313-764-2373
FAX 313-763-9181
E-mail rmstern@umich.edu

ISSUES OF TRADE AND INTERNATIONAL LABOR STANDARDS IN THE WTO SYSTEM*

Robert M. Stern
University of Michigan

> "Essentially, international action can be justified where the core labor standards that define a civilized economy are violated, or where low labor standards persist despite economic growth, and where the weakness or absence of democratic institutions gives grounds for belief that living conditions are suppressed by policy, not poverty." Reich (1994, p. 5)

> "One is then to conclude that the idea of the Social Clause in the WTO is rooted generally in an ill-considered rejection of the general legitimacy of diversity of labour standards and practices across countries. The alleged claim for the universality of labour standards is...generally unpersuasive. The developing countries cannot then be blamed for worrying that the recent escalation of support for such a Clause in the WTO in major OECD countries derives instead from the desire of labour unions to protect their jobs by protecting the industries that face competition from the poor countries. ...'blue protectionism' is breaking out, masking behind a moral face." Bhagwati (1995, p. 756)

I. Introduction

The interaction of labor standards and international trade policy is by no means a new issue. Nonetheless it has assumed new importance due to the increasingly vocal arguments by labor interests and social activists in the United States and elsewhere that issues of "unfair" labor practices and conditions have been ignored in multilateral trade negotiations and therefore should be placed high on the agenda of the World Trade Organization (WTO). Issues of lax enforcement of labor standards in Mexico were also at the center of the public debate in the United States especially in 1992-93 when the North American Free Trade Agreement (NAFTA) was being negotiated and later submitted for approval by the U.S. Congress. The concern of labor and social activist interests is that the increased imports from countries in which labor

* This is a revised version of a paper presented at the Seventh U.S.-Korea Academic Symposium, "The Emerging WTO System and Perspectives from East Asia," which was held at the University of Michigan on August 28-30, 1996. I wish to thank Ted Bergstrom, Alan Deardorff, Gary Fields, Alan Krueger, Linda Lim, T. N. Srinivasan, Betsy White, and the Symposium participants for their many helpful comments on earlier drafts of the paper. I wish also to thank Judith Jackson for typing and editorial assistance. The research underlying the paper was supported in part by the Korea Economic Institute of America.

standards are ostensibly not enforced at a sufficiently high level will be detrimental to wages and working conditions in the United States and other industrialized countries. The above quotations from U.S. Secretary of Labor Robert Reich (1994) and Columbia University Professor Jagdish Bhagwati (1995) clearly suggest a wide disparity of views on issues of international labor standards. The purpose of this paper is to explore these different views and the available options for addressing the issues involved.

The paper is structured as follows. Section II deals with the definition and scope of labor standards. Theoretical aspects of the economic effects of labor standards are considered in Section III, while Section IV summarizes the available empirical evidence. The monitoring and enforcement of labor standards are discussed in Section V. Conclusions and implications for policy are presented in Section VI.

II. Definition and Scope of Labor Standards

Labor standards are multi-faceted and may vary from country to country depending on the stage of development, per capita income, and political, social, and cultural conditions and institutions. It may be difficult therefore to distinguish unambiguously those labor standards that everyone would consider to be universal human rights from other labor standards that will depend on given national circumstances. Nonetheless, efforts have been made to identify and achieve consensus on a group of so-called core labor standards which ideally should apply universally. For example, according to OECD (1996, p. 4), core labor standards include: prohibition of forced labor; freedom of association; the right to organize and bargain collectively; elimination of child labor exploitation; and nondiscrimination in employment. Agreement on the universality of these core labor standards derives from the widespread acceptance and ratification of United Nations Covenants and Conventions as well as acceptance (though not necessarily ratification) of the pertinent Conventions of the International Labour Organization (ILO) that deal with human rights and labor

standards.[1] Besides the aforementioned core standards, there are other labor standards that relate to "acceptable conditions of work," which include: a minimum wage; limitations on hours of work; and occupational safety and health in the workplace[2].

To illustrate some of the difficulties that may arise in interpreting and implementing core standards and distinguishing between core and other standards, it is interesting to note what Fields (1995, p. 13) has proposed as "...a set of *basic labour rights for workers throughout the world*:

> i) No person has the right to enslave another or to cause another to enter into indentured servitude, and every person has the right to freedom from such conditions.
>
> ii) No person has the right to expose another to unsafe or unhealthy working conditions without the fullest possible information.
>
> iii) Children have the right not to work long hours whenever their families' financial circumstances allow.
>
> iv) Every person has the right to freedom of association in the workplace and the right to organise and bargain collectively with employers."

To illustrate further, Aggarwal (1995, pp. 4-5) has proposed that a distinction be drawn between standards related to *labor processes* and standards related to *labor outcomes*. This distinction would apply some definition of what constitutes a "minimum" standard to the determination of basic worker rights in terms of labor processes. Presumably, the point of taking labor processes, rather than outcomes, into account is to make allowance for differences and changes over time in the level of economic development and related factors. What remains unclear, however, as Aggarwal acknowledges, is the difficulty of deciding whether the identification and guarantee of labor processes provide an effective pre-condition for attaining the minimum criteria associated with achieving labor outcomes.

---

[1] According to ILO (1995), there are seven fundamental ILO Conventions that form the basis of consensus among the ILO's constituents. These include: prohibition of forced labour (No. 29); freedom of association and protection of the right to organize (No. 87); right to organize and collective bargaining (No. 98); equal remuneration for men and women for work of equal value (No. 100); abolition of forced labour (No. 105); nondiscrimination in employment and occupation (No. 111); and minimum age of employment of children (No. 138).

[2] See Brown, Deardorff, and Stern (1996, Appendix Table 1) for the definitions and principles of the core and other labor standards that are articulated in U.S. trade law, based on Lyle (1991, pp. 20-31).

While, as already mentioned, there is concern in several industrialized countries that many of their developing country trading partners appear to be violating certain basic worker rights, it has been pointed out, for example, by Bhagwati (1995, pp. 754-55) that the United States is hardly a paragon of virtue when it comes to the realization of core labor standards. He cites in particular the relative rarity in the United States of worker participation in decision making, ill treatment of migrant agricultural workers, existence of sweatshops especially in the clothing industry that pay substandard wages and maintain oppressive working conditions, the relatively low rate of unionization in the private sector, limitations on the right to strike in some sectors, and the fact that American children are often employed in a variety of different jobs in the work place and at home. He argues accordingly that it is "morally obtuse" for the United States to seek to impose on poor countries particular requirements relating to worker rights.[3]

The foregoing discussion is by no means intended to deny the desirability of improving working conditions through higher labor standards. The issue, rather, is how this can best be accomplished. My own view is that the discussion and determination of what constitutes core labor rights should be carried out in the context of an organization such as the ILO and not through the WTO. The ILO has a long history of trying to define and monitor labor standards and practices and to achieve its goals by providing information and technical assistance and utilizing moral suasion to induce countries to change policies that the international community of nations considers to be violations of basic worker rights. I shall have more to say on this below in discussing existing institutions and mechanisms for the monitoring and enforcement of labor standards. It may be useful first though to discuss the central theoretical issues and the available empirical evidence involved in analyzing the economic effects of labor standards.

---

[3] A similar argument is made by Srinivasan (1994, 1995, 1996), who further argues that, if developed countries with high labor standards are serious in doing something about working conditions in developing countries, the developed countries could lift immigration restrictions and/or provide income transfers to workers and to families in developing countries. His point is that humanitarian concerns need to be reflected in the willingness of citizens in developed countries to assume responsibility and pay financially to enhance the welfare of workers, including children, in developing countries.

III. Economic Effects of Labor Standards: Theoretical Considerations

In this section, we consider two main issues: (1) the diversity of labor standards and the case for free trade; and (2) the effects of standards and the international harmonization of standards on economic welfare and the terms of trade of individual nations.

Diversity of Standards and the Case for Free Trade

As noted in the preceding discussion, labor standards may vary across nations depending on their level of development, per capita incomes, and a host of political, social, and cultural conditions and institutions. The issue is whether such diversity of standards alters the case for free trade. This has been investigated in depth by Srinivasan (1995), based on a theoretical model in which standards use productive resources and also affect consumer welfare. The upshot of Srinivasan's theoretical analysis is that the diversity of labor standards between nations may reflect differences in factor endowments and levels of income, and that such diversity is consistent with the case for free trade. When trade is not balanced and if minimum international labor standards are to be attained, it will be necessary to have arrangements for international income transfers and domestic tax/subsidies. This will be the case as well when consumers in countries with high standards have a moral preference to raise standards in their trading-partner countries. Further, if there are market failures that prevent the attainment of minimum labor standards, income transfers and domestic tax/subsidies will be required to achieve optimal conditions for resource allocation and consumer welfare.[4] Finally, the use of trade intervention may hinder rather than improve the attainment of higher labor standards, and it may be in the collective interests of countries to cooperate in setting labor standards. I shall have occasion below to examine the implications of Srinivasan's conclusions in considering the different options for dealing with international differences in labor standards.

---

[4] Srinivasan points out that the case for promoting labor unions and collective bargaining, which is considered to be a core labor standard, is by no means obvious in many developing countries, especially where unions are concentrated in the organized manufacturing and public sectors rather than in agriculture where a relatively large proportion of the population may be employed.

International Harmonization of Standards

Brown, Deardorff, and Stern (BDS, 1996) analyze the effects of standards on economic welfare and the terms of trade and do not concern themselves directly with issues of the diversity of standards and the case for free trade. They employ a variety of theoretical models in which different national characteristics may determine the outcome of the introduction of labor standards.[5]

A general conclusion emerging from the BDS analysis is that economic welfare is best served when countries act to correct their domestic (labor) market failures. But, since these market failures will likely differ between countries, they conclude that there is no obvious case on welfare grounds for pursuing universal standards and the international harmonization of standards that this may imply. This conclusion is consistent with that of Srinivasan, namely that diversity of working conditions between nations is the norm and is by no means in itself "unfair" so long as the extant labor standards are consistent with efficient resource use.[6] Further, despite the good intentions of government, it may well turn out that the imposition of labor standards may fail to correct a market failure if the preferences of workers are heterogeneous with respect to what they consider to be acceptable levels of, say, health and safety conditions in the workplace.[7]

In considering the economic consequences that may result from pursuing the international harmonization of labor standards, BDS conclude that in cases in which low-income countries are relatively labor abundant, harmonization will reduce the labor endowment of these countries and thereby the supply of labor-intensive production on the world market. This could improve (worsen) the terms of trade of the low (high) income countries, although this is not what the high-income countries may intend.

---

[5] See Bloom and Noor (1994) for research along related lines. Casella (1996) develops a model in which labor standards respond endogenously to changing levels of income.

[6] An exception arises here in cases of slave labor and what may be considered to be egregious treatment of child labor.

[7] See Maskus, Rutherford, and Selby (1996) for a computable general equilibrium (CGE) model analyzing the effects of changes in Mexico's labor standards. They demonstrate conditions in which improved labor standards may enhance the welfare of Mexican workers.

BDS further assess arguments for having standards imposed on low-income countries. They note that low-income countries might benefit in case a government is unable for domestic political reasons to enact legislation on its own, although this presumes that the policy in question will indeed correct a market failure. Another possibility is that requiring the guarantee of such standards as the right to organize may serve to reinforce development of democratic institutions. Finally, they ask if there is any justification for high-income countries to take countervailing actions against the ostensibly unfair labor standards of their trading partners. They answer in the negative so long as efficient resource use is present. If, nonetheless, a high-income country imposes a tariff or quota on labor-intensive imports from a low-income country, this will obviously be harmful to the economic interests of workers in the low-income country. In general then, the case for international harmonization of labor standards appears rather weak, and it is quite possible that harmonization could have unintended adverse consequences for the very people they are intended to protect. Based on the BDS analysis, it is difficult therefore to generate much theoretical support for pursuit of core labor standards that would have universal application.

Labor Standards as Private/Public Goods

We have already indicated that there may be a strong moral basis motivating the pursuit of higher labor standards. Thus, in his analysis noted above, Srinivasan made allowance for moral considerations in consumer utility functions so that consumers could express their concern by a willingness to pay relatively higher prices for goods and services that reflected higher labor standards. In this connection, there is an issue of whether labor standards are to be considered as *public* or *private* goods. As long as the same standards appear in the utility functions of more than one individual, the standards are public goods. Suppose, on the other hand, that individual consumers have a sense of virtuousness and derive pleasure from believing that the good being considered embodies some acceptably high level of labor standards. In this case, individual consumers care only about their own satisfaction and not about others, so that labor standards can be treated as private goods.

This view of higher standards as private goods has been expressed most forcefully by Freeman (1994a), who argues that a market solution based on labeling may be an especially effective way to raise labor standards internationally. Labeling has the advantage that consumers pay more for what they consider morally acceptable, and at the same time foreign suppliers are compensated for their increased costs. Labeling also undercuts protectionist influences.

It is not altogether clear, however, that labor standards should be considered to be private goods which lend themselves to a market-based treatment dependent on supplying all relevant information to consumers. If instead, labor standards take the form of public goods, Freeman (p. 30) acknowledges that some type of government intervention may be called for. In their theoretical analyses, Srinivasan and Brown, Deardorff, and Stern considered cases of domestic market failure in which a governmentally imposed tax/subsidy arrangement would be introduced to correct the distortion and permit the first-best optimum to be attained. While tax/subsidy (price-based) arrangements have a clear theoretical appeal, it is important to recognize in dealing with issues of labor standards that governments often prefer to use nonprice measures, i.e., legal regulation and enforcement. Freeman (p. 29) cites a number of regulatory examples in U.S. law, including prohibition of slavery, restrictions on child labor, occupational health and safety standards, and discrimination in the workplace. As he argues, the choice of different policy measures will depend on given empirical and institutional circumstances, and it is likely that some combination of price-based and regulatory approaches will produce the best results[8].

Freeman goes on further to argue that what were referred to above as process-related labor standards involving prohibition of forced labor, freedom of association, and collective bargaining may be

[8] It should be noted that this discussion refers to national or federal standards. In his Symposium comment, John Jackson noted that there may be significant differences between U.S. states and regions in the impacts that national standards may have and yet the national standards remain operative. What helps this to work is that there is free movement of labor within the United States coupled with various programs of income support and transfers. As noted in my theoretical discussion above, one or both of these elements would be needed for an international system of labor standards to function effectively.

best dealt with by regulatory measures while outcome-related standards involving wages and working conditions may be more amenable to market-based informational and labeling approaches. While Freeman's analysis and perspective are in many ways compelling, his case for consumer labeling may be limited insofar as it rests on treating labor standards as private goods. He does not make clear, moreover, what role the government should play, if any, in providing information to consumers and facilitating labeling and preventing private labeling arrangements from being co-opted by producing interests. In any event, what actually should be done regarding international labor standards from the standpoints of the high- and low-income countries with differing standards still remains to be determined. There is a need in particular to take international political economy considerations into account.

Political Economy Aspects of International Labor Standards

In discussing the sources of support for governmental action on labor standards, it is important to identify the constituent interest groups involved. Thus, it would appear that in the United States organized labor, import-competing firms, and human-rights public-interest groups are the main proponents of stricter labor standards applied to low-income countries. These interest groups may often recommend policies, including sanctions and import restrictions, which are intended ostensibly to change the behavior of trading-partner governments. By the same token, interest groups are influential in many low-income countries, especially among unionized workers in manufacturing sectors, employees of state enterprise, and owners/managers of import-competing firms. These groups may seek to protect and enhance their own ends and to resist foreign intrusion in setting standards. Krueger (1996, p.4) refers to the protectionist motivation as the "prevailing *political economy* view of international labor standards."[9,10] The issue then is how governments choose to respond to the various interest groups.

---

[9] While Krueger's characterization may apply to unions and import-competing firms, it may not apply to the activities of human-rights public-interest groups which are not motivated by protectionist considerations.

Krueger also discusses other aspects of labor standards, including: (1) pursuit of policies to change the distribution of income (e.g., a minimum wage); (2) correction of market failures; (3) preventing a race to the bottom; (4) moral preferences; and (5) enhancement of labor market institutions. While some of these aspects are subsumed in the political economy view of labor standards and have already been touched on, it is useful nonetheless to discuss each of them briefly.

(1) There is of course a longstanding controversy regarding the extent to which distributional policies like a minimum wage reduce the employment or raise the income of low skilled workers. But in many developing countries in which wages are already relatively low, there is a theoretical presumption that pressuring them to institute a minimum wage could be detrimental to their economic welfare, not to mention that there could be considerable noncompliance as well.

(2) Policies to correct market failures were mentioned above, and the general conclusion was that governments should attempt to target their domestic policies to correct market failures and thereby attain optimal resource allocation and maximization of consumer welfare.

(3) Concerning a race to the bottom, Srinivasan (1995) has shown that this need not occur particularly if countries behave cooperatively. Moreover, there is nothing to prevent countries from implementing higher labor standards when these are judged to be in their own society's best interests.

(4) Moral preferences can be accommodated in consumer utility functions. The issue is whether they should be treated as a public or private good. If preferences take the form of a public good, some type of government action may be called for. This raises issues of how best to satisfy such preferences, that is, through governmental tax/subsidy or regulatory measures. If preferences can be considered to be a private good, a market-based approach using consumer labeling may be desirable.

---

[10] See Noor (1996) for development of a theoretical model in which labor standards may enhance protection in an industrialized country. Also, see T. N. Srinivasan's comments below.

(5) Perspectives differ noticeably with regard to the enhancement of labor institutions. On the one hand, as noted above, labor unions in low-income countries may be concentrated in the manufacturing sectors, and there may also be substantial numbers of workers employed in public enterprises. As a consequence, the fostering of unions could be harmful to workers and families in the informal and in the rural/agricultural sectors. On the other hand, it can be argued that encouragement of unions and collective bargaining may enhance the efficiency of labor markets and increase the productivity of workers, especially when there are monopsonistic employers. There may also be significant and beneficial political and social spillover effects as democratic institutions are strengthened and social harmony is reinforced. While it is not an easy matter to incorporate all these potentially beneficial elements into economic models, they could nonetheless turn out to be of great importance in the course of time.

In this section, we have reviewed a number of the salient theoretical and political economy aspects of international labor standards. Since many of the conclusions reached apparently depend on the economic structure and related characteristics of different nations, it is useful to consider next the existing empirical evidence on the economic effects of labor standards.

IV. Economic Effects of Labor Standards: Empirical Evidence

Labor Standards and Trade

In our earlier discussion, we distinguished "core" and "other" labor standards. Core standards typically include: prohibition of forced labor; freedom of association; the right to organize and bargain collectively; elimination of child labor exploitation; and nondiscrimination in employment. Other labor standards relate primarily to conditions of work and include: a minimum wage; limitations on hours of work; and occupational safety and health in the workplace. The question then is the extent to which international differences in the various standards affect trade performance.

Rodrik (1996) represents an especially noteworthy effort to determine whether labor standards matter for trade. He constructed measures of labor standards, including: (1) total number of ILO Conventions ratified by a country; (2) a more focused measure of ratifications of ILO Conventions relating to "basic worker rights"; (3) a measure of democracy encompassing indicators of civil liberties and political rights; (4) an indicator of problems of legislation or enforcement of standards affecting child labor; (5) statutory hours of work; (6) days of annual leave with pay in manufacturing; and (7) the percent of the labor force that is unionized. His data were from a variety of sources based on information in the 1980s and 1990s.

Using multiple regression analysis, Rodrik first investigated whether labor standards affect labor costs. Making allowance for the effects of worker productivity, based on a sample of 35-36 countries, he found that per capita income was strongly correlated with labor costs. He also found positive and significant coefficients for the measures of the ratification of the ILO Conventions and the indicator of democracy and a negative coefficient for child labor practices. His conclusion then was that labor costs tend to rise as standards are applied more stringently across countries.

Turning next to the effects on trade, Rodrik focused on labor-intensive goods, using as a dependent variable the ratio of textile and clothing exports to other exports, excluding fuels. He included proxy measures for a country's labor/land ratio and for human capital to reflect the basic determinants of comparative advantage.[11] Taking high- and low-income countries together, he found that only the comparative advantage variables were statistically significant. None of the labor standard indicators were statistically significant. He also ran a regression omitting the high-income countries, concluding that the statistical fit was improved but that there was at best only limited support for the impact of labor standards on trade for low-income countries.

[11] Rodrik did not include a separate measure of physical capital in his analysis.

Another study of interest is Aggarwal (1995), who investigated in detail the relationships of labor standards and the pattern of U.S. imports from ten major developing countries in 1994. The countries included were: Singapore; Hong Kong; Mexico; South Korea; Malaysia; Thailand; the Philippines; China; Indonesia; and India. These ten countries accounted for 26.5 percent of U.S. imports in 1994. Aggarwal's major findings (p. 7) were as follows:

> "Sectors typically identified as having egregious labor conditions do not occupy the only or even the primary share of these countries' exports.
>
> Comparisons across more export-oriented and less export-oriented sectors indicate that core labor standards are often lower in less export-oriented or non-traded sectors such as agriculture and services.
>
> Similarly, within an export-oriented sector, labor conditions in firms more involved in exporting are either similar to or better than those in firms that are less involved in exporting.
>
> Changes in technology and the structure of international trade are leading developing countries to compete in a race upward in terms of product quality rather than a race downward with respect to price.
>
> ...Wages and working conditions in developing countries have been exhibiting positive trends. In general, these have been in line with productivity changes."

Aggarwal also had occasion to analyze the impact of imports from the ten major developing countries on the U.S. economy. Her main conclusions (p. 24) were:

> "At the aggregate level, the impact of imports from these developing countries is small relative to imports from industrialized countries.
>
> Countries with lower labor standards do not exhibit higher rates of import penetration than countries with relatively higher labor standards.
>
> Imports from these developing countries do not appear to have larger displacement effects on U.S. employment and wages in sectors associated with poor labor standards relative to other sectors."[12]

---

[12] In addressing issues of labor standards and trade, Erickson and Mitchell (1996) focus on the pattern and labor content of U.S. trade for evidence of adverse wage effects and displacement of U.S. workers. While they find a fairly small impact from trade, they do not investigate the extent to which low labor standards are the root source involved.

Finally, we may cite some of the main conclusions from the summary of the OECD Report on Trade, Employment and Labour Standards (1996, p. 5):

> "...empirical research suggests that there is no correlation at the aggregate level between real-wage growth and the degree of observance of freedom-of-association rights;
>
> ...there is no evidence that low-standards' countries enjoy a better global export performance than high-standards' countries;
>
> ...a detailed analysis of US imports of textile products (for which competition from low-standards' countries is thought to be most intense) suggests that imports from high-standards' countries account for a large share of the US market. Moreover, on average, the price of US imports of textile products does not appear to be associated with the degree of enforcement of child labour standards in exporting countries;
>
> ...some cases have been recorded where governments appear to deny core standards to workers or do not enforce them deliberately with the aims of improving sectoral trade competitiveness or attracting investment into export-processing zones (EPZs); the expected economic gains from such a strategy are, however, likely to prove short lived and could be outweighed in the longer term by the economic costs associated with low core standards;...."[13]

While the studies cited above may not constitute the final word on the relationships between labor standards and trade, the conclusion seems inescapable that there is little compelling empirical evidence suggesting that low labor standards have an impact on trade.[14]

---

[13] The OECD Report (p. 6) further notes that "... there is a positive association over time between successfully sustained trade reforms and improvements in core standards." They also note that core labor standards could be enforced without risking negative repercussions on FDI flows. "...These results imply that concerns expressed by certain developing countries that core standards would negatively affect their economic performances or their international competitive position are unfounded; indeed, it is theoretically possible that the observance of core standards would strengthen the long-term economic performance of all countries." There is certainly much to agree with in this conclusion, and I return to it below in discussing Freeman's (1993) research.

[14] Alan Krueger has suggested to me that this is consistent with the view that the demand for international labor standards in the United States does not emanate from disguised protectionism. On this matter, see the discussion below of Krueger's research.

Labor Standards and Foreign Direct Investment (FDI)

As mentioned in earlier discussion, it is often alleged that multinational enterprises may be attracted to locate in countries with lower labor standards to take advantage of lower costs. The available empirical evidence actually indicates the opposite to be the case.

Thus, Rodrik (1996) investigated the determinants of U.S. FDI abroad during 1982-89, including measures of foreign exchange distortions, population, and income growth in host countries together with the various indicators of labor standards. He found (p. 22) that: "Countries with a lower democracy score and a higher CHILD score have received *less* foreign investment during 1982-89 than would have been predicted on the basis of other country characteristics. Taken at face value, these results indicate that low labor standards may be a hindrance, rather than an attraction, for foreign investors." Aggarwal (1995, p. 7) reached a similar conclusion: "U.S. foreign direct investment is not typically concentrated in countries or industries with poor labor standards." Finally, as reported in OECD (1996, p. 6): "...while core labour standards may not be systematically absent from the location decisions of OECD investors in favour of non-OECD destinations, aggregate FDI data suggest that core labour standards are not important determinants in the majority of cases."

Thus, the empirical evidence suggests rather convincingly that low labor standards are not reflected in the existing trade performance of the major developing countries and that FDI is more attracted to countries with high rather than low standards.

Labor Standards and the Role of Interest Groups

As mentioned above, the conventional political economy view of international labor standards is that support for standards reflects protectionist interests in the United States and other industrialized countries. In an effort to test this proposition empirically, Krueger (1996) analyzed the determinants of support in the U.S. House of Representatives for the Child Labor Deterrence Act of 1995. If approved, this Act could prohibit imports of goods produced abroad by child labor under specified circumstances,

including by children under 15 years old and subject to a review of child labor practices by the U.S. Secretary of Labor. The Act has been co-sponsored by Senator Tom Harkin (D-IA) and Congressman Barney Frank (D-MA), with 35 co-sponsors in the House and 7 in the Senate.

Krueger hypothesized that support for the legislation would be strongest in districts in which there are relatively large numbers of unskilled workers, as measured by high-school completion rates. Other independent variables included in the analysis were: the proportion of unionized workers in a given state; previous votes on NAFTA and GATT; party affiliation; the representative's "liberalness" rating by the Americans for Democratic Action (ADA); the representative's popular vote in the 1994 election; and the number of terms served. Using a linear probability model for estimation purposes, Krueger found that "...Congressmen from districts with a high concentration of high school dropouts are *less* likely to cosponsor the Child Labor Deterrence Act. ...This finding is contrary to what I would expect from a simple political economy model...." Krueger also found that higher rates of unionization were associated with support for the Child Labor Deterrence Act as were representatives who were Democrats and also had voted against NAFTA and GATT.

In interpreting his results, Krueger (p. 21) suggested that the demand for international child labor standards should be considered to be a "normal" good, following Freeman (1994a). That is, voters with higher socioeconomic attainment will select Congressmen who favor limitations on employment of child labor. He further argued that unionized workers who tend to be more highly skilled and thus may not benefit directly from a ban on imported goods made with child labor may in this case be acting to pursue policies that strengthen worker rights more generally rather than pursuing their own narrow self interest. He goes on more broadly to state (p. 22): "Indeed, in many instances I am surprised that the AFL-CIO uses its

limited political capital to press for international labor standards that are of little benefit to its members, when instead it could pursue policies that are of much greater direct benefit to its membership."[15]

While Krueger's results are suggestive, they are by no means definitive. In particular, as Srinivasan (1996) has noted, a representative may have chosen not to sponsor the legislation and yet may be supportive of it. Further, since less educated and less skilled individuals tend to vote less, their interests may not have been given sufficient weight in the representative's deciding whether or not to be a cosponsor. Finally, as already noted, Krueger's results suggest support for the legislation from representatives from districts with a higher rate of unionization and voting records opposing NAFTA and GATT.

Another noteworthy empirical study is by Freeman (1993) who investigated the evidence in developing countries for and against government intervention designed to introduce/remove labor-market distortions and, alternatively, to enhance labor-market institutions.[16] He labels these two views, respectively, the "World Bank Distortion View" and the "International Labour Organization (ILO) Institutional View." These views differ insofar as removing interventions is believed to enhance economic efficiency and welfare, whereas introducing interventions is believed to lead to these same results.

Freeman (p. 119) notes that: "The distortion case hinges on four claims about interventions: they misallocate labor, waste resources through rent-seeking, impair adjustment to economic shocks, and deter

---

[15] Krueger also has examined other aspects of child labor, including the relationship between employment of children and GDP per capita and the experiences with compulsory schooling laws. He found that employment of young children was negatively related to GDP per capita. That is, child labor is more prevalent in low-income regions and negligible in high-income regions. This is a clear demonstration of the fact that restrictions on child labor can be looked at as a normal good, in this case less of it being condoned as per capita incomes rise. Evidence on the effects of compulsory schooling laws suggested that there may be definite benefits from such laws in high-income countries, but that there is widespread noncompliance with existing laws in many low-income countries. These findings suggest that reliance on child labor in low-income countries will diminish as family incomes rise, and that realization of the benefits of compulsory schooling laws depends on increasing economic opportunities and financial support for poor families so as to reduce their dependence on employment of their children.

[16] See also Freeman (1994b) which contains empirical studies of labor-market institutions and policies in several industrialized countries and some lessons for the United States suggested by the experiences of other countries.

investment, thereby reducing economic growth." But the Institutional View rejects these claims (p. 121): "When actual labor markets operate differently from the ideal, institutional modes of influencing outcomes, such as collective bargaining, tripartite negotiations, and government-mandated wages or labor standards, can be Pareto improvements. In the institutionalist view, they usually are." To investigate the validity of these alternative views, Freeman examined evidence for selected developing countries mainly during the 1980s. He considered: (1) sectoral wage differentials; (2) nonwage labor costs; (3) minimum wages; (4) wage adjustments; (5) employment security regulations; and (6) collective bargaining.

His findings can be summarized as follows:

> (1) Public sector and urban wage premia have decreased remarkably in Africa and Latin America during the 1980s. There have been longstanding wage differentials among comparable workers in many developing countries, apparently despite differences in policy interventions and institutions.
>
> (2) Nonwage labor costs (i.e., payroll taxes, unemployment compensation, other fringes) do not appear to be distortionary.
>
> (3) Depending on their level, minimum wages could be distortionary, but these distortions have not been serious in several instances, and minimum wages have actually been lowered to prevent undue negative employment impacts in some cases.
>
> (4) Real wages apparently dropped sharply in many countries in response to macroeconomic and structural adjustments, although unemployment may have increased.
>
> (5) There is mixed evidence on the effects of job security and other employment regulations. Further, relatively large public sector employment could be, but is not necessarily, distortionary.
>
> (6) There is no consistent evidence that suppression of unions promotes economic growth, or that the relative presence or absence of unions retards or encourages growth.[17]

It would appear from Freeman's empirical findings that neither the distortion nor the institutional view of labor-market policies and institutions is clearly supported by the available data. In particular, real

[17] In her Symposium comments, Linda Lim pointed out that, in spite of the absence of formal worker rights and standards in such Southeast Asian countries as Malaysia, Singapore, and Indonesia, wages and working conditions had improved markedly. In contrast, the experiences in Thailand and the Philippines had been much less favorable even though these nations encouraged worker rights and minimum wages. She also noted that both Malaysia and Singapore had attracted considerable inflows of FDI and that workers had benefitted in the firms involved.

and relative wages in developing countries turned out to be much more flexible in response to changing market conditions than the strict distortionist view would suggest. With his findings in mind, Freeman developed a theoretical model in which labor-market interventions may influence attitudes towards reforms and ways of expressing these attitudes. The thrust of this model was that it is important to identify the winners and losers involved in making changes in labor-market policies, how their positions and composition may change over time, and what kinds of side payments may be necessary to generate continued support for the policy changes. Freeman's overall conclusion was that the costs and benefits of labor-market policies will depend on individual country circumstances.

This selective review of labor standards and the role of interest groups leaves the present author at least with a rather agnostic view of the issues. Our theoretical discussion suggested that it was difficult conceptually to make a case for pursuing universally mandated labor standards. Further, the conclusions of the empirical evidence were that international differences in labor standards do not have any significant impact on existing patterns of trade and that flows of FDI respond to high rather than low standards. Moreover, despite the prominence of the view that insufficient labor standards may reflect policy distortions and protectionist pressures, the available empirical evidence in support of this view is mixed. Finally, there may be grounds for interventions involving labor standards that enhance the efficiency and equity of labor-market institutions in given circumstances and in ways that are not adequately reflected in the distortions framework.

Because labor standards are obviously important in the current policy environment, it is essential to consider the alternative arrangements that exist for their monitoring and enforcement. This will be done in the following section. We will conclude with some recommendations that may serve the interests and needs of both high- and low-income countries.

V. Monitoring and Enforcement of Labor Standards

Labor standards are presently dealt with in a variety of settings: global; regional; national/unilateral; and other, including private, arrangements. We shall discuss briefly each of these in turn.

Global Arrangements

The main international organization that is concerned with labor standards is the ILO, which was established as part of the Treaty of Versailles of 1919 following the end of World War I. The methods and principles set out in the ILO constitution deal with all conceivable aspects of labor standards. As stated in ILO (l988, p. 4), ILO action designed to promote and safeguard human rights takes three main forms: (1) definition of rights, especially through adoption of ILO Conventions and Recommendations; (2) measures to secure the realization of rights, especially by means of international monitoring and supervision but not by imposition of trade sanctions; and (3) assistance in implementing measures, particularly through technical cooperation and advisory services. Since World War II, the role and influence of the ILO regarding labor standards have been central to the declarations and efforts of the United Nations and associated regional organizations designed to protect and promote human rights. Rodrik (1996, p. 15) notes that 174 ILO Conventions have been approved since 1919, although some of them have been revised by other Conventions subsequently.

We have already mentioned what might be considered to be ILO core labor standards. According to OECD (1996, p. 4), these include: Conventions 87 and 98 relating to freedom of association, the right to organize, and collective bargaining; Conventions 29 and 105 prohibiting all forms of forced labor; Convention 111 dealing with non-discrimination in employment; and Convention 138 providing for a minimum age for employment of children. It is interesting that formal ratification of ILO Conventions differs considerably among ILO members, apparently because particular Conventions may be at variance with national laws and institutional practices. Thus, for example, as Rodrik (1996, p. 15-16) notes, the

United States has ratified only 11 ILO Conventions in all whereas several other industrialized and developing countries have ratified a significantly larger number of Conventions. Ratification of ILO Conventions may therefore not be an accurate indicator of existing national regulations governing labor standards, and there are many cases in which ratified Conventions are in fact not enforced.

In looking over the spectrum of international organizations that have been created over the years, Srinivasan (1995, pp. 3-4) points out that these organizations have been specialized according to function. For example, he notes the particular rules and mandates that apply to such organizations as the: ILO; GATT/WTO; UNCTAD; World Bank; International Monetary Fund; Universal Postal Union; and Berne and Paris conventions. The issue that he raises then is whether it is desirable and efficient to require that individual organizations assume responsibilities for rules for which the organizations were not designed. More specifically, he argues that issues of labor standards are best left to the ILO and should not be mandated to the GATT/WTO, which has been designed to articulate, monitor, and enforce the rules governing the international trading system.[18]

It is interesting in this connection, as Charnovitz (1987, pp. 566-67) has noted, that issues of alleged unfair competition involving labor standards were addressed in Article 7 of Chapter II of the 1948 (still-born) (Havana) Charter of the International Trade Organization (ITO). Since the GATT was conceived with a more narrow mandate as compared to the ITO, it did not address labor standards, except in Article XX(e) that provides for prohibition of goods made with prison labor. Charnovitz (p. 574) notes further that as early as 1953 the United States proposed (unsuccessfully) adding a labor standards article to the GATT. This would have empowered GATT members to take measures against other countries under the provisions of GATT Article XXIII (Nullification and Impairment). The United States continued, again unsuccessfully,

[18] Similar views are expressed in Bhagwati (1995), Charnovitz (1995), and Pangestu (1996). Some Symposium participants took issue with this characterization of the GATT/WTO, arguing that it constitutes a forum for discussion and negotiation on trade-related matters, and, in this light, should include issues of

to push for negotiation of a GATT article on labor standards in both the Tokyo and Uruguay Rounds of Multilateral Trade Negotiations in the 1970s and 1980s. But the international community was put on notice in April 1994 at the Marrakesh signing of the Uruguay Round accords that the United States intended to pursue issues of labor standards in future multilateral negotiations.

In the interim, there have been efforts at drafting a so-called social clause dealing with core labor standards and including trade sanctions for noncompliance that might eventually be incorporated into the WTO. As noted in Aggarwal (1995, p. 38), in June 1994, the ILO began a research program dealing with the integration of social welfare and trade policy. A central objective was to develop a stronger enforcement mechanism. The ILO Working Party on the Social Dimensions of the Liberalization of International Trade proposed that the ILO and WTO work jointly on the oversight of international core labor standards, with the ILO concentrating on international monitoring and the WTO responsible for enforcement by means of trade-related sanctions. But because of disagreements among the ILO Working Party country representatives, it was decided in early 1995 to suspend further discussion of the use of trade sanctions for alleged noncompliance with core labor standards. Instead, as noted in OECD (1996, pp. 7-8), the ILO has undertaken a program of research on the effects of trade liberalization on core standards and a review of ILO means of action for the promotion of standards.

The United States, with some support from France and southern European Union members, Canada, and Japan, have nonetheless continued to pursue the issue of trade and labor standards in the context of the WTO. There is an ongoing effort to add the issue to the agenda for the WTO ministerial meeting that will be held in Singapore in December 1996. Thus, in this connection, de Jonquieres and Williams report in an article in *The Financial Times* (June 20, 1996, p. 8) that:

---

labor standards. Some concern was nevertheless expressed about overloading the WTO with labor standards and other new issues like the environment and competition policy.

> "The US has not in, in fact, sought to make its case on economic grounds. It also insists it is not seeking an excuse to erect trade barriers or discriminate against low-wage competitors, and does not want labour standards upheld through trade sanctions.
>
> Washington's argument, echoed by Sir Leon Brittan, EU trade commissioner is that popular feeling on the issue is so strong that unless the WTO at least acknowledges it, public support for trade liberalisation risks being undermined.
>
> 'We need to be able to give a political signal to our domestic workforce that, while they may face competition from workers in lower-wage countries, they will not face competition on the basis of denied worker rights,' a recent US position paper says.
>
> The US wants WTO ministers to issue a 'political declaration' in Singapore linking the maintenance of an open world trade system to promotion of 'core' labour standards, such as freedom of association, prohibition of forced labour and elimination of exploitative child labour.
>
> It also wants the ministers to create a working party to identify and report back to them on links between labour standards and WTO rules.
>
> But recent US efforts to clarify its aims appear to have won few converts. South-east Asian trade ministers are committed to opposing any discussion of trade and labour standards in the WTO, as is India."

The U.S. position could be interpreted in part as pre-election posturing by the Democrats, as de Jonquieres and Williams note, especially since the Republicans have opposed linking labor standards and trade. The Republican controlled Congress has been reluctant to grant "fast-track" negotiating authority to the Clinton Administration so long as the intention is to include labor issues as part of any future trade negotiations. Depending on the outcome of the U.S. election, it is therefore possible that the U.S. position on trade and labor standards may be muted. However, given U.S. political realities and concerns about issues of wage stagnation and inequality, it seems unlikely that the link between trade and labor standards will disappear altogether from public discourse.

The question therefore remains whether or not the WTO is an appropriate forum for dealing with trade and alleged violations of core labor standards. It is pertinent in this connection to note the conclusion reached in the OECD Report on Trade, Employment and Labour Standards (1996, p. 8):

> "Existing WTO provisions have not been designed for promoting core standards. Some of the suggestions under discussion would imply a reinterpretation of WTO practices and procedures while others would require to a greater or lesser extent renegotiation and amendment of WTO articles. Extending the WTO's Trade Policy Review Mechanism

> procedure to include labour standards would fall into the former category while other proposals would fall into the latter. In all cases, a consensus among WTO Members on the appropriateness and effectiveness of using WTO procedures to promote core labor standards and on the institutional changes required would have to be reached. Such a consensus does not exist at present. However, while some countries continue to call for discussion of the issue in the WTO and others are opposed, this remains an issue for international consideration. The debate on this issue and on the associated conceptual and practical difficulties will continue."[19,20]

I shall return to the question of the appropriate international forum for addressing issues of international labor standards in the concluding section below.

---

[19] Rodrik (1996) makes a case for using the Uruguay Round safeguard procedures for investigating complaints arising from imports from countries with unacceptable labor standards that may be disruptive to domestic producing interests. He stresses the need for including the views of consumers and public interest groups in the importing countries as well as the views of foreign producers. Srinivasan (1996) has pointed out an important problem with Rodrik's argument, namely that there are all kinds of government regulations, besides labor standards, that influence production costs (e.g., building codes and zoning laws). Thus, in principle, objections might arise concerning imports that may not conform to any one or a host of domestic regulations. Singling out labor standards is then not convincing. It is not obvious, moveover, that the safeguards procedures, which are designed to be temporary, can be implemented with the broad representation that Rodrik recommends. Finally, as Anderson (1996) has observed, the U.S. experiences with antidumping and countervailing procedures certainly suggest how difficult it may be to avoid the temporary safeguard procedures from being captured by producing interests.

[20] It is also worth noting that Freeman (1994a, p. 32) is somewhat inclined to support the inclusion of labor standards in trade agreements: "Unlike trade economists who view any interference with free trade as the work of the devil, I would be pragmatic in this area. ...If trade negotiations are the only way to raise forcefully the standards flag in an international setting, why not? If trade sanctions can improve labor standards, that benefit must be weighed against the cost of lost trade. If trade sanctions can overturn an evil dictatorial regime and save human lives, go for it. Perhaps the standards issue will induce international trading groups to consider innovative ways that international trade might be used to finance improvements in standards." Krueger (1996, p. 13) has expressed a similar view: "Labor standards strike me as a legitimate subject of bargaining in trade negotiations. Presumably, a well-intentioned government will not accept an agreement unless, in total, it is expected to make the country better off. ...Since the demand for labor standards tends to rise with national income, many countries will endogenously desire to strengthen and enforce their standards following trade agreements." While the views expressed by Freeman and Krueger may be justified on pragmatic and political grounds, there is still a question of whether and how labor standards should be dealt with in the WTO multilateral context. The welfare gains from trade liberalization have long been a central feature of nondiscrimination in the GATT system. It would be a major departure from precedent if countries with allegedly low labor standards were now to be denied improved market access on these grounds.

Regional Arrangements

European Union

Issues of worker rights have been a focus of attention in the European Union (EU) because of concerns over low-wage competition from some EU member countries, persistent unemployment, and wage stagnation. Sapir (1995b) notes that the first efforts to address the harmonization of social policies in Europe can be traced back to early stages of European integration prior to 1958. According to De Boer and Winham (1993, p. 17), the issue of a Community-wide Social Charter was first broached in 1972. Subsequently, with the issuance in 1985 of the white paper signalling the intention to remove remaining barriers to trade and creation of a Single Market, a Community Charter of Fundamental Social Rights for Workers was drafted in 1988. This Charter, which is quite comprehensive and encompasses the "core" and "other" labor standards noted in our earlier discussion, was adopted by all EU members except the United Kingdom. It was hoped to incorporate the Social Charter into the Maastricht Treaty in December 1991, but this was opposed once again by Britain. The Social Charter was subsequently approved by the other 11 EU members, but on a voluntary basis and not as part of the Maastricht Treaty.[21]

In his evaluation of the EU Social Charter, Sapir (1995a, pp. 742-743) concluded that harmonization of social policies was not a pre-condition of successful European trade liberalization and integration. He noted further that:

> "In the mid-1990s, differences in labour standards between member states remain substantial and 'social harmonisation' remains a distant reality. ...whatever harmonisation has been achieved in Europe, it could not have occurred without redistributive mechanisms between countries. In the absence of such mechanisms, the harmonisation of social policies cannot be contemplated internationally."

[21] The highlights of the Charter of Fundamental Social Rights are summarized in De Boer and Winham (1993, pp. 36-37), and the full text is to be found in Commission of the European Communities (1990).

NAFTA

At the time that NAFTA was being negotiated, some observers urged that NAFTA include a Social Charter for North America as a possible means of protecting the interests of workers.[22] Instead of including a Social Charter, however, and since the NAFTA had already been signed by the member countries in the summer of 1992, the newly elected Clinton Administration opted to pursue a separate side agreement covering labor issues as well as an agreement covering environmental issues.[23] Aggarwal (1995, p. 34) has summarized the main features of the labor side agreement as follows:

> "First, the NAFTA supplemental agreement contains a more comprehensive list of labor standards than the five typically present in U.S. trade programs [which are noted below]. The agreement commits each party to the promotion of eleven broad labor conditions ranging from freedom of association to migration policies. Second, the agreement does not attempt to apply U.S. standards or...common uniform criteria in its evaluation of labor conditions in other countries. Instead, the agreement contains different enforcement mechanisms for different standards. The complaint process consists of three stages--filing a petition with the domestic National Administrative Office (NAO), Ministerial consultations, and lastly consultation with the Evaluation Committee of Experts (ECE). Complaints pertaining to freedom of association, the right of collective bargaining, and/or the right to strike can only be taken to the second stage of the complaint process. More importantly, sanctions cannot be utilized to encourage enforcement of laws pertaining to these rights. Of the eleven labor principles, only the implementation of those pertaining to child labor, minimum employment standards, and occupational health and safety can be supported by sanctions."

Because it required some time to establish the institutional framework following the implementation of NAFTA in January 1994, there has been limited experience to date in administering the labor side agreement. As of August 1996, the U.S. NAO has received five submissions alleging non-compliance by Mexico with its labor laws. These submissions have involved issues of freedom of association being denied to Mexican workers. No action was recommended on two submissions, the third was withdrawn, and the fourth and fifth are pending. Mexico has received one

---

[22] A useful reference is Lemco and Robson (1993).

submission about U.S. noncompliance with its labor laws, involving closure of a subsidiary of the Sprint Corporation in San Francisco. This case is pending.

It is of course interesting to ask whether the NAFTA labor side agreement might serve as a model for an agreement to be incorporated into the WTO. This seems doubtful since the NAFTA side agreement goes beyond what are considered to be core labor standards. Further, the side agreement emphasizes the observance of existing national laws governing labor standards in the NAFTA member countries rather than the intercountry harmonization of these laws that proponents of labor standards favor. Finally, not all standards are subject to sanctions and those that are (i.e., child labor, minimum employment standards, and occupational safety and health) are precisely ones that have engendered much of the ongoing controversy in the global context.

National/Unilateral Arrangements

As noted in Brown, Deardorff, and Stern (1996, p. 229), since the 1980s it has become increasingly common to include international labor standards criteria in U.S. foreign economic legislation.[24] The most important of these actions have been in establishing eligibility for trade preferences in the 1983 Caribbean Basin Economic Recovery Act and the 1984 renewal of the Generalized System of Preferences (GSP), and making the foreign denial of worker rights actionable under Section 301 of the 1988 Trade Act. The 1988 Trade Act also expanded the requirements of the Departments of State and Labor to submit periodic reports to Congress on human rights abuses and foreign adherence to internationally recognized worker rights. The stipulations on labor standards in the GSP were made mandatory. GSP eligibility has in fact been revoked

---

[23] At the time, the negotiation of these side agreements may have been helpful in obtaining Congressional approval of the NAFTA. However, as I note below, the resort to such side agreements does not carry over necessarily to the multilateral context.

[24] The standards include: (1) freedom of association; (2) the right to organize and bargain collectively; (3) freedom from forced labor; (4) a minimum age for employment; and (5) acceptable conditions of work, including a minimum wage, limitations on hours of work, and occupational safety and health rights in the workplace.

at times for a number of developing countries until they showed evidence that the offending actions had been or were in the process of being eliminated. Apparently prompted by the U.S. experience, the EU has adopted similar labor standards criteria for its GSP program to become effective in 1998.

While there may be instances in which countries have improved their labor standards in order to maintain GSP eligibility, these cases may not be important economically, considering the size of the countries involved and the limited benefits from the GSP because of the restricted product coverage. Also, in the future the value of GSP will be eroded as the result of implementing the tariff reductions negotiated in the Uruguay Round. Nonetheless, it may appear that the experiences with quid-pro-quo actions under the GSP program can possibly provide some useful insights into the design and implementation of policies and procedures governing trade-linked labor standards in other contexts. This may be misleading, however, since the removal of GSP eligibility is essentially decided unilaterally by the United States and the EU, both of which are obviously very powerful entities in the global trading system. Unilateral U.S. action can also be taken under Section 301 of the U.S. Trade Act. One should be wary therefore of arrangements in which developing countries may be coerced into taking actions detrimental to their own interests in response to pressures from their more powerful trading partners.

Other Arrangements

There are a number of other arrangements that deserve mention in addition to those already discussed above.

For example, as noted in OECD (1996, pp. 8-9), the OECD has been active in promoting cooperative programs of economic development in which practical measures backed up often by multilateral and bilateral financial assistance can be devised to deal with some of the underlying causes of poverty in poor countries that may be reflected in the employment of children and the absence or relatively weak enforcement of core labor standards. The OECD and ILO have also developed international codes of conduct applicable to multinational enterprises (MNEs) that may assist in improving labor standards and

working conditions in MNE affiliates in host developing countries. Individual MNEs can also attempt to develop codes of conduct on their own, as Aggarwal (1995, p. 39) has noted has been done by such U.S. MNEs as Levi Strauss, Liz Claiborne, Nike, Reebok, Sears, Timberland, and Walmart. These cooperative efforts and codes of conduct are essentially voluntary in nature, and, of course, there is no guarantee that they will be effective in all circumstances in low-income countries, as some MNEs have already discovered. Nonetheless, they serve an important role insofar as they help to focus attention on the importance of the root causes of underdevelopment and the types of business practices that may help low-income countries to raise per capita incomes and improve conditions of work.

Finally, we may reiterate the importance of consumer labeling in providing a market-based method for helping to improve labor standards when these standards can be treated as private goods. The advantage of labeling is that it provides information about production processes being used and allows consumers in making their consumption choices to reflect the satisfaction that they derive from the presumed realization of higher labor standards internationally.[25] When labor standards are considered to be public goods, there will be a need for governmental policies. What is important is that these various private and public actions can be carried out without the coercion that may be involved when efforts are made internationally to influence governments to change their domestic labor-market policies.

VI. Conclusions and Implications for Policy

The initial motivation for this paper was to consider whether international labor standards should be incorporated into the rules and mandate of the WTO. A case could possibly be made for devising WTO

[25] Aggarwal (1995, pp. 39-40) cites the example of the Child Labor Coalition, which was formed in 1989 by several religious, human rights, and union groups for the purpose of informing consumers in high-income countries about child labor conditions used in producing goods such as rugs in South Asia. The Coalition has sponsored the so-called Rugmark campaign which provides producers with a certifying label that they can attach to their exports indicating that they do not employ child labor. According to de Jonquieres and Williams (1996), the United States has proposed in the ILO that the Rugmark labeling system be extended to clothing and other products.

rules and disciplines to improve core labor standards in low-income countries and, by the same token, to prevent high-income countries from abusing their economic power in seeking measures that would be detrimental to the cost competitiveness and economic welfare of low-income countries.[26] However, it is difficult in my view to make this case convincingly because of the diversity of labor standards in countries with differing national characteristics, policies, and institutions. Furthermore, my literature review suggests that there are no compelling theoretical and empirical grounds to support the international enforcement and harmonization of labor standards.[27]

What then should be done? Issues of international labor standards have historically been the province of the ILO, which is often criticized because it lacks a mechanism for enforcement of discipline to raise labor standards and because it espouses an interventionist social agenda. While these criticisms may be true, they miss the point in my judgment. There is ample evidence that labor standards are raised as countries achieve higher levels of economic development and per capita incomes. If so, then what is needed are policies to provide technical and financial assistance to promote economic progress and the accompanying realization of higher labor standards in low-income countries.

With sufficient encouragement and increased financial support, the ILO can provide a multilateral forum that would serve to strengthen its role and authority in pursuing improved labor standards internationally. I recognize that this may not accord with the current policy positions of the United States

---

[26] Bernard Hoekman has suggested that some existing features in the WTO such as the agreements on pre-shipment inspection and trade-related intellectual property rights could be helpful in facilitating the provision of information to international traders and consumers.

[27] I would take issue therefore with the point made in the OECD Report (1996, p. 6) that: "Even though efforts to improve observance of core labour standards may be facilitated by economic growth and freer trade, there are reasons to doubt that market forces alone will automatically improve the standards. Hence, the importance of more direct promotion mechanisms." The key words here are "automatically" and "direct." As I have tried to make clear in my discussion and as Srinivasan also notes in his comment, it may well be that labor-market failures are present in many countries. But if this is the case, the optimal policies are domestic in character, and it is by no means obvious why international policies are preferred and how they can better overcome the domestic market failures at issue.

and many of the member countries in the European Union that would link labor standards and trade in the WTO.[28] But I would urge in conclusion that these high-income countries redirect their positions on international labor standards to reinforce the institutional role for which the ILO has been designed.[29]

[28] Indeed, some of the Symposium participants characterized my position as a "head in the sand" attitude and ignoring political realities. I recognize that policies are driven by politics. But this is no justification for condoning measures which are ill conceived and aimed especially at low-income countries. It is evident that international labor standards has become a very divisive and confrontational issue in the global trade community. While many low-income countries have a deep-rooted suspicion of where a WTO initiative might go, it would nonetheless certainly help to reduce tensions if these countries were to be more active in promoting domestic legislation and introducing other measures to improve working conditions and economic welfare.

[29] See Charnovitz (1995) for suggestions for reinvigorating the ILO and for changes especially in U.S. policies that would serve to strengthen the ILO and for arguments against using trade sanctions under WTO auspices to enforce international labor standards.

References

Aggarwal, Mita. 1995. "International Trade, Labor Standards, and Labor Market Conditions: An Evaluation of the Linkages," USITC, Office of Economics Working Paper No. 95-06-C (June).

Anderson, Kym. 1996. "Social Policy Dimensions of Economic Integration: Environmental and Labour Standards," in T. Ito and A. O. Krueger (eds.), *Regionalism vs. Multilateral Trade Agreements*. Chicago: University of Chicago Press for the NBER.

Bhagwati, Jagdish. 1995. "Trade Liberalisation and 'Fair Trade' Demands: Addressing the Environmental and Labour Standards Issues," *The World Economy* 18:745-59.

Bloom, David E. and Waseem Noor. 1994. "Labor Standards and the Emerging World Economy," processed, Columbia University.

Brown, Drusilla K., Alan V. Deardorff, and Robert M. Stern. 1996. "International Labor Standards and Trade: A Theoretical Analysis," in Jagdish Bhagwati and Robert Hudec (eds.), *Harmonization and Fair Trade: Prerequisites for Free Trade?* Cambridge: MIT Press.

Casella, Alessandra. 1996. "On Standards and Trade: A Review of Simple Results," in Jagdish Bhagwati and Robert Hudec (eds.), *Fair Trade and Harmonization: Prerequisites for Free Trade?* Cambridge: MIT Press.

Charnovitz, Steve. 1986. "The Influence of International Labor Standards on the World Trading Regime: A Historical Review," *International Labour Review* 126:565-84.

Charnovitz, Steve. 1995. "Promoting Higher Labor Standards," *The Washington Quarterly* 18:167-90.

Commission of the European Communities. 1990. *The Community Charter of Fundamental Social Rights for Workers.* European File 6/90. Brussels: Commission of the European Communities.

De Boer, Elizabeth and Gilbert R. Winham. 1993. "Trade Negotiations, Social Charters, and the NAFTA," in Jonathan Lemco and William B.P. Robson (eds.), *Ties Beyond Trade: Labor and Environmental Issues under the NAFTA.* Canadian-American Committee: C.D. Howe Institute (Canada) and National Planning Association (U.S.A.).

de Jonquieres, Guy and Frances Williams. 1996. "Balancing fair trade and fair work," *The Financial Times* (June 20), p. 8.

Erickson, Christopher L. and Daniel J.B. Mitchell. 1996. "Labor Standards and International Trade: Background Analysis," presented at conference on "The Multilateral Trading System in a Globalizing World," sponsored by the East-West Center (August 7-9).

Fields, Gary. 1995. *Trade and Labour Standards: A Review of the Issues.* Paris: OECD.

Freeman, Richard B. 1993. "Labor Market Institutions and Policies: Help or Hindrance to Economic Development?" *Proceedings of the World Bank Annual Conference on Development Economics 1993,* pp. 117-44.

Freeman, Richard B. 1994a. "A Hard-Headed Look at Labor Standards," in U.S. Department of Labor, Bureau of International Labor Affairs, *International Labor Standards and Global Economic Integration: Proceedings of a Symposium*. Washington, D.C.: U.S. Department of Labor.

Freeman, Richard B. 1994b. "Lessons for the United States," in Richard B. Freeman (ed.), *Working Under Different Rules.* New York: Russell Sage Foundation.

International Labour Organization (ILO). 1988. *Human Rights: A Common Responsibility.* International Labour Conference, 75th Session, 1988. Geneva: ILO.

Krueger, Alan. 1996. "Observations on International Labor Standards and Trade," paper prepared for the World Bank Annual Conference on Development Economics (April 25-26).

Lemco, Jonathan and William B.P. Robson (eds.). 1993. *Ties Beyond Trade: Labor and Environmental Issues under the NAFTA.* Canadian-American Committee: C.D. Howe Institute (Canada) and National Planning Association (U.S.A.).

Lyle, Faye. 1991. "Worker Rights in U.S. Policy," *Foreign Labor Trends,* 91-54, U.S. Department of Labor, Bureau of International Labor Affairs. Washington, D.C.: U.S. Government Printing Office.

Maskus, Keith E., Thomas J. Rutherford, and Steven Selby. 1996. "Implications of Changes in Labor Standards: A Computational Analysis for Mexico," *North American Journal of Economics and Finance* 6:171-88.

Noor, Waseem. 1996. "Labor Standards: A Guise for Protectionist Policy?" processed, Columbia University.

Organization for Economic Co-operation and Development (OECD). 1996. "Report to the Council at Ministerial Level on Trade, Employment and Labour Standards," COM/DEELSA/TD(96)9/FINAL (May 3). Paris: OECD.

Pangestu, Mari. 1996. "Asia to West: Stop Playing the Labor Game," *The Asian Wall Street Journal Weekly* (July 1, p. 18).

Reich, Robert. 1994. "Keynote Address," in U.S. Department of Labor, Bureau of International Labor Affairs, *International Labor Standards and Global Economic Integration: Proceedings of a Symposium.* Washington, D.C.: U.S. Department of Labor.

Rodrik, Dani. 1996. "Labor Standards in International Trade: Do They Matter and What Do We Do About Them?" Paper prepared for the Overseas Development Council (February).

Sapir, André. 1995a. "Symposium: Does Free Trade Require Fair Trade and Harmonisation? Introduction," *The World Economy* 18:741-44.

Sapir, André. 1995b. "The Interaction Between Labour Standards and International Trade Policy," *The World Economy* 18:791-803.

Srinivasan, T. N. 1994. "International Labor Standards Once Again!" in U.S. Department of Labor, Bureau of International Labor Affairs, *International Labor Standards and Global Economic Integration: Proceedings of a Symposium.* Washington, D.C.: U.S. Department of Labor.

Srinivasan, T. N. 1995. "International Trade and Labour Standards," in Peter van Dyck and Gerrit Faher (eds.), *Challenges to the New World Trade Organization*. Amsterdam: Martinus Nijhoff/Kluwer.

Srinivasan, T. N. 1996. "Post-Uruguay Round Issues for Asian Member Countries," in process (August).