

Breidenstein, Gerhard

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# International Division of Labour and Structural Unemployment

by Dr Gerhard Breidenstein, Düsseldorf \*

In **INTERECONOMICS** No. 12, 1975 the case for relocation of industries in developing countries was discussed by representatives of German industry. The following article deals with the same problem from the trade unions' point of view.

Fears are growing that the present high level of unemployment is not only due to cyclical causes which will pass but also to long-term structural changes which may persist even after the long-awaited recovery has set in. "Structural weaknesses" inherent in certain branches of industry can be caused in various ways *inter alia* also through the shifting of productions and jobs to foreign parts.

In recent years this was no problem as far as the Federal Republic of Germany was concerned. Investments by German firms in foreign countries used to play a relatively insignificant role. A comparison with other industrial nations makes this clear. At the end of 1973, German direct investments abroad (the total net value of all transactions since 1952) amounted to no more than DM 32 bn. Admittedly this meant that Western Germany had moved into third place among foreign investor-nations, but it was still far behind Great Britain, with DM 85 bn and the USA with DM 315 bn. And, whereas the American concerns produce abroad four times as much as they export, so far the relation between what German firms produce abroad to what they export from Germany was a mere 0.4:1.

## Changing Trend in Investment Policy

There are, however, some signs and portents which seem to indicate that this will not always be so and that in fact things have been imperceptibly changing for some time and that more drastically than would have been thought likely<sup>1</sup>. The main reason for the change now under way is to be sought in the repeated revaluations of the D-Mark which have impaired the German manufacturers' export chances while stimulating their will to invest abroad. Besides, competitive pressure on the world markets has increased as in the industrial nations all firms, but especially those in Western Germany and Japan, are seeking abroad alternative outlets to their saturated home markets. In addition, there is also the competition

of more and more products from the developing countries coming on the world markets. Even the state-trading countries are nowadays exporting more to the non-socialist world than in former years. At the same time, an increasing number of governments of developing countries are having recourse to import restrictions in order to protect their own nascent industries. In these circumstances, German concerns see no alternative to investing abroad, that is direct in hard fought-for or protected markets in order not to lose their present or future sales chances. It is thus possible that in the long run the trend in Germany may swing away from the export of goods to the export of capital<sup>2</sup>. In an economy which is as dependent on exports as the German economy, such a movement would have grave consequences for the employment situation.

In this context much has been said and written about "international division of labour". It is argued that from the point of view of the national economy it is quite right to transfer labour-intensive industries from the highly industrialised countries, where they have become too expensive to operate, to developing countries where because of much lower wage levels the same goods may be turned out more cheaply. Such transfer, so the argument runs, is at the same time a contribution to the solution of the immense employment problems which the developing nations are facing. It would, therefore, be better if the industrial nations were to concentrate on the development and production of tech-

\* Public relations adviser on development policy to the International Department of the German Trade Unions Federation (DGB). This article was already published in German language in: *Gewerkschaftliche Monatshefte* 12/75.

<sup>1</sup> In 1974 German Companies invested DM 4.5 bn abroad; this was 60 p.c. more than in 1972.

<sup>2</sup> Such a reversal of trend has already been statistically demonstrated, at least for several individual sectors and large-scale enterprises in the HWWA-study, entitled *Die deutschen multinationalen Unternehmen. Der Internationalisierungsprozeß der deutschen Industrie* (The German Multinational Concerns - The Process of Internationalisation in the German Industry), pp. 8-14, Manfred H o l t h u s (ed.), Frankfurt 1974. According to "Spiegel", No. 46/1975, p. 98, three quarters of all the firms asked by the Ifo-Institute, Munich, declared that they intended until 1978 to invest more abroad than at home.

nologically advanced products. A liberalised world trade would enable the specialised manufacturers to exchange their goods freely.

It is being maintained that such an "international division of labour" is particularly beneficial to the developing countries; some go even further, saying it is the only viable way towards their speedy industrialisation and integration into the world trade. We propose to postpone the testing of the validity of this assertion until the end of this article. For the present we prefer to consider what effects German investments abroad and the setting up of new industries in developing countries are having on Germany's own industry.

#### Various Motives for Investments Abroad

The reasons for making an investment abroad vary of course from branch to branch and from project to project; and it is quite possible that in a particular case several motives may have been operative at once.

□ The prime motive so far for German firms to invest abroad has been their desire to *make sure of their market share or even to increase it*. This applies particularly to the countries which protect themselves against imports. In such countries it is essential to mount a production inside those tariff barriers if a permanent share of the market is to be secured. But even where import barriers do not exist — as for instance inside the EC — it is advantageous to have a factory in close proximity to where the goods are to be sold, if for no other reason than to save transport costs.

□ Another motive, which is gaining in importance, is that of *cutting costs*. There are frequently possibilities of economising on transport, of obtaining tax concessions which developing countries normally grant to foreign investors and of reducing expenditure on anti-pollution measures. But particularly in the case of labour-intensive factories an important consideration is the *saving of wages*. Even in the case of industries whose wage bills are no more than average, or even below, the siting of a factory in a "low wages country" where wages and ancillary social costs amount to only 1/10 of those in Germany can result in sizeable cuts in the amounts payable to the work force. These considerations apply for instance to modern capital-intensive textile plants where wages nowadays account for no more than about 25 p.c.

□ A third motive, usually closely connected with the prospect of wage economies, is a *favourable investment climate* — favourable that is for the private capital. Such favourable climate exists in a dictatorially ruled country such as Spain, Brazil, South Africa or Iran. Outside the Common Market,

such countries have become centres of attraction for German investors, for there free trade unions and industrial action by wage earners are banned, and everything is done to help the private investor, whereas in Germany, wage claims, code-termination and government supervision cramp his style.

□ Finally, the desire to make sure of an *uninterrupted raw material flow* may also be a reason for an investment abroad. Through such an investment it is possible to obtain at any time any quantity of any raw material at a price which is independent of the world market prices because it is arbitrarily fixed by the concern for internal purposes such as the transfer of profits from one part of a multinational concern to another. In contrast to American and British investments abroad, German investments in the raw material sectors have been comparatively rare; yet in view of the increasing urgency of the raw material problem this is quite liable to change in future.

□ It need hardly be mentioned that behind all these separate motives there is the prime motive force activating all private investment decisions: the striving for maximum profits with which in the long run to generate more capital. If the chances of making profits worsen at home, or, by the same token, prospects abroad are better than at home, capitalist enterprises invest abroad.

#### The Industrialisation of Developing Countries

Direct investments from industrial countries create new production plants in developing countries. Furthermore, government and international development aid finances investments mainly of an infra-structural nature in developing countries. But by far the greatest part of all investments in developing countries stems from these countries' own accumulated capital reserves. These savings vary considerably from country to country and from industry to industry. Relative to total investments they account on average for 80 p.c. in Africa, 89 p.c. in Asia and even 95 p.c. in Latin America (cf. UN and OECD Statistics for the years 1969/71). In other words: even if they received no private or public capital transfers from industrial countries at all, the developing countries would nevertheless go on industrialising themselves, thus creating additional production capacities. This additional capacity will for the most part be employed to meet the rapidly rising needs of these countries' own populations and therefore constitutes no competition for production and employment in the industrialised countries.

But a part of the additional output capacities which are in process of being created in the developing countries replaces imports from indus-

trialised countries, thus reducing the latter's exports. The developing countries, compelled by the pressure of catastrophic balance of payments deficits, encourage such investments aimed at the substitution of imports. For the same reason they also step up the rate of foreign investments designed to increase exports. And, given the fact that industrialised countries are practically the only ones with markets capable of absorbing additional goods from abroad and prepared to do so, the developing countries' production for export threatens jobs in the industrialised countries just as the import substitution does. In whatever way the industrialisation of developing countries is financed — through their own savings, private investments from abroad or development aid — their industrialisation means in some way that their workers compete for jobs in the industrialised states. This is true at least in the following cases:

#### Various Ways of Threatening Job Security

□ The processing and manufacture of raw materials which the developing countries hitherto used to ship to the industrialised countries to be turned there into finished goods, now increasingly takes place in the developing countries. (Here are some examples: the roasting, packing and pulverisation of coffee beans; the spinning, weaving and sewing of cotton; the smelting of bauxite, copper and other materials.)

□ The developing countries are setting up their own factories turning out finished products to replace imports from industrialised countries (examples: manufacture of small machines, artificial fertilizers and sophisticated consumer goods).

□ The developing countries are setting up factories to turn out finished goods intended for export to industrialised countries (for example: articles of clothing from South Korea; sports goods from Pakistan, toys from Hong Kong).

□ Firms in the industrialised countries transfer the manufacture of their goods for export to foreign countries (examples: Volkswagen and Mercedes Benz transfer their lorry production to Brazil, Argentina, Mexico, South Africa, etc., agrochemical and pharmaceutical subsidiaries of German chemical concerns are to be found in all parts of the world).

□ Enterprises in the industrialised countries transfer, for reasons of cost, production plant to developing countries to re-import the cheaper goods in their finished or semi-finished form into the home market (examples: Müller-Wipperfürth has trousers sewn in Tunisia to sell them in Germany; German manufacturers of electrical appliances get their goods — household appliances,

radios, television sets — intended for the German market assembled in low-wage countries).

On the other hand, is it not true to say that the industrialisation of developing countries brings with it additional sales chances for the industrialised countries, for instance for machinery and primary products? It would be difficult, if not altogether impossible to calculate whether the above-mentioned instances of losses of jobs in industrialised countries caused by the industrialisation of developing countries is offset by the additional jobs created by the improved export possibilities the industrialised countries enjoy as a result of the industrialisation of developing countries. Actually, what is at issue is not the national balance sheet of the country's economy, but the threat to individual branches of industry. From the standpoint of the national economy as a whole it would be only fair to point out that until the end of 1973 the influx of foreign capital into Germany (about DM 34 bn) slightly exceeded the outflow of German capital abroad (DM 32 bn).

It may further be pointed out that 70 p.c. of German investments abroad went to other industrialised countries (above all to those of the Common Market). This, until the end of 1973 left only 30 p.c. or DM 10 bn for developing countries. Nevertheless, for individual branches of industry, the briefly mentioned consequences of a widely advertised "international division of labour" seem to be alarming enough to merit serious notice, even if statistical material on the issue is still largely lacking<sup>3</sup>.

Unaffected by an increasing international division of labour or by capital's propensity to emigrate are sectors of industry which satisfy our own needs and whose products or services are not suitable for being transported over long distances and must, therefore, be consumed locally. Sectors belonging to this category are of course all service industries, the energy industry, the mining and building industries, fresh farm produce; then all the basic industries (iron, steel and chemicals); heavy engineering as well as the plant construction and motorcar industries. Moreover, all sectors whose output presupposes a high degree of

<sup>3</sup> True, the authors of the above mentioned HWWA-study made some inquiries and published some estimates concerning some firms typical for their particular sector. They estimated inter alia for 1971 the relation of the firms' foreign production to their home sales. They arrived for the processing industry at 6.5 p.c.; far above average were the figures for the chemical industry with 17.5 p.c.; the motor vehicle industry with 14.1 p.c. and the electro industry with 11 p.c. The corresponding relationships between the number of workers employed abroad and at home, which interests us in this connexion were as follows: Processing industry 7.1 p.c.; chemical industry 20.3 p.c.; electro industry 15.8 p.c.; motor vehicles 10.6 p.c. The textile industry shows below average figures: 3.4 and 5 p.c., respectively. On the other hand, some leading individual textile concerns are especially conspicuous, for example the Triumph AG. This concern produces 41.5 p.c. of its total output abroad employing to do so 51.6 p.c. of its total work force (cf. Tables 34, 35, 36, pp. 141-146, *ibid.*).

technical ability and know-how will also remain in the industrial countries. In fact, there is a tendency for such sectors as the electronic industry, the precision instrument makers, the aircraft industry as well as the research and development activities of all industries to concentrate even more than before in industrialised countries.

#### Affected Industries

On the other hand, all technologically simple production processes as well as all the highly automated ones can easily be transferred to developing countries or be displaced by local industries. Exporting such goods to the markets of the industrialised countries (by the developing countries) or re-importing them (by firms of the industrial nations) is a different matter. High transport costs make such a course prohibitive for any but light industries manufacturing or processing textiles and leather, or making toys, musical, precision or optical instruments. Likely to benefit are further sections of the wood and metal processing industries, and the electro-technical industry (domestic appliances, radio and television sets and high-fidelity equipment). The more wage intensive a production process, the greater the incentive to transfer it to a "low wage country" or, alternatively, to mount it there. Not infrequently only certain labour-intensive phases of the production process, and not the whole process in its entirety, are evacuated, as for instance the sewing together of the parts in the case of shoe or glove making.

In as far as the output is intended for the new markets in the developing countries no transport problems exist. On the contrary, the transfer of production to a developing country is more likely to result in a saving of transport costs. In these conditions a fair number of other industrial sectors are likely to find a transfer of their production plant an attractive proposition. Among these are: iron and steel production and processing, even ship building, further the serial production of motor vehicles as well as chemical concerns, particularly those manufacturing pharmaceuticals and agro-chemicals and lastly branches of the medium-heavy industry like mechanical engineering.

The above-mentioned enumeration shows that it is not always the textile and clothing industry which reduces jobs inside Germany through organising cheap imports or transfer of production plant to foreign parts. Admittedly, the decline in the number of people working in that industry is particularly drastic. In the period from 1967 to 1974 its work force decreased by roughly 100,000 and it is estimated that a further 70,000 jobs will be lost in the next ten years. So far, nobody seems to have calculated how many of these

jobs will simply be "rationalised" out of existence and how many will vanish through output capacity being transferred abroad. Up to the present it is not yet possible to gauge, with a similar degree of accuracy, the effect of these trends on other industries which have been mentioned above as theoretically being likely to suffer a similar fate (but cf. statistics in footnote 3). All the same, a study recently undertaken on behalf of the Federal Ministry for Economic Cooperation by the Institute for World Economics, Kiel estimates that by 1985 between 250,000 and 600,000 work places will be lost in the processing industry through liberalised imports from developing countries, some branches shedding up to a third of their work force, whereas others reduce theirs by more than 20,000. On the other side of the scale only some 200,000 new jobs are expected to be created to cope with increased exports to the developing countries.

The other effect — i.e. the substitution of exports through German firms transferring their production abroad — is presumably a relatively recent phenomenon. In the year 1974, however, German exports showed for the first time an appreciable decline. Was this due solely to the world recession, or can it possibly be the first indication of a movement to replace exports by manufacturing goods in foreign countries? To be said in favour of the latter is that the change of the parity of the German Mark could not immediately lead to an increase of the foreign output by German firms; for this to happen would certainly take a few years. In any event, there is reason enough to study more thoroughly than has been possible in the present article the likely and actual effects on the German economy and in particular on the labour market of the much publicised and already practiced "international division of labour".

This is by no means to be taken as a plea for stopping the transfer of production capacity on principle — quite apart from the fact that there is no political power on the horizon strong enough to prevent multinational concerns from effecting such transfers if such is in their interest. Nor is it the intention to advocate a primitive protectionism as a means of sheltering German industry from the competition of cheap imports. In the long run it would not be economically justifiable to keep alive by protective tariffs and subsidies output which can be produced more cheaply in other parts of the world. This is why the German Trade Unions Federation — for instance at its meeting in Hamburg in May 1975 — has declared itself in favour of greater integration of developing countries into world trade (and this means, of course, also as exporters). But this on one important condition: on condition that the shrinkage of certain industries inside Germany and the resultant re-

duction in the number of jobs are fully made up by the creation of new jobs in growth industries. This, in the view of the trade unions, requires a thorough going study of prospective trends and an actively guided structural plan. To deal with structural unemployment as it arises in individual sectors, it would be necessary to investigate at much greater depth than has been done hitherto the effect of increasing foreign investments by German firms and to what extent the employment situation is likely to be impaired by cheap imports from developing countries, or, for that matter, from East-European countries. Provided the consequences of an on-going process of change in the international division of labour are analyzed as accurately as possible and are parried by controlled investments and/or overall economic co-determination, then there is no need for the German trade unions to raise any objections to such developments.

It is true, though, that no such active control has so far existed, at least not to an adequate extent, and it is to be feared that behind the present largely cyclical unemployment there may possibly lurk a good deal of structural unemployment. As long as there are grounds for such a suspicion, the trade unions must remain sceptical. But there are also a few development-political considerations, which may be mentioned in conclusion and which may serve as a warning against too enthusiastically welcoming the "international division of labour", however much it is publicized by interested parties.

#### **International Division of Labour from the Standpoint of Development Policy**

In relations between industrialised and developing countries the concept of international division of labour is by no means new. It existed as long ago as colonial times — times when the colonies used to provide agrarian and mineral primary products whereas the colonial powers, which were just in the process of becoming industrialised, provided for their part consumption goods and later-on investment goods. The economic dependence which resulted from such an order of things has often given rise to complaints. Yet the resulting single-crop farming and neo-colonial economic relations have continued to exist to the present day. This dependence and the direct and indirect exploitation of the developing countries which flows from it is being more and more regarded as the decisive cause of the poverty problems confronting the Third World today<sup>4</sup>.

<sup>4</sup> This has been particularly taken up and described in the Latin-American dependencia-discussion, especially in publications by J. Gaitung and D. Senghaas, mainly *Imperialismus und strukturelle Gewalt (Imperialism and Structural Power)* and also *Peripherer Kapitalismus (Peripheral Capitalism)*, both published in the Suhrkamp Edition by D. Senghaas.

International division of labour, so urgently demanded in recent days, is hardly likely to alter this dependence significantly. For, if in future the developing countries are "permitted" to deliver, in addition to primary commodities also labour-intensive finished goods, but will still have to rely on the industrialised countries for the delivery and maintenance of all their technologically advanced capital goods — all that will have happened is that the developing countries will have moved up one rung of the ladder. The state of dependence stemming as it does from a division of labour between unequals remains thus an "asymmetrical dependence" and this means domination and exploitation.

In the long run the developing countries will succeed in fruitfully exploiting their natural resources and achieve true development only, if economically they go their own way, as little influenced by others as possible, avoiding, rather than seeking, further involvement in the crisis-plagued world trade, striving for a higher degree of autonomy and developing their industries themselves and that in as many directions as feasible — and possibly with a regional division of labour. Some countries (e.g. China, North Korea and Albania) have demonstrated that such striving for autonomy is not only possible, but also very successful.

The developing countries must also solve their employment problems themselves, applying their own (labour-intensive, not capital-intensive) methods and strategies. The transfer of our highly automated production methods into the developing countries presumably does more harm (destruction of local places of employment unable to compete) than good (small number of new jobs). Today's unemployed in the Third World are estimated to number 150 million; this figure will probably increase annually by 30 million which means that by 1980 Third World unemployment will have doubled to 300 million. Even a transfer from the industrialised countries of 15 million jobs — which would already mean a catastrophic increase of 100 p.c. of our present unemployment — could do no more than either bring employment to 10 p.c. of those at present out of work in the Third World or absorb half the unemployed coming newly on the labour market in one single year. It is obvious that a forced transfer of jobs within the framework of an "international division of labour" solves no problems in the Third World but causes new ones in our countries. The only beneficiaries of such an "international division of labour" would be the multinational concerns in that it would enable them to drive the workers of various countries into a wages competition with each other and to exploit all cost differences to their advantage.