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The Employment Problem in Latin America: Perceptions and Stylized Facts

by

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Employment in Latin America: What is the Problem and How to Address it?

Inter-American Development Bank
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1 The authors gratefully acknowledge the comments of Ricardo Hausmann, Carmen Pagés and Miguel Székely, and the valuable assistance of Mauricio Olivera in furnishing the labor statistics.
Introduction

Most Latin Americans are concerned about lack of jobs, low wages and the possibility of being unemployed. Macroeconomic policies have taken a radical turn in the past decade, which has boosted economic growth in the region by more than two percent points, reduced the inflation rate to below 30% in nearly every country, and opened up new opportunities for private investment in the most diverse economic activities. But during the 1990s, employment has grown at a slower pace than in the second half of the 1980s, unemployment rates have not declined and informal sector activity has increased. Although real wages have performed much better, whether earnings have risen higher, enormous wage gaps have opened up between skilled and unskilled workers. And while workers lament the lack of jobs, employers consistently complain about the scarcity of properly qualified staff and the deficiencies of the educational system. The employment problem in Latin America is undoubtedly one of the greatest challenges faced by the governments in the region.

This article, which serves as an introduction to the group of studies prepared by the Office of the Chief Economist of the IDB, will present the perceptions of Latin American citizens and employers concerning the employment problem and will compare them to the conditions in the labor markets of the region.
I. PERCEPTIONS

What importance do Latin Americans assign to the employment problem?

For the average Latin American, the principal reason for concern is the lack of jobs and of adequate earnings. According to the Latinobarómetro survey, which is conducted by an independent private entity in 17 countries, 19 out of every 100 Latin Americans think the biggest problem today is unemployment, and eight cite low wages. These job-related problems are ranked higher than inflation, poverty or any other social ill suffered by the countries in the region, such as delinquency, violence or drug addiction. Only one other problem receives more attention: education, which is the biggest problem for 15 out of every 100 Latin Americans (Figure 1).

![Figure 1: Importance of the Problem of Unemployment (Percentage who think it is the number 1 problem*)](image)

* Simple Average of 17 Countries
Source: Latinobarómetro 1997

The great majority of Latin Americans also believes that the unemployment problem could affect them personally at any time. Seven of ten Latin Americans rate themselves concerned (or very concerned) about losing their jobs or being unemployed in the next twelve months. Even in places where people are less troubled about their job prospects, such as Chile and Uruguay, five out of every ten people are concerned or very concerned about the possibility of unemployment (Figure 2).
Latin Americans are calling for government action to confront employment problems. Surprising as it may seem after a decade of market reforms—which were applied in an effort to reduce government intervention in economic activities—88% of Latin Americans think it is the government’s responsibility to “give work to everyone who wants to work,” and a similar percentage (85%) believe that the government is also responsible for “providing a decent standard of living for the unemployed.” This opinion differs little from country to country, despite any difference of approach their economic policies may have taken in the past.

It is often said that Latin Americans are living in a climate of pessimism about the economic and social progress of recent years, and this is witnessed by the fact that 71% of the people believe that their country is in the same or worse condition by the end of 1997 than twelve months ago. There is no doubt that this view stems in large part from a belief that the employment problems have not been resolved.

**What are the concerns of Latin American employers?**

While the average citizen finds the lack of jobs and adequate pay to be troubling, employers complain about the deficiencies in the labor supply and inadequate worker training.

According to employers, it is not easy to find workers and employees in Latin America. In a sample of seven countries considered by the Global Competitiveness Report, on a 10-point scale, Argentina receives the highest rating in Latin America (5.7 points) and Venezuela the lowest (3.4). Given the relatively modest growth rates

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2 See Appendix 1 for a more detailed description of the source and the questions given to employers.
achieved in Latin America, the difficulty in finding workers is especially critical. In fact, in a group of nine Southeast Asian countries which, until the recent crisis, had grown for several decades at average rates above 7%, obtaining workers was the same as or easier than in Latin America, where the average growth since 1980 has been a scant 2% (Figure 3).

![Figure 3: How Easy Is to Get Skilled Labor? (very easy = 10)](source: Global Competitiveness Report (1997))

The employers felt that the deficiencies in the labor supply are rooted in the educational system. In their view, education is unable to meet the needs of a competitive economy. Measured by this yardstick, the quality of education (on a scale of 1 to 10) in the seven largest economies in the region ranges from 1.2 in Venezuela to 3.8 in Chile, for a regional average of 2.8. This compares very unfavorably with the average of 6.2 exhibited by the "Asian tigers," or the 5.0 registered by the above-mentioned group of nine Southeast Asian countries (Figure 4). There is more fragmentary evidence for employers' contention that workers have little capability for keeping current and adapting to new technologies, and that this is true even for professionals and specialists within the companies, which is a reflection of the deficiencies in quality of education.

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3 As indicated for Colombia in a Fedesarrollo survey of industrial firms conducted in 1996.
Figure 4: The Educational System Meets the Requirements of a Competitive Economy

Source: Global Competitiveness Report (1997)
II. LABOR MARKET SITUATION: STYLIZED FACTS

The labor markets in Latin America create a very heterogeneous picture, owing to the differences of economic development, demographic structures, labor institutions and economic fluctuations of the various economies. Despite this heterogeneity, certain traits common to most countries can be found in the 1990s. The rates of job growth have fallen, unemployment rates have not declined in a sustained manner, informal sector activity and employment in nontradable-goods sectors have escalated, and wages have performed better than in the second half of the 1980s, but with growing differentials between skilled and unskilled workers.

• Job creation has slowed

Employment in Latin America has grown at an average rate of only 2.8% during the 1990s, which is 0.5 points slower than in the latter half of the 1980s. Most countries have been affected by this reduced job growth rate. The only notable exception is the Dominican Republic, where employment has grown at a rate three points higher. Mexico, Paraguay and Peru have seen increases, though at a much more modest level (Figure 5).
The supply of workers has also diminished

The total work force (employed and unemployed) that constitutes the labor supply is also growing more slowly than in the second half of the 1980s. The rate of increase in the labor supply has slowed from 3.6% to 2.8% in the 1990s, the only departures from this trend being Argentina, Mexico, Peru and Guatemala (Figure 6). The growth of the labor supply is the result of the rate of growth of the working-age population, and the percentage of that population that decides to participate in the labor market. During the 1990s, both factors have moved in the same direction. On the average for 17 countries, the working-age population is growing at a rate 0.4 points slower than in the second half of the 1980s. Only Argentina has deviated noticeably from this trend: its working-age population is increasing at nearly 0.3 points higher. (Bolivia and Uruguay are also witnessing accelerated growth, but on a more modest scale.) The rates of participation in the work force have also contributed to a systematic reduction in supply. In Bolivia, Chile and Peru, the percentage of the working-age population taking part in the labor market has dropped. In all the other countries, participation has remained stable or has increased at a rate below that of the early 1980s, thus contributing to the reduced increase in the labor supply (see the detailed calculations in Appendix 2).

Unemployment rates have not fallen

Higher economic growth rates and more moderate rates of increase in the labor supply could well have produced significant drops in the unemployment rates. But that is not what happened. During the past decade, unemployment rates have fluctuated with no definite pattern: the average rate of unemployment (for 19 countries) has remained around 10%. And if each country is weighted according to the size of its labor force, we find that the percentage of unemployed Latin Americans rose from less than 6% in the late 1980s to around 8% in 1996 (Figure 7). The most conspicuous feature of the unemployment rates has been their persistence: they have tended to remain low where they were low before, and vice-versa. The greatest changes have occurred in Argentina, Barbados and Nicaragua, with increases of more than three points between 1989-90 and 1995-96, and in Bolivia, Honduras, Panama and the Dominican Republic, which have achieved reductions of three or more points in their unemployment rates.
Informal employment has increased

The informal employment rate increased from an average of 51.6% in 1990 to 57.4% six years later. Thus, in that brief period, the percentage of those self-employed, working in small enterprises of 5-10 workers, or in domestic worker positions rose nearly 6%; all of these cases involving reduced coverage by worker protection mechanisms and social security. All 14 countries with available information showed increased rates of informal employment (see Figure 8), and throughout the region, an average of 80 out of 100 additional jobs
created in the 1990s have been informal. In the extreme cases of Argentina and Mexico, while informal employment has increased considerably, formal employment has dropped in absolute numbers.\(^4\)

- **Employment rates have risen in the nontradable-goods sectors**

During the 1990s, most countries have experienced increased job growth in the nontradable-goods sectors, which include construction and services. Participation in these types of jobs rose from 58.4% in 1990 to 63% five years later in the group of 18 countries examined in Figure 9. Only Brazil showed a different trend. Despite that exception, on the average, all of the additional jobs created during the 1990s in Latin America have been in the nontradable-goods sectors.

![Figure 10: Public Employment Percent of Urban Employment (1995 vs 1990)](image)

- **Public employment rates have fallen**

In 14 countries, participation in public employment fell from 15.3% in 1990 to 13.2% in 1995. In seven countries (Argentina, Brazil, Costa Rica, Ecuador, Panama, Peru and Uruguay), direct employment in the public sector fell in absolute terms, in some cases quite significantly. Calculations for Argentina indicate that the reduction in public employment represented 11% of all formal employment, while the corresponding figure for Peru was 7% (Figure 10).

\(^4\) Note, however, that the most recent data available for this comparison are from 1996, when these two countries were still recovering from the effects of the Tequila crisis.
• **Wages have recovered**

In most Latin American countries, the performance of real wages has been more favorable in the 1990s than in the latter half of the 1980s. On the average, real wages throughout the region have tended to increase from their lowest point reached in 1991 (but in some countries they have not exceeded the levels achieved in the early 1980s). Although real wages have again moved upward in most cases, some countries —Barbados, Ecuador, El Salvador, Trinidad and Tobago, and Venezuela\(^5\) — have had significant drops. With the exception of Barbados, wages in those countries also fell in the latter half of the 1980s, so the decline has been sharper (Figures 11 and 12).

• **Latin American wage differentials —the highest in the world— have increased**

In places where real wages have registered the greatest increases during the 1990s, wage differentials between skilled and unskilled workers (or between professional and administrative employees as compared with factory workers and manual laborers) have increased substantially. The wage differentials have seen the greatest increase in Peru, Colombia and Mexico (Figure 13). In these three countries, real wages of the more skilled workers have increased during the 1990s at an annual rate at least three points above those of unskilled workers. The wage gap has increased more than 30% in Peru, 20% in Colombia, and nearly 25% in Mexico. Conversely, where wage gaps have been reduced in the 1990s, this has occurred in smaller proportions, with Costa Rica registering the maximum (5%). And even where the wage gaps between these two groups of workers have narrowed, the total distribution of wages has deteriorated (measured, for example, by the standard Gini Coefficient).\(^6\)

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5 The figures also show a drop in Argentina, though this result should be viewed with caution because of the difficulty of measuring real wages in the hyperinflationary environment of 1990 (base year for comparison).

6 For more on this subject, see the study by Duryea and Szekely (1998).
A similar phenomenon of wage gap expansion has been observed in other regions of the world, usually attributed to the technological development of the past decade. But Latin America stands out in international comparisons, in both the magnitude and the recent trends of the wage gaps. Consider the data shown in Figure 14. Using as a basis of comparison the (relative) gap in wages in the industrialized countries, we find that the gaps in Latin America are twice as large. In the four “Asian tigers” (Korea, Hong Kong, Singapore and Taiwan), the wage differentials between office workers and manual laborers are similar to those in the industrialized countries; and although there are greater relative wage gaps among other, less developed countries in Asia and Africa, they are less pronounced than in Latin America. While the wage differentials in
these groups of countries have been gradually approaching those of the industrialized countries, that pattern was broken in Latin America in the late 1980s, and during the 1990s the differentials have tended to increase.\footnote{The reader can refer to the Appendix for the details of these calculations. Essentially, it is a comparison of earnings among workers with the same personal characteristics (education, experience, age, family status) in jobs that are similar from one country to the other (department manager of a company of a certain size, secretary, chauffeur, construction worker, etc.). The method of calculation ensures that comparisons are not affected by changes in the composition of the labor supply or in employment, or by macro price phenomena (inflation, variations in exchange rate, etc.).}
III. PERCEPTIONS AND PATTERNS: SIMILARITIES AND DIFFERENCES

A brief consideration should be given to whether the concerns of the public coincide with the stylized facts of the labor markets in Latin America as described in the preceding section. This comparison will show that the importance attributed to the unemployment problem in each country is a good reflection of the magnitude of the problem, and that concern over becoming jobless is linked to the extent of informality and to the expansion of employment into the nontradable-goods sectors. Latin Americans’ opinions on the wage problem, on the other hand, seem to contradict the facts.

- The unemployment problem: coincidence of perception and reality

Latin Americans’ concern with the lack of jobs has a basis in reality. In countries where the unemployment rates are higher, such as Nicaragua, Argentina and Panama, a higher percentage of the population clearly feels concerned, as compared to countries like Honduras, where the reported unemployment rates are considerably lower. However, in Colombia and Venezuela, though unemployment has recently increased, other problems receive more attention (Figure 15).  

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8 In Colombia, political violence is considered the most important problem by 31% of those surveyed, and in Venezuela education by 21%.
Concern over becoming unemployed: greater in countries with high informal employment and where employment has risen in the nontradable-goods sectors

In countries with high informal employment rates, a higher percentage of people say they are “concerned about losing their jobs” (Figure 16). In informal jobs, workers usually lack the job protection mechanisms that are associated with jobs in larger companies, such as access to social security and certain rights to job stability and severance pay. Consequently, turnover in these jobs is higher, and the risk of unemployment tends to be greater.

Likewise, in the countries where employment in the nontradable-goods sectors has increased as a percentage of total employment, a higher proportion of interviewees say they are “concerned” or “very concerned” about losing their jobs (Figure 17). In fact, the increase in informal jobs and employment in the nontradable-goods sectors are related phenomena, because small enterprises and independent workers are more common in the nontradable-goods sectors, such as construction, personal services and trade, than in the industrial sectors.

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9 The article by Márquez and Pagés (1998) presents evidence of this phenomenon.

10 See the article by Lora and Olivera (1998).
• The wage problem: contrast between perception and reality

Paradoxically, the countries where citizens ascribe greater importance to the wage problem are the ones where the most progress has been made in the 1990s, and vice-versa (Figure 18). A notable case is Peru, where 10% of the population believes that low wages are the country’s principal problem, despite the fact that average wages appear to have gone up consistently during the 1990s. Although this case could be attributed to the large wage lag of the past, the same argument cannot be applied to a case such as that of Chile, where complaints are even higher. The apparent contradiction between the perception and the reality of the wage problem holds up when it is related to the growing wage differentials, which leaves open the question of what factors are influencing the perception of this problem.
IV. CONCLUSION AND TOPICS FOR STUDY

Despite Latin America’s improved economic performance, employment growth in the 1990s has slowed, unemployment rates have not tended to decline systematically and informal sector activity has increased. Real wages have recovered, though in many countries only partially when compared with the 1980s, and countries with the greatest increases have also seen a more substantial widening of wage differentials. The wage gaps in Latin America between skilled occupations and manual labor are the largest in the world.

This situation opens up innumerable questions about the functioning of the labor markets in the region and the implications for economic policy. In view of the diversity of topics for analysis, the group of studies following this introductory article will focus on selected topics, which are summarized below.

• The slower growth of the working-age population and slower rates of participation in the labor market are both well-known phenomena in most countries. Do these supply factors explain the slower growth of employment? To what extent are these two phenomena reflecting demographic factors and other forces of a structural nature that could continue into the future?

• Unemployment rates have not tended to decline systematically, despite the countries’ improved economic performance and a slower increase in the labor supply. What characteristics of the labor supply are causing this rigidity? To what extent is the rigidity of unemployment rates due to inflexibility in the labor markets? Which labor groups are affected by these rigidities? What inferences can be made about future unemployment rates?

• The patterns of employment have changed in three directions in the 1990s: informal employment has increased, participation in nontradable-goods sectors has risen, and public employment has declined. Is there a link between these changes in patterns and the reorientation of macroeconomic and structural policies in the past decade? What role can be attributed to job protection mechanisms and other rigidities of the labor market in these findings? Is it correct to interpret informality as a refuge for the unemployed, when it may be a response to the changes in the composition of demand by sectors and by firms’ size?

• Real wages have recovered in the 1990s, while employment growth has slowed. Does this constitute evidence that high wages are limiting job creation, or that there are limitations in the labor supply that are putting pressure on wages? And linked to that same question, to what extent are the growing wage differentials caused by an insufficient supply of skilled labor, and to what extent are they the result of changes in the demand pattern that may have been induced by the new economic conditions in these countries?
Bibliography


APPENDIX 1
Statistical Sources

Perceptions of Latin Americans. The source for these statistics is the Latinobarómetro, an annual Latin American public opinion poll that covers 16 countries in the region. The results presented refer to the poll conducted in November and December 1997. The numbers cited in the text are simple country averages, but the Figures also show averages weighted by population.

Employer perceptions about the labor supply. The indicators for quality of the labor supply come from the Global Competitiveness Report, which is published by the World Economic Forum. The information is for 1996, except for Peru, which is for 1995, since that country was not included in the 1996 version. It is based on surveys of employers, who are asked to rate on a scale of 0 to 10 how strongly they agree with the statements ?it is easy to obtain skilled workers? and ?the educational system meets the demands of a competitive economy.? The Figures show simple country averages (no weighted averages).

Wage comparisons with countries in other regions of the world. The sources for these comparisons are statistics on earnings by occupation compiled by Union Bank of Switzerland every three years and published in Prices and Earnings Around the World. For Latin America, this source includes the following cities: Bogota, Buenos Aires, Caracas, Mexico City, Panama City, Rio de Janeiro and Sao Paulo. The comparisons were made against the simple average of 24 industrialized countries, the capitals of the four ?Asian tigers? (Hong Kong, Seoul, Singapore and Taipei) and 12 cities in other, less developed countries: Bangkok, Bombay, Istanbul, Jakarta, Jeddah, Johannesburg, Kuala Lumpur, Lagos, Manama (Bahrain), Manila, Nairobi and Nicosia. In the latter group, it was necessary to fill information gaps for some cities in a few countries, which was done by using the average variations for the remaining observations from the same group. All wages are expressed in dollars, with no adjustments for local purchasing power. Wages are defined as annual gross earnings, which include any wage supplement, such as profit sharing, bonds, vacation bonuses, extra pay and family allowances. All calculations are simple averages of wages or of relative wages in each occupation for all cities in each group.

The occupations included in the calculations are defined below, according to the source cited:

Administration:

- Department manager: manager of operations of a production department (in charge of more than 100 employees) for a large company in the metallurgical industry, with professional training completed and several years of experience in the field, about 40 years of age, married with two children.
- Engineer: employed by an industrial firm that manufactures machinery or electrical equipment, power plants or the like, with college education completed (university, technical college or advanced technical school) with at least 5 years of practical experience, about 35 years of age, married with two children.
- Credit bank employee: with complete bank training and about 10 years of bank experience, approximately 35 years of age, married with two children.
• Secretary: secretary to a department manager of an industrial or commercial firm, with about 5 years of experience (stenography, typing, computer know-how, with one foreign language), approximately 25 years of age, single.

• Salesman: in a women’s clothing department of a large department store, with sales training and several years of experience in sales, approximately 20-25 years of age, single.

Manual laborers and factory workers

• Bus driver: employed by the municipal system, with about 10 years of experience, 35 years of age, married with two children.

• Auto mechanic: with apprenticeship completed and about 5 years of experience, approximately 25 years of age, single.

• Construction worker: unskilled or semi-skilled laborer, about 25 years of age, single.

• Skilled industrial worker: with vocational training and about 10 years of experience in a large company in the metallurgical industry, approximately 35 years of age, married with two children.

• Textile industry worker: unskilled or semi-skilled machine operator in a medium-sized plant, mostly in the textile industry, about 25 years of age, single.

Other statistical sources:

Wage differentials between skilled and unskilled workers: the countries’ statistics departments and IDB calculations.


Employment in the services and construction sectors: International Labour Organization.

Employment in the public sector: International Labour Organization.

Participation in the labor market: household surveys processed by the IDB.

Working-age population: United Nations, based on national censuses.

Working population: Calculations based on household surveys processed by the IDB and working-age populations.

Real wages: International Labour Organization.

Unemployment rates: International Labour Organization.

Informal employment rates: International Labour Organization.
## Appendix 2

### Source of Change of Growth in Labor Force and Employment

<table>
<thead>
<tr>
<th>Country</th>
<th>Working Age population Growth (Annual %)</th>
<th>Participation Rate (% of Working Age Population)</th>
<th>Growth and Participation Rate (Annual %)</th>
<th>Change of Labor Force and Growth Rate (%)</th>
<th>Change of Employment Growth Rate (%)</th>
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