

**EXPLORING THE EMPLOYMENT NEXUS:
TOPICS IN EMPLOYMENT AND POVERTY**

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I. INTRODUCTION

The International Labour Office (ILO) has persistently championed the cause of expanding employment opportunities for the poor – in the form of ‘decent work’ – as an effective means of poverty reduction.¹ The notion of ‘decent work’ also conforms to the human development approach propounded by the United Nations Development Programme (UNDP) since decent work is both a constitutive element of human development and an important instrument for bringing about improvement in other dimensions of human development. Both perspectives agree that while economic growth is essential for poverty reduction, the poor need expanded opportunities for decent work if they are to enjoy the benefits of growth better.

While it seems intuitively obvious that decent work should be important for poverty reduction in particular and human development in general, much work remains to be done before the analytical and empirical relationships between the two are clearly understood. Such an understanding is essential for devising appropriate policy measures to strengthen the ‘decent work’ route to poverty reduction. For this purpose, ILO and UNDP have decided to embark on a collaborative programme to advance the understanding of the links between employment and poverty.

It is in this background that the Task Force on the Joint ILO-UNDP Programme on Employment and Poverty engaged the present consultant to prepare a paper outlining:

1. The scope, content and focus, as well as, the modus operandi for a joint ILO-UNDP report on employment and poverty, and
2. Possible Topics for a joint research programme on issues relating to employment and poverty.

In writing the paper, the consultant started from the premise that before suggesting topics for a report and a research programme on employment and poverty, it is first

¹ For a recent presentation of this position, in the specific context of Africa, see ILO (2001).

necessary to have a conceptual framework exploring the analytical links between growth, employment and poverty. Once this framework is in place, the topics and contents of a report will suggest themselves; and once the topics for the report are identified, research topics will follow logically as a means of supporting the report.

Accordingly, the bulk of the paper is devoted to developing and explaining a conceptual framework that explores the role of employment as a critical nexus between growth and poverty reduction (Section II). Based on the issues and hypotheses thrown up by this framework, three topics are then identified, which the ILO-UNDP Reports might try to elaborate (Section III). Corresponding to these three topics, three research agenda are then identified (Section IV).

II. EMPLOYMENT AND POVERTY REDUCTION: A CONCEPTUAL FRAMEWORK

II.1 The Relationship between Growth and Poverty

There was a time when the growth of national income was taken to be the explicit objective of economic development. More recently, poverty reduction has come to be accepted as the explicit objective. A synthetic view is now emerging, however, which contends that the two objectives are not really different, because sustained poverty reduction is not possible without sustained and rapid economic growth. A spate of recent empirical studies indeed demonstrates that persistent growth failures have invariably been accompanied by persistent failure to reduce poverty, and that, conversely, sustained and rapid economic growth has invariably been accompanied by reduction of poverty.²

The empirical evidence, however, also points to an important feature of the relationship between growth and poverty that is often neglected – namely, that there is no invariant relationship between the rate of growth and the rate of poverty reduction.

² For recent and comprehensive reviews of this literature, see, among others, Osmani (2001) and Srinivasan (2001).

In other words, faster growth is not always accompanied by faster rate of poverty reduction, just as slower growth does not always entail slower rates of poverty reduction. The reasons for these variations are not yet fully understood. Why is it that rapid growth sometimes entails rapid reduction of poverty but sometimes rather modest rate of poverty reduction? How is it possible that even relatively modest growth sometimes goes hand in hand with relatively rapid reduction of poverty? If the goal of policy-making is to eliminate poverty in the shortest possible time, then it is important to understand what lies behind these variations.

Any attempt to explain the variable relationship between the rate of growth and the rate of poverty reduction must investigate the causal mechanisms, or channels, that link growth with poverty. When poverty is viewed broadly to imply basic capability failures (as opposed to just low income) – such as the capabilities to be free from hunger, to live a healthy and active life, and so on – two basic channels can be identified:

- *The social provisioning channel:* Growth-generated resources are utilised by the society to provide services to the poor so as to enhance their various capabilities.
- *The personal income channel:* Growth of the economy translates into higher personal income of the poor, who then utilise their income so as to enhance their capabilities.

The workings of both the channels are subject to variations. The extent to which growth-generated resources actually get to be utilised for the purpose of social provisioning can vary from society to society. And the extent to which growth of the economy translates into higher income of the poor can also vary. Both types of variations can underlie the observed variable relationship between the rate of growth and the rate of poverty reduction.

A crucial variable that determines the functioning of the personal income channel is employment. It is the quantity and quality of employment of the poor that determines

how growth of the economy would translate into higher income of the poor.³ This might be called the ‘employment nexus’ between growth and poverty. Explicating the nature of this nexus – i. e., understanding what factors make this nexus strong and what makes it weak – is an essential precondition for devising policies that will best serve the poor.

II.2 The Employment Nexus between Growth and Poverty

In order to see how the employment nexus mediates between growth and poverty, it is useful to begin with some taxonomies of the poor based on the nature of their employment.

One basic taxonomy is to distinguish between the poor who are in the labour force and those who are not. Some among the latter group may have no one in the labour force to support them. For them, obviously, the employment nexus is of little relevance; some form of social provisioning will be needed in order to alleviate their poverty. However, most of the poor who are not in the labour force would actually be dependants of the first category of poor, so that their conditions will be inextricably linked with each other. For analytical purposes, therefore, it is adequate to focus only on those among the poor who are in the labour force.

The poor in the labour force can in turn be divided into two groups: the unemployed poor and the working poor. As an empirical reality, it is fair to suggest that the unemployed poor would constitute a numerically insignificant category in the poor countries. The reason simply is that the vast majority of these countries do not have any social insurance mechanism, without which the poor cannot afford to remain unemployed. Thus the working poor would constitute by far the major segment of the poor in the labour force.⁴

³ Employment may be relevant for the social provisioning channel as well, because in some cases a person’s eligibility to claim social provisioning may depend on whether or not he or she has a job – for instance, when free or subsidised health and education services are provided by the employer.

⁴ For a pioneering attempt to estimate the number of the working poor in the developing world, see Majid (2001).

The working poor themselves can be further classified, along two different lines. The more traditional line of classification looks at the relationship between labour and the means of production, and accordingly classifies the working poor into the self-employed poor and the wage-earner poor. A different line of classification would look at the proximate causes of low income that make the working people poor. Two broad categories of proximate causes can be distinguished: *underemployment* and *low returns to labour*.

Those who suffer from *underemployment* can be of two types:

- The *open underemployed*, i.e., those who work less than full time and hence cannot earn enough to rise above the poverty line.
- The *disguised underemployed* i.e., the Nurkse-Lewis type surplus labour – those who apparently work full time but at low intensity, within an institutional framework that permits both work-sharing and income-sharing.⁵

Those who suffer from *low returns to labour* despite working full-time and at high intensity can be classified into three categories depending on the causes of low returns.⁶

- Those who work for very low wages because they have to compete with potential entrants (comprising the unemployed and the underemployed, and constituting a pool of surplus labour) who have very low reservation wages – the *surplus labour* syndrome.
- Those who work with poor skill, or poor technology, or inadequate complementary factors – the *low productivity* syndrome.

⁵ Work-sharing implies that the size of the workforce can be expanded adding little to total production, while income-sharing ensures that the same total output or income is distributed among more workers, thereby reducing everyone's individual income and in the extreme case pulling everyone below the poverty line.

⁶ It should be noted that these are meant to be analytical categories, not empirical categories in which individual workers can be neatly fitted, because in practice a single worker may suffer from more than one reason for low returns to labour.

- Those who suffer from adverse terms of trade, either because of low product prices, or high input cost (including high cost of credit), or both – the *adverse terms of trade* syndrome.

The preceding typologies demonstrate that there are a wide variety of pathways through which a part of the working population can become poor. These typologies thus provide a rich analytical framework for understanding the detailed processes through which different groups of people come to experience poverty. The objective of the present discussion, however, is not to embark on a full-fledged exploration of these detailed processes, but to identify in broad terms the channels through which the employment nexus relates the proximate causes of poverty to what might be called the underlying factors that affect poverty.

As noted above, the proximate causes of poverty are unemployment/underemployment and low returns to labour – in other words, the quantity and quality of employment.⁷ To see what the underlying factors are, one might begin by noting the rather trivial fact that the condition of the poor will depend on their scope of earning higher income –either through greater quantity of employment or through higher returns to labour, or a combination of the two. This scope will obviously depend on factors affecting both the supply of and the demand for labour.

On the supply side, there are long term forces affecting the growth of labour force and there are both long and short term factors affecting the supply of labour of a given labour force. The present analysis will abstract from considerations of the forces that affect the growth of labour force, which means that it will discuss only the factors that affect the incomes of the poor for any given growth of labour force. The factors affecting the supply of labour of a given labour force will, however, be considered.

⁷ Strictly speaking, the quality of employment refers not just to the returns to labour but also to a host of other attributes of work that are subsumed under the notion of labour standards – viz., protection against unfair dismissal, health and safety standards at the work place, the length of the working day, the power of the workers to organise and to bargain collectively with the employers, the scope of the workers to take part in the decision-making processes and so on. In this comprehensive sense, what the workers need is what ILO describes as ‘decent work’. The present analysis, however, abstracts from

On the demand side, too, there are both long-term and short-term forces. The present analysis will abstract from considerations of short-run fluctuations of demand for labour associated with business cycles, which means that the phenomenon of Keynesian unemployment will be left out of discussion. There are a number of reasons for this. First, since the focus of this paper is on the factors affecting the trend of poverty over time, unemployment of structural types is much more relevant for the present purpose than the Keynesian type. Second, as an empirical reality Keynesian unemployment happens to be much less prevalent than structural unemployment in most of the poor countries. Third, the analytics of Keynesian unemployment is quite well advanced in the existing literature, and this paper has nothing to add in this regard. So, if Keynesian unemployment happens to be a significant factor in a particular context, the existing literature can be drawn upon to supplement the framework of analysis presented in this paper.

Subject to these limitations, the ensuing discussion presents a framework for analysing the underlying factors that affect the incomes of the poor, for any given growth of the labour force. Three sets of underlying factors can be identified:

1. *The growth factor*: The rate at which the production potential of the economy expands, as represented by an upward shift of the production possibility frontier.
2. *The elasticity factor*: The extent to which an upward shift of the production possibility frontier enhances the employment potential – the latter being defined as the scope for improving the quality and quantity of employment. In other words, we are concerned here with the elasticity of employment potential with respect to growth in production potential.
3. *The integrability factor*: The extent to which the poor are able to integrate into economic processes so that, when growth occurs and the employment

the broader dimensions of decent work, and focuses exclusively on employment and returns to labour, because a rather different framework of analysis would be needed to address those broader issues.

potential expands, they can take advantage of the greater scope for improving the quality and quantity of employment.

Some brief remarks on each of these underlying factors are in order. The starting point for any programme of sustained poverty reduction must be the expansion of an economy's production potential, as determined by the growth of its labour force, accumulation of human and physical capital, and technological progress. Only such an expansion can create the basis for sustained increase in the incomes of everyone, including the poor. For a while, of course, redistribution of existing income can help alleviate poverty to some extent; and to the extent that this is possible without seriously compromising the growth potential of the economy, redistributive measures should certainly be undertaken. But it is clear that sustained increase in the income of the poor must be underpinned by sustained growth of potential output.⁸

Given any shift in the production potential, the next parameter that has a bearing on the poor's income is the extent to which growth in output expands the scope for improving the quantity and quality of employment – in short, the employment potential. The expansion of employment potential will manifest itself as an upward shift of the marginal value product curve of labour. For the wage labour sector, this is nothing but the standard demand curve for labour. For the self-employed sector, however, the term demand curve does not strictly apply. Even so, the common feature of both cases is that an upward shift of the curve allows the workers to improve the quality and quantity of their employment. Precisely in what way the effect would be split between quality and quantity would depend on the nature of the supply curve of labour. If the supply curve is relatively flat – as in a situation of surplus labour – most of the impact would be felt as greater quantity (as reflected in reduced underemployment for the poor). If the supply curve is steep – as when surplus labour is exhausted or nearly so – most of the impact would be felt as higher quality – as

⁸ Note that we are referring here to the growth of potential, as distinct from actual, output. The reason for this lies in the methodological quest for identifying the underlying *exogenous* factors that determine poverty i.e., the factors that affect poverty but are not themselves affected by it. As we shall see below, the growth of actual output is not an exogenous factor in this sense because it may well depend to some extent on the rate of poverty reduction.

reflected in higher wages in the case of wage-labour and higher returns to labour in the case of the self-employed.⁹

Thus, the greater the expansion of employment potential, the greater the opportunity for reducing underemployment and raising the returns to labour – the two proximate causes of poverty mentioned earlier. The growth elasticity of employment potential is therefore an important intermediate variable that shapes the extent to which the growth of the overall economy translates into higher incomes of the poor.¹⁰

Of course, a high elasticity of employment does not necessarily entail higher incomes of the poor. All it does is to allow the working population as a whole to reduce their unemployment and underemployment and raise their returns to labour. In short, it expands the opportunities, generally. There remains the question, however, whether the poor are able to take this opportunity or whether it is grabbed mainly by the non-poor workers, or even whether the opportunities are seized at all. Much depends on whether the poor possess the necessary attributes that will enable them to integrate fully into the workings of an expanding economy. This is what we have termed the ‘integrability’ factor.

⁹ The latter being defined as the curve that shows, for different amounts of self-employed labour, net value added (after deducting from gross value added the wages paid to hired workers) divided by the amount of self-employed labour.

¹⁰ It should be noted that the notion of elasticity that is being used here is quite different from the standard one that is found in the empirical literature on growth and employment. The standard definition refers to the observed empirical relationship between actual growth of income and actual increase in the quantity of employment (as measured by the number of people employed). This is different from the concept used here on a number of counts. First, our concept relates potential growth with expansion in employment potential defined as a shift in the marginal value product curve of labour. Since, employment potential, as we have seen, is only partly reflected in the quantity of employment, the other part being reflected in the returns to labour, it’s quite possible that a high elasticity in our sense may be associated with little or no expansion in the quantity of employment. Secondly, to the extent that our concept refers to the quantity of employment, it focuses on the intensity-adjusted amount of work rather than the number of workers. Thus, a high elasticity in our sense may well be associated with a reduction in underemployment, without actually showing up as more people being at work. Finally, and perhaps most importantly, our concept looks solely at the demand side of the labour market so as to capture the ability of growth to absorb labour. By contrast, the standard definition, by relating actual growth with actual employment, looks at the net result of the interaction between supply and demand. It is thus a reduced form concept, and as such doesn’t have much analytical content. Consider, for instance, a case where labour force is growing rapidly, and since open unemployment is rare in poor countries, the number of people at work is also growing rapidly. If growth of income happens to be low in this case, the standard definition will reveal a high elasticity, but it will be misleading to interpret it as indicating that growth has been highly labour-absorbing.

The preceding analysis shows that while economic growth is indeed essential for sustained poverty reduction, the rate of poverty reduction also depends crucially on two other parameters – the elasticity factor and the integrability factor. These two factors constitute the core of the employment nexus between growth and poverty reduction. We shall deal with these two factors in greater details below. But first we shall demonstrate the analytical importance of these concepts by showing how they help answer some of the important questions that are often asked in the literature on poverty and growth.

The first question relates to the empirical fact noted earlier that there is no invariant relationship between the rate of growth and the rate of poverty reduction. Why is it that the same rate of growth in per capita income is not always associated with the same rate of poverty reduction? One possibility is that the poverty alleviation effect of redistributive measures or direct employment-creation programmes (such as food-for-work) makes a difference. Our analysis offers an alternative (but not mutually exclusive) hypothesis – namely that the difference is made by variations in the elasticity and the integrability factors that are associated with the growth process. From a policy perspective, it is important to know which hypothesis is empirically the more relevant one.

Another issue that our analysis helps illuminate is especially relevant in an age of increasing globalisation. It is arguable that in a globalising world, the best way for a country to grow fast is to specialise in the sectors in which it has comparative advantage. And, since for a labour-abundant poor economy, such specialisation will necessarily lead to concentration on labour-intensive activities, it can be argued that rapid growth will automatically be accompanied by rapidly rising income of the working poor (leaving aside any transitional problems owing to reallocation of resources). So, why, one might ask, do we have to worry about a special anti-poverty strategy and why not be content with putting in place a growth strategy that is proper for a poor economy in a globalising world?

This question has some merit, but its argument is not altogether convincing. What it claims, in terms of our framework of analysis, is that the growth process in a poor open economy will by its very nature be associated with a high elasticity of

employment potential, which is good for the poor. We shall argue in the following section that this is not always true for all types of poor economies. But even where it is, there remains the question of the integrability factor – are the poor well-equipped to take advantage of the expansion of employment potential? If not, then the mere pursuit of an appropriate growth strategy for a poor open economy will not be enough to make the maximum possible impact on poverty. The fact that in certain cases the appropriate growth strategy for a poor open economy may not even be associated with a high elasticity of employment potential makes this argument even stronger.

These considerations provide the rationale for adopting an approach to poverty reduction that is not single-mindedly obsessed with, but does pay due regard to, the growth factor. This alternative, and in a sense more comprehensive, approach will also pay due regard to the elasticity factor and the integrability factor. Since these last two factors form the core of the employment nexus between growth and poverty reduction, this comprehensive approach may reasonably be described as the employment-focussed strategy for poverty reduction.

It is worth emphasising that the proposed framework is also comprehensive in a somewhat different sense. Although we have described it as an employment-focussed approach, its relevance is not confined merely to those who are currently unemployed and seeking employment opportunities. It is also relevant to those who are currently working but poor and to the new entrants to the labour force. Indeed, one of the strengths of the proposed framework is that a single analytical framework is used to address the concerns of the unemployed (except the Keynesian variety), the working poor, and the new entrants of the labour force. For all these categories of people, the proximate determinants of income are the quantity and quality of employment, which in turn depend on the same three underlying factors – namely, growth, elasticity and integrability.

II.3 The Elements of an Employment-Focussed Strategy of Poverty Reduction

As noted above, by an employment-focussed strategy of poverty reduction, we mean a comprehensive approach that gives serious consideration to all three underlying

factors that have a bearing on the incomes of the poor – namely, the growth factor, the elasticity factor and the integrability factor.

The importance of growth is already well-recognised in the literature. It is obvious that without the growth of production possibilities there can be no sustained expansion in employment potential. The only way employment can be expanded in a stagnant economy is either by depressing the returns to labour or by increasing the rate of underemployment. Neither route is good for the poor. Only a growth-induced shift in the employment potential will enable the poor to enjoy rising income either through reduced unemployment/underemployment or through higher returns to labour. Economic growth is therefore an essential component of any employment-focussed strategy of poverty reduction. The strategies for promoting growth have been discussed extensively and systematically in the literature. By contrast, the discussion of the other two factors, while it exists, is much less extensive and far from systematic. Since these two factors also happen to be the distinctive features of an employment-focussed approach, the following discussion concentrates on them.

The Elasticity Factor

The elasticity factor refers to the ability of any given growth of production to stimulate the growth of employment potential, as represented by upward shift of the marginal value product of labour curve. The idea behind this concept is that any given growth rate can be associated with different degrees of shift in employment potential depending on the nature of the growth process. And the growth process that is associated with a bigger shift – that is, the one that is more employment-elastic – would be more helpful for the poor, other things remaining the same. The degree of elasticity would depend on three features of the growth process:

- *Sectoral composition of output*: The extent to which the growth of output is concentrated in the more labour-intensive sectors.
- *Choice of technique*: The extent to which more labour-intensive techniques are used, especially in the growing sectors.

- *Terms of trade*: The extent to which the internal and external terms of trade improve for the labour-intensive sectors.

One of the main reasons why economic growth did not lead to appreciable reduction of poverty in many developing countries in the past is that the growth process did not promote labour intensity in either the composition of output between sectors or in the choice of technique within sectors. The inward-looking import-substituting strategy of industrialisation followed in these countries had created an incentive structure that fostered capital-intensity of production at the expense of reducing the employment potential. The trend is now changing, and there is greater understanding today about the need for adopting a more outward-looking open economy strategy. In general, this change will not only enhance the ‘growth factor’, but will also impact positively on the ‘elasticity factor’ by promoting greater labour-intensity in labour-abundant poor economies. Both of these will be beneficial for the poor. Therefore, the elimination of policy distortions that create an artificial bias towards capital-intensity in the pursuit of widespread import substitution must form an essential part of an employment-focussed strategy for poverty reduction

It should be noted, however, that abandoning widespread import substitution and opening up the economy will not necessarily enhance the elasticity factor in all circumstances. There are a number of reasons for this.

First, there are many poor countries – for instance, in sub-Saharan Africa – who are land-abundant rather than labour-abundant. The standard Heckscher-Ohlin theory of international trade, which predicts that labour-abundant countries will specialise in labour-intensive products as they open up their economies, also predicts by the same logic that land-abundant countries will specialise in land-intensive activities – crop production, for example. The impact on employment potential will then depend crucially on the institutional arrangements that govern labour’s access to land. If, for instance, land distribution happens to be highly unequal and production is dominated by a few large owners cultivating large tracts of land through mechanised means, then the impact on employment-elasticity might be small.

Second, the predictions of the simple version of the Heckscher-Ohlin theorem may not hold when complications arising from the presence of multiple goods and in particular, non-traded goods, are introduced. Thus, even in a labour-abundant economy, if the labour-intensive products require complementary non-traded inputs that are scarce in supply, then comparative advantage may not actually lie in these products. Opening up the economy will not then necessarily impact positively on the elasticity factor.¹¹

Third, poor infrastructure – both physical and human – may inhibit the expansion of labour-intensive activities, even if they happen to have potential comparative advantage. This is especially likely if the existing infrastructure was geared specifically towards supporting capital-intensive activities that were promoted artificially in an earlier regime of import substitution. The recognition that infrastructural bottlenecks seriously inhibit the expansion of sectors that have a potential comparative advantage is a common theme in the literature on underdevelopment in sub-Saharan Africa.

These are some of the reasons why greater labour-intensity of production is not guaranteed merely by the opening up of a poor economy. An employment-focussed strategy of poverty reduction would then demand that, simultaneously with the opening up, other measures are taken to overcome the bottlenecks that might inhibit labour-intensity in particular circumstances.

Apart from labour-intensity of production, the other factor that affects the employment potential is the terms of trade. Higher terms of trade will raise the marginal value product of labour, and thereby create greater opportunities for increasing the quality and quantity of employment. Much of the woes in sub-Saharan Africa in the recent decades stems from the fact that the primary commodities in which it has comparative advantage are experiencing sharp and sustained reduction in their terms of trade. This makes it difficult for the working poor engaged in the production of these commodities to raise their income either through greater employment or through higher returns to labour.

¹¹ For evidence on the diverse effects of trade liberalisation on manufacturing employment, see Ghose (2000).

Internal – that is to say, inter-sectoral - terms of trade may also be important. The experience of China in the post-reform period is especially relevant here. China has maintained a very high growth rate ever since it launched market-oriented reforms in the late '70s, but its record of poverty reduction has varied enormously. Rural poverty was reduced sharply in the period immediately following the reforms, but since the mid-1980s there has been very little reduction (and probably even some increase in poverty for a while) despite rapid growth. This asymmetrical performance has much to do with the behaviour of the terms of trade of farm products, in the production of which the majority of China's rural poor are employed. The terms of trade increased sharply up to the mid-1980s, and fell sharply thereafter. The rate of poverty reduction followed the same pattern, while rapid growth of the overall economy continued unabated (Khan and Riskin 2001).

The Integrability Factor

Rapid growth and high elasticity of the employment potential can together ensure that economic activities create greater opportunities for workers to increase their income through a combination of greater employment and higher returns to labour. However, workers do not necessarily mean 'poor workers', and opportunities are not necessarily seized. So, even a combination of rapid growth and high elasticity does not guarantee a rapid rate of poverty reduction. If the new opportunities are such that the capabilities they demand do not match the capabilities of the poor, then either non-poor workers will seize the opportunities or perhaps the opportunities will not be seized at all. Much, therefore, depends on the correspondence between the structure of opportunities that are opened up and the structure of capabilities possessed by the poor. The integrability factor refers to the degree of this correspondence. The greater the degree of correspondence, the more extensively will the poor be able to integrate into the processes of economic expansion and the faster will be the rate of poverty reduction for any given rate of growth.

There are a variety of reasons, however, why the poor may not be able to integrate fully into economic processes so as to take advantage of any expansion in employment potential created by economic growth.

One extreme case is illustrated by some recent nutrition-based theories of unemployment and underemployment. The problem stems from the physiological fact that every individual has to incur a 'fixed cost' of energy expenditure simply to maintain the body (at rest) before incurring any additional energy expenditure for doing physical work. For an individual who does not have an alternative means of meeting the fixed cost – for example, an assetless labourer – the energy value of the returns to labour will have to be large enough to cover both the fixed cost and the variable cost associated with work. The sum of fixed and variable energy costs will then represent his reservation wage, below which she would not work. However, those with some asset income might be willing to work for a lower wage, since a part of the fixed cost will be met by other means. As a result, in a competitive labour market, the assetless labourers will be priced out by those who have some assets and will suffer from unemployment (Dasgupta 1993). By the same token, those who have fewer assets may be priced out by those who have more. To put it differently, the poorest among the poor may not be able to integrate into economic processes because of competition from the less poor, or perhaps the non-poor as well, even in the face of an overall expansion in the employment potential.

The lack of integrability may also result from market failures, especially the failure of the credit market. It is well-known that because of informational asymmetries the formal credit market often tends to resort to credit rationing in such a way that the poor, because of their lack of assets, are left out or are at least severely discriminated against. The poor entrepreneurs are then compelled to turn to monopolistic informal moneylenders. But the exorbitant rates of interest they charge may render it impossible to expand the business even if there is an overall expansion of economic opportunities. Similarly, poor infrastructure, lack of information, market thinness, and other problems of living in remote areas may make the transaction costs so prohibitive that the poor entrepreneurs of those areas may not find it worthwhile to expand

business or to undertake new business activities even if new opportunities open up in the overall economy.¹²

Labour market institutions may also play an important role by creating an insider-outsider problem. Certain types of labour laws and practices of collective bargaining may create such an asymmetry of power between insiders (i.e., those already employed in the organised sector) and outsiders (i.e., those seeking entry into the organised sector) that the insiders may be able to effectively prevent the outsiders from gaining entry (Lindbeck and Snower 1989). In that case, the outsiders will find it hard to integrate into the mainstream of economic expansion. The benefit of expansion will then accrue largely to the insiders in the form of higher returns to labour, leaving little direct benefit for the outsiders. To the extent that the outsiders are likely to be poorer than the insiders, this will be detrimental to the cause of poverty reduction.¹³

Another source of limited integrability lies in a possible mismatch of skills – between the skills demanded by the expanding sectors and the skills possessed by the poor. A case in point is the current experience of many Latin American countries. As these countries try to open up their economies, they find that, unlike the countries in East and South East Asia which had opened up their economies earlier, their comparative advantage does not lie in the activities that are intensive in relatively unskilled labour. The emergence of the poor and populous countries such as China and India on the global scene has ensured that Latin America would not be able to compete in these types of products. Instead, it is in the relatively skill-intensive activities that most of the Latin American countries find their comparative advantage (Wood 1997). The opening up of these economies has therefore led predictably to an expansion of these

¹² It is conceivable that in both cases of market failure mentioned above – viz., credit market imperfections and high transaction costs of living in remote areas – poor entrepreneurs will find it worthwhile to expand business provided the shift in the marginal value productivity curve of labour is sufficiently large to offset the additional costs. This implies the existence of a threshold effect – that is to say, integrability will remain a problem unless the expansion in employment potential is large enough to cross a minimum threshold.

¹³ It must be noted, however, that if the incentives provided to the insiders can be designed so as to increase their productivity – for example, by paying them efficiency wages or by improving their working environment – then the spill-over effect of higher productivity may indirectly benefit the poor outsiders. These indirect benefits must be weighed against the direct cost to the outsiders when considering the desirability of labour laws and practices that strengthen the hand of the insiders.

skill-intensive activities, but the poor have benefited little from this expansion so far, as they do not possess the skills that are needed by the expanding sectors.¹⁴

A rather different kind of mismatch relates to the gender dimension of the integrability problem. The types of jobs for which demand rises may be culturally defined as men's jobs, whereas poverty may be concentrated mostly among women. This problem is especially relevant in much of Africa, where crop production has acquired a gendered pattern – with many cash crops being identified as men's crops and subsistence food crops being identified as women's crops. Trade liberalisation and greater commercialisation of agriculture may boost the employment potential in cash crop production, but to the extent that gendered pattern of crop production remains a constraint, poor women will find it hard to take advantage of the new opportunities.

Yet another problem that creates difficulty for women in their efforts to integrate into economic processes is the time constraint. Poor labour-abundant economic may have a comparative advantage in labour-intensive activities, and if market distortions are removed then such activities may indeed flourish, but many poor women may not be able to take advantage of these opportunities. There is a direct conflict between the demands of labour-intensive activities and the severe time constraint faced by poor women as they try to combine productive and reproductive activities within the household.

III. SUGGESTED TOPICS FOR ILO/UNDP REPORTS ON EMPLOYMENT AND POVERTY

The conceptual framework presented in the preceding section can be used to derive a number of ideas that can be explored at length in the proposed ILO/UNDP reports on employment and poverty. Three important topics are discussed briefly below:

¹⁴ The resulting phenomenon of widening wage differentials between skilled and unskilled workers has

1. Reducing Poverty through the Employment Nexus.
2. Globalisation and Poverty: An Exploration of the Employment Nexus.
3. Enabling the Poor to Integrate into the Growth Process.

III.1 Reducing Poverty through the Employment Nexus

The primary objective of the proposed Reports is to explore the various links between employment and poverty and to suggest policy measures that can strengthen these links. It would therefore make sense for the very first Report to provide a rationale for focussing on employment as the crucial nexus between growth and poverty. For this purpose, first a conceptual framework will have to be developed linking growth with poverty through the employment nexus, perhaps building on the kind of discussion presented in section II above. But, in addition, empirical analysis will have to be undertaken so as to demonstrate the practical value of adopting an employment-focussed approach.

Since the issues involved in developing the conceptual framework have already been discussed at some length in section II, I need only summarise some of the major points here.

- The concept of the working poor can be taken as useful starting point, by noting that even the poor who are actually unemployed are usually facing frictional unemployment in most poor countries so that they too may be considered working poor from a longer term perspective.
- The two proximate causes of poverty of the working poor are underemployment and low returns to labour. Therefore, the objective of any poverty reduction strategy must be either to reduce underemployment or improve the returns to labour or achieve a combination of the two.
- The strategies needed for addressing the two proximate causes are not different, however. An improvement in the employment potential, as

been analysed by Behrman *et al.* (2000).

represented by an upward shift of the marginal value product curve of labour, will help address both causes.

- The extent to which the employment potential improves depends on the one hand on the expansion of an economy's production possibilities (growth, for short), and on the other hand on the extent to which the employment potential responds to any given expansion in economic activities (elasticity, for short).
- Once the employment potential expands, the extent to which the poor will benefit (by reducing underemployment and/or raising the returns to labour) depends on the capabilities of the poor to integrate into the expanding sectors of the economy (integrability, for short).
- Thus the rate of poverty reduction depends on three underlying factors: growth, elasticity and integrability. The currently fashionable growth-oriented strategy of poverty reduction tends to focus on the first factor to the relative neglect of the other two. By contrast, an employment-focussed strategy will be concerned with all three, with the last two factors – namely, elasticity and integrability – being the distinctive features of this approach. As such, an employment-focussed strategy will be more comprehensive than a growth-oriented strategy, and to that extent superior.

Having made the theoretical case for adopting the employment-focussed strategy of poverty reduction, the Report should then proceed to demonstrate its practical usefulness. There are many alternative ways of doing this, but one that appeals to me most is to use the concept of the employment nexus to explain the empirical fact that there is no invariant relationship between the rate of economic growth and the rate of poverty reduction. It can be argued that the reason for the variable relationship can best be understood by noting the role played by elasticity and integrability – the two distinctive features of the employment nexus. If elasticity and integrability are high, then even modest growth can be associated with a rapid rate of poverty reduction. By contrast, if elasticity and integrability are low, then even a high rate of growth may be associated with slow progress in poverty reduction.

An empirically interesting way of making this point is to identify different experiences of growth and poverty from the recent history of the developing world, and then to demonstrate that these differing experiences can be explained in a large measure by invoking the notions of elasticity and integrability. Four different kinds of growth-poverty episodes may be identified, referring to specific countries during specific periods of time:

- A. Rapid growth with rapid poverty reduction.
- B. Rapid growth with slow poverty reduction.
- C. Slow growth with rapid poverty reduction.
- D. Slow growth with slow poverty reduction.

The objective of the exercise will be to demonstrate that the difference between episodes A and B was that elasticity and integrability were more favourable in A than in B. Similarly for the difference between C and D.

It is not being proposed here that attempts should be made to actually quantify elasticity and integrability as specific numbers. Whether such quantification is at all possible is itself a moot issue, but the relevant point is that quantification is not necessary for the purpose at hand. Rather these concepts should be used as analytical devices with which to explore systematically certain related empirical phenomena. Thus in the context of elasticity, the task is to study the production structure in order to ascertain what has happened to labour intensity of production and the terms of trade – the prime determinants of elasticity. In the case of integrability, the task is to explore the barriers that the working poor might face when trying to integrate into the processes of economic expansion.

If these empirical studies can demonstrate that the success in poverty reduction depends not just on growth but also on the forces that determine elasticity and integrability, this will form a sound basis for arguing the case for an employment-focussed strategy for poverty reduction.

III.2 Globalisation and Poverty: An Exploration of the Employment Nexus

Whether globalisation helps or hurts the poor is one of the most contentious economic and political issues of modern times. Part of the reason for continued disagreement lies in the very notion of globalisation, which has many dimensions – some economic, some political, some technological, and some cultural – and as such may mean different things to different people. But even when the term is defined narrowly to mean increasing economic integration among countries brought about by trade liberalisation, technology transfer and greater capital mobility, arguments continue to persist. There are those who argue that globalisation is contributing to increasing economic disparities in the world by allowing some countries and some segments of the population to become ever richer while marginalising the poorer countries and the poorer population groups. They tend to blame globalisation itself for deepening poverty in parts of the world. Others contend that if some countries and some population groups have failed to benefit from globalisation, the fault lies not in globalisation itself but in the fact that they have not actually embraced globalisation as fully as the rest of the world.¹⁵

Whether one likes it or not, globalisation has come to stay. So it is important to understand the processes through which the forces of globalisation affect the poor and, if the effects are not always good, to identify appropriate policy measures that can make globalisation work better for the poor. It is argued here that the conceptual apparatus underlying the employment-focused strategy of poverty reduction can help illuminate the current debate and in the process clarify the true nature of the impact of globalisation on poverty. It will therefore be most appropriate to devote an ILO/UNDP Report on this theme.

Those who claim that globalisation will help the poor in developing countries typically rely on the argument that the forces of globalisation will help promote growth as well as labour-intensity in labour-abundant developing countries, both of which should be beneficial for the poor. The inference they draw from this argument

¹⁵ For accessible presentation of the some of the arguments in this debate, see DFID (2000) and World Bank (2002).

is that if the poor are not actually gaining, it must be because globalisation has not gone far enough.

While the hypothesis that globalisation has not gone far enough is a plausible one, this is not the only plausible explanation of why the poor in some parts of the world might fail to benefit from globalisation. In terms of the conceptual framework proposed in this paper, it may be argued that while globalisation may help the growth factor, the benefits may fail to accrue to the poor because of unfavourable elasticity and integrability factors.

The proponents of globalisation tend to argue, of course, that by forcing open the erstwhile closed economies globalisation will move the economic structure of developing countries towards more labour-intensive methods of production. If true, this will ensure that globalisation will improve the elasticity factor as well as growth. But as we have argued in section II, it is by no means certain that opening up of the economy will bring about greater labour intensity. There are a number of reasons for this. In the first place, while labour-abundant countries are indeed likely to move towards greater labour intensity, not all developing countries are labour-abundant; some are more properly described as land-abundant. Secondly, the scarcity of complementary non-traded inputs may lead to a situation where even a labour-abundant economy may not be able to move towards greater labour-intensity. Besides, infrastructural bottlenecks and adverse movements in the terms of trade may inhibit the translation of potential increase in labour-intensity into an actual increase.

For all these reasons, it is by no means assured that the process of globalisation will automatically enhance the elasticity factor in developing countries. Then there remains the further problem that the poor might face difficult integrability problems in gaining from the new opportunities opened up by globalisation. Thus, if globalisation has failed to benefit the poor in certain circumstances, it may in theory have happened for any of the following three reasons:

1. Globalisation did not proceed far enough.
2. Globalisation was accompanied by a worsening of the elasticity factor.

3. The integrability problem prevented the poor from enjoying the benefits of globalisation.

This way of looking at the relationship between globalisation and poverty will help conduct the debate on globalisation along more rational lines. The proponents of globalisation who recognise that poverty has not declined everywhere in the wake of globalisation tend to emphasise the first possibility. But clearly the other two explanations are also possible. The opponents blame globalisation itself for the perpetuation of poverty. But they too need to recognise that the fault probably lies in the failure to improve elasticity and integrability and that if these factors can be improved, perhaps globalisation will be good for the poor after all.

It is, therefore, essential to determine which of the three possibilities (which are not mutually exclusive, however) is actually driving the relationship between globalisation and poverty. This is essentially an empirical matter, and different forces might operate in different situations. It is this empirical analysis that I am proposing that one of the ILO/UNDP Reports should undertake.

After explicating the theoretical basis of the three alternative hypotheses mentioned above, the Report should proceed to identify a number of countries and/or regions in which globalisation has failed to reduce poverty. Through an in-depth analysis of the economic conditions of those countries/regions, the Report should come out with an assessment of what were the really constraining factors in specific circumstances. Policy recommendations can then follow from this analysis.

In order to place the policy recommendations on sounder footing, it would be useful to carry out a parallel analysis of another set of countries/regions in which globalisation has actually been accompanied by rapid poverty reduction. Once again, the experience of this set should be analysed in the light of three alternative hypotheses, which are actually the converse of the ones mentioned above – namely, (1) globalisation was extensive, (2) elasticity was high, and (3) integrability was high. An understanding of how these countries/regions actually managed to render globalisation a friend of the poor will help to guide the policy formulation of those who failed to do so.

III.3 Enabling the Poor to Integrate into the Growth Process

This paper has argued that the main rationale for adopting an employment-focussed strategy of poverty reduction is that rapid growth is no guarantee of rapid poverty reduction. While rapid growth, if sustained over a period of time, will almost certainly help reduce poverty, the rate at which poverty will be reduced depends not just on the rate of growth but also on the barriers faced by the poor while trying to integrate into the expanding activities – i.e., the integrability factor. One of the ILO/UNDP Reports could aim to provide a fairly comprehensive empirical understanding of the nature of the integrability problem as it exists in different parts of the developing world.

The importance of this problem in the context of poverty reduction cannot be overemphasized. We have already argued that the extent to which economic growth will contribute to poverty reduction depends a great deal on the degree of integrability of the poor. It is also important to emphasise that this factor may have a bearing on the rate of growth itself.

To consider just one possibility, suppose a labour-abundant country opens up its economy, thereby creating an opportunity for moving the production structure towards greater labour-intensity. But also suppose, not unrealistically, that the new labour-intensive activities require a certain minimum level of skills that are not in plentiful supply (because of, say, lack of education or health on the part of the poor) – a case of limited integrability. Producers will then be forced to switch to activities that require fewer workers with perhaps greater skill. And if the structure of the society is such that it allows a small number of well-educated and well-nourished workers to exist side by side with a large number of uneducated and malnourished ones, then the producers will have no difficulty in doing so. But this is a second best option since such activities would rank below the most labour-intensive activities in the scale of comparative advantage. As a result of adopting the second-best option, however, economic efficiency will be sacrificed, and to that extent growth will fall short of its potential. Limited integrability can thus inhibit poverty reduction twice – by limiting

the poverty-reducing impact of any given rate of growth and by reducing the rate of growth itself.¹⁶

Despite its undoubted importance, it is fair to say that of the three underlying factors that affect poverty – viz. growth, elasticity, and integrability – it is the last that is understood the least. It is not that we do not understand in theory what kind of barriers could stand in the way of the poor benefiting from growth. In fact, a number of possible barriers were listed in section II – for example, a nutrition-based barrier, the insider-outsider problem, market failures of various kinds, mismatch of skills, cultural stereotyping of occupations, women’s struggle to combine productive and reproductive activities, and so on. The point rather is the empirical one that we do not have sufficient understanding of which of the barriers act as the major constraint in different parts of the developing world. Since policies cannot possibly deal adequately with all the problems at the same time, it is necessary for the sake of efficient policy formulation to identify the constraints that dominate in particular circumstances. This Report should endeavour to provide this kind of detailed empirical knowledge for different countries/regions of the developing world.

In addition, the Report should also undertake a comparative analysis of how some countries/regions have been able to improve the integrability factor more successfully than others.

IV. SUGGESTED TOPICS FOR RESEARCH

It is evident from the preceding discussion of possible topics for future ILO/UNDP Reports on Employment and Poverty that it will be necessary to undertake a great deal of new research in order to inform those Reports. While the proposed research programme may eventually aim to have a wider perspective than that demanded by the Reports, it might be rational to concentrate the early efforts on the type of research that will best support the Reports. Based on this consideration, I would suggest the following research topics for immediate attention.

¹⁶ It is for this reason that the actual, as distinct from potential, rate of growth was described as an endogenous variable earlier in the paper.

IV.1 Growth and Poverty Reduction: Explaining the Variety of Experience

The focal point of this research topic is the empirical observation that there is no invariant relationship between the rate of growth and the rate of poverty reduction. Rapid growth can be associated with both rapid and slow rates of poverty reduction, just as slow growth can be associated with both slow and at least moderate if not rapid rate of poverty reduction.¹⁷ The research question is: what lies behind this variable relationship?

Two general types of hypothesis can be advanced as explanation. The first hypothesis is that differential emphasis on targeted anti-poverty programmes explains the variable relationship between the rate of growth and the rate of poverty reduction. It is indeed conceivable that if anti-poverty programmes such as direct redistribution of food or cash and special employment creation programmes for the poor are undertaken on a large enough scale, then even slow or moderate growth can go hand in hand with rapid rate of poverty reduction, at least for a while.

The second hypothesis rests on the idea of the employment nexus explored in this paper. This hypothesis suggests that any given rate of growth can have variable impact on the rate of poverty reduction depending on variation in the elasticity and integrability factors. For any given rate of growth, what determines the rate of poverty reduction is the degree to which the employment potential responds to economic growth (elasticity) and the extent to which the poor are equipped to integrate into the expanding activities (integrability). Thus, according to this hypothesis, the explanation for the variable relationship between the rates of growth and poverty reduction lies in the nature of the growth process itself, as determined by the whole gamut of economic policies and the structural features of the economy, not just in a few targeted actions directed towards the poor.

¹⁷ The variety of experience from around the developing world has recently been analysed by Khan (2001).

The objective of this undertaking research is to ascertain, in the first instance, which of these alternative hypotheses best explains the empirical facts. To the extent that the second hypothesis is found to have some explanatory power, the next objective would be to assess the relative importance of elasticity and integrability factors. Some general policy conclusions will then be drawn on the basis of the findings of empirical research.

IV.2 Globalisation and the Poor

While closer integration with the world economy has been accompanied by rapid reduction of poverty in some developing countries (e.g., in parts of Asia), it is also true that the experience has been quite different in other countries (e.g., in parts of Africa and Latin America), where poverty has not declined and may even have increased. The experience of the latter group of countries has helped foster the view in some circles that globalisation marginalises the poorest economies of the world and increases the vulnerability of the poor. This view is hotly contested by most economists, whose theory predicts that globalisation should generally be a favourable force for the poor. An important research agenda is to disentangle the arguments involved in this debate and to confront the competing arguments with empirical facts.

Part of the problem in disentangling the arguments lies in the fact that globalisation means different things to different people. There is also the methodological problem that while appealing to empirical evidence care is not always taken to isolate the impact of globalisation from that of extraneous factors such as civil wars, natural disasters, temporary disorders in the world economy, and so on. But even after these problems are taken care of, there remains scope for offering alternative interpretations of the observed relationship between globalisation and poverty. For instance, where increasing integration with the world economy has not been associated with significant reduction of poverty (even after controlling for extraneous factors), three alternative hypotheses can be advanced to explain the phenomenon:

- Globalisation has not proceeded far enough.
- Globalisation has unleashed forces that are not favourable to the poor.

- The poor have not been able to take advantage of the opportunities opened up by the forces of globalisation.

Obviously, the policy implications of these alternative hypotheses are radically different from each other. Yet, in much of the current debate on globalisation strong policy conclusions are made without first trying to ascertain which hypothesis actually holds in a particular situation. The objective of the proposed research agenda is to test empirically the validity of the alternative hypothesis, recognising that different hypotheses might hold under different circumstances.

For testing the first hypothesis, it will be necessary to use some indicators to measure the degree of globalisation for individual countries. A number of such indicators have already been devised by other researchers. A decision will have to be taken on whether to use them as they are or to improve them further.

The second hypothesis suggests that globalisation has worsened or at least not improved the employment potential for the poor – i.e. the impact on elasticity has not been favourable. Testing this hypothesis will involve investigation of the impact of globalisation on labour-intensity of production and the terms of trade.

The third hypothesis focuses on the integrability factor. Testing of this hypothesis will require investigation of the attributes and capabilities of the poor where globalisation has failed to make a dent on poverty and then assessing the degree of correspondence between these capabilities and the opportunities opened up by globalisation.

IV.3 The Barriers to Integration: Why Can't the Poor Always Benefit Fully from Growth?

The conceptual framework developed in this paper to explicate the nature of the employment nexus between growth and poverty has emphasized the importance of the integrability factor as a determinant of poverty reduction. Not much is known, however, about the precise nature of the problem in different countries/regions of the world. While it is easy to provide a list of barriers that the poor typically face in trying

to integrate with the growth process, efficient policy-making demands that the policy-makers are aware of the major barriers that act as the binding constraint in particular circumstances. The objective of this research programme is to provide this information for policy-makers in different countries/regions of the developing world.

This is admittedly an ambitious task but well worth pursuing. Since integrability depends on the degree of correspondence between the structure of opportunities on the one hand and the structure of capabilities of the poor on the other, this task is informationally very demanding. Macro and meso-level knowledge on the structure of production and the associated employment potential will have to be combined with micro-level information on the attributes and capabilities of the poor.

For the micro-level information on the poor, the Report will have to rely on various household-level surveys of income, expenditure and employment. Fortunately, many household-level surveys of national coverage already exist in different parts of the world, thanks largely to the efforts of the UNDP and the World Bank. Many more surveys of more limited (and yet representative) coverage also exist – for example, those conducted by the International Food Policy Research Institute and the International Rice Research Institute as well as by various national research institutions. The research project will have to draw upon this rich source of information as much as possible.

The immediate objective of the exercise will be to clarify the empirical picture regarding the binding constraints on integrability in different parts of the developing world. In identifying these constraints, the research programme should pay special attention to the constraints faced by poor women. Cultural stereotyping of occupations, time constraint imposed by the burden of combining productive and reproductive activities, and discrimination in various spheres of life render the integrability problem especially severe for poor women.¹⁸

The other, related, objective would be to study how some countries have been able to improve the integrability factor more successfully than others and to draw policy

¹⁸ The specific disadvantages faced by poor women are discussed, among others, by DAW/UN (1999, 2001) and World Bank (2001).

lessons from this comparative analysis. As an example of such comparative analysis, reference is often made to the greater success of the East Asian and South East Asian economies in improving the education and health status of their people relative to the rest of the developing world.¹⁹ These experiences confirm that the emphasis on human development given in recent years by UNDP and others is justified not only because human development is a worthy goal in itself but also because it can play an important instrumental role in promoting improvements in material living standards. However, as noted in section II, education and health are not the only variables that have a bearing on the integrability factor. There are many more, but very little is known about the comparative success in dealing with them. A more comprehensive analysis will help identify the strategic policy interventions that might be fruitfully employed in the less successful countries/regions. This type of knowledge is essential for making the employment nexus an effective tool for poverty reduction.

¹⁹ For a recent review of the Asian experience from the employment perspective, see Islam (2001).

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