Social Protection Is a Necessity, Not a Privilege

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Real people’s livelihoods and families are at the receiving end of the chain of shocks that have rocked the globe during the recent economic crisis. Many are now questioning the effectiveness of unfettered free markets to deliver sustained and broad-based economic opportunity and prosperity—not least because they have experienced economic crises before. The debt crisis in Latin America in the 1980s and the Asian financial crisis in the late 1990s raised important questions about the efficacy of market mechanisms left to their own devices. And yet here the world is again.

The Great Recession, like past crises, highlights deficiencies in the social protection systems that are, or should be, in place to promote broad-based economic growth and to help citizens cope with economic hardship. Strengthening or sometimes setting up these social protection systems (see box) is now more important than ever.

Public spending serves an important function in pursuing economic growth objectives while ensuring that the gains are widely distributed to promote broad-based increases in living standards. Effective government social protection systems have a critical role to play in ensuring the well-being of its citizens.

What constitutes a safety net?

The definitions and terminology used in discussions of protection are as wide as the concept itself. Broadly defined, social protection systems are government policies, programs, and regulations that enable “societies to advance the well-being and security of their citizens by protecting them from vulnerability and deprivation so that they can pursue a decent life.”

A joint publication by the International Labor Office and the International Social Security Association uses a more specific definition describing social protection as consisting of

…all income transfers (or benefits) in kind and in cash that a society affords to its individual members in order to:

• Avoid or alleviate poverty
• Assist them in coping with a series of life contingencies or risks such as unemployment or illness which, if they occurred, might otherwise lead to a loss of income
• Reduce or correct inequalities created through the primary (pre-transfer) income distribution

Unemployment insurance as well as financial support for education, health care, disability, and retirement pensions are all examples of social protection.
For these reasons, setting up social protection systems was stated as one of the top priorities of the heads of government who make up the Group of 20 leading developed and developing nations, as well as the other key international groups such as the Group of 8 industrialized democracies and the G8+5 (see box). The G8+5 leaders were perhaps the most explicit at their most recent summit in 2009 in L’Aquila, Italy, where they stated:

*Concerned by the high social costs of the crisis in terms of unemployment and poverty, we are committed to tackle the social dimension of the crisis, putting people’s concerns first. We are modernising, reinforcing and increasing the efficiency of social protection policies, including safety nets, health and education. Strengthened and sustainable social protection, supporting employment and enhancing skills, will also help to sustain and rebalance global demand.*

But the G20 is now the primary institution for global governance, and it must make social protection a priority in its actions, not just in words, especially at a time when several countries face pressures for fiscal consolidation. The G20 evolved from a meeting of finance ministers and central bank governors to a meeting of the heads of state from G20 countries in the fall of 2008 to jointly deal with the shock waves emanating from the U.S. subprime mortgage crisis and the ensuing global financial crisis. At the G20 summit in Pittsburgh in the fall of 2009, the leaders declared that their governments would “continue to provide income, social protection, and training support for the unemployed and those most at risk of unemployment.”

### The global groups

**Group of 20:** The G20 consists of the heads of state, finance ministers, and central bank governors from 20 leading economies that together comprise about 90 percent of global gross national product and two thirds of the world population. The members are the United States, the European Union, Japan, Canada, China, Russia, India, Mexico, Argentina, Brazil, South Korea, Saudi Arabia, Indonesia, Turkey, and Australia.

**Group of 8:** The G8 consists of the eight heads of governments from Canada, France, Germany, Italy, Japan, Russia, the United Kingdom, and the United States.

**Group of 8+5:** The G8+5 consists of the heads of state from the G8 nations plus the heads of state of the five leading emerging economies—Brazil, China, India, Mexico, and South Africa.
While G20 leaders at the summit in Seoul in November this year agreed in their communiqué to “put jobs at the heart of the recovery, to provide social protection, decent work and ensure accelerated growth in low income countries,” the communiqué is thin on laying out a plan of action beyond this statement. There has been little progress on these goals since the early G20 leader’s summits, and as the world economy has slowly started to recover, countries are casting coordination aside to solidify their own recovery and rebuild their own economies at the expense of jointly fostering global demand by focusing on just job creation.

Sustained, broad-based economic growth continues to elude several developed and developing economies alike, even as the global recession is slowly receding. New policies for fiscal consolidation threaten existing social systems, let alone support new ones. But it is imperative that the world’s leaders move beyond rhetoric to action. The G20 leadership must ensure that:

• All national governments make social protection systems a priority.
• All donors should provide technical and financial assistance to help the developing world establish these social protection institutions.
• All multilateral development institutions such as the International Labor Organization, the World Bank, and regional multilateral development banks coordinate their efforts to achieve maximum and lasting impact in the establishment of these social protection systems.

Social protection systems are fundamental to stabilizing and rebalancing national economies as well as the global economy in the wake of the economic crises. These systems facilitate economic and social adjustments to smooth out the ups and downs of business cycles and provide a means of ensuring that the benefits of growth are widely distributed to achieve rising living standards. Widely enacted social protection systems can raise living standards in countries around the world, contribute to stimulating economic growth during downturns, and expand the global middle class to fuel and rebalance global consumption. Social protection systems help to reduce poverty, inequality, and exclusion, and thus strengthen the social contract between national governments and society, reinforcing social cohesion and global stability.

The absence of adequate social protections both prolongs the pain of economic crises and makes economic recovery more difficult. The Great Recession, for example, resulted in global unemployment of nearly 212 million in 2009.4 Such a stunningly high unemployment rate poses a serious problem in developed...
countries. In the United States for example, workers significantly tightened their belts as they lost their jobs, their incomes, and their employment-based health care, which sent shock waves through a global economy that had become highly dependent on American consumption to fuel world economic demand.

This contraction in the United States as well as in other developed nations highlights the importance of rebalancing the global economy in a way that reinforces domestic consumption instead of relying on export-led growth, particularly in key emerging markets such as China and India. A recent analysis by the Center for American Progress encapsulates the importance of this rebalancing to restore global economic prosperity:

Expanding the social safety net will directly tackle the primary cause of high savings rate in China and spur domestic consumption, which would offset export declines in the short term and generate sustainable, balanced growth in the long term. For China, the massive 850 million yuan healthcare plan, alongside better labor practices and pension plans, and more available public goods together constitute a significant step toward establishing the necessary services that Chinese citizens would need to stop stowing away contingency savings at such high rates.5

But consumption is difficult to boost in China, where most economists estimate that the savings rate is at roughly 50 percent of gross domestic product.6 Such high savings rates stem primarily from the fact that Chinese citizens need to plan for health-related contingencies in the absence of an adequate social protection system.

What’s more, the Great Recession adversely affected the export-oriented sectors of developing countries’ economies, adding to unemployment and informal employment as formal employment waned, mostly in manufacturing.7 Estimates suggest that the most recent global economic crisis will raise the number of people living below $1.25 a day by 50 million.8

National leaders’ attention to the merits of social protection systems in rebalancing the global economy has diminished as the painful effects of an economic crisis start to abate for some, and as news coverage shifts to different subjects such as fiscal consolidation. Sustainable reforms are unfortunately frequently the loser when the long-term benefits of establishing social protection systems meet the short-term political needs of ribbons to cut and elections to win. The exception that proves the rule is the effort and strife to enact comprehensive health care reform in the United States.
This policy brief highlights the benefits and indeed the necessity of social protection. It is a call to the international community and national governments to keep the focus on establishing adequate, effective, and efficient social protection systems for countries around the world. It makes the economic case for enacting worldwide social protection systems and then presents some specific policy recommendations to achieve this critical goal.
The economic case for social protection systems

The International Labor Organization, or ILO, in a paper presented to its November 2005 Governing Body, lays out several conduits through which efficient and reliable social protection systems promote economic growth. The ILO report’s key finding is "the view that there is an inevitable trade-off between the levels of social protection and economic growth is most likely wrong, as the world’s most productive economies tend to have strong social protection systems." The ILO subsequently examined this key link between social protection systems and economic growth (see Figure 1).

Social protection systems underpin society’s productive capabilities by investing in people in a way that allows them contribute to the economy and propel economic growth. They are a mechanism for ensuring that the gains from growth are widely distributed among the population through government programs. These programs then help raise productivity, further contributing to economic growth.

The provision of health care and occupational safety standards, for example, facilitate greater efficiency and production. Health insurance can help remove seriously ill and thus unproductive workers from the labor force and at the same time ensure that they are able to continue to consume, while creating employment opportunities for more productive workers. Health care also prevents individuals from becoming sick or unproductive. And worker safety standards ensure productive workers are not driven from their jobs due to workplace accidents, and if they are, that there is disability insurance or assistance available.

Long-term investment in human capital—through education and worker training for example—also plays an important role in maximizing worker productivity and income growth. Education is a tool that allows one to participate in higher value-added activities. Training allows workers to meet the demands of the labor market and retraining allows one to stay current and adjust to changing labor market needs.
The lack of social protection systems conversely leads to deteriorating human capital, particularly in an economic crisis. Without these systems, the health of workforces declines markedly, children are pulled out of school to make up for lost family income, and free community resources that are available are quickly overwhelmed while tax receipts decline due to a shrinking economy. All these consequences contribute to rising poverty and can fuel social unrest and instability.

Choosing the right mix of investments in social protection systems that are productivity raising and pro broad-based growth helps outweigh the costs of implementing these systems. But it is clearly possible, and essential, to design social safety net systems so that the costs and benefits are in balance and sustainable.

**Consumption smoothing**

The key to sustainable government spending on social protection systems rests on the concept of consumption smoothing. Consumption smoothing refers to the balance of public and private savings and spending that individuals in society
We need to facilitate recovery from an economic crisis, enhance the resilience of citizens in the face of an economic downturn, and promote long-term, broad-based economic growth and stability.

Social protection systems also boast positive multiplier effects by providing further positive gains for society and the economy, such as reducing the incidence of child labor. The 2000/01 World Bank World Development Report notes that child labor is an undesirable coping mechanism for families facing economic dislocation or sudden economic shocks. Families often use child labor in such instances as a mechanism to cope with household income fluctuations. Families would perhaps rely less on their children if they had other social protection options to help smooth out their income.

Social protection systems have three clear merits that are critical to facilitating recovery from an economic crisis, enhancing the resilience of citizens in the face of an economic downturn, and promoting long-term, broad-based economic growth and stability:

- They promote investments in people that prevent individuals from becoming unproductive, such as health care.
- They invest in long-term human capital formation through education and worker training, which reinforces productivity and long-term innovation and economic growth.
- They essentially remove unproductive workers and the elderly from the workforce while still allowing them to consume with appropriate public assistance.

Social protection systems use these three conduits to boost living standards, which helps stabilize and rebalance national and global economies.

And social protection systems do this without hindering market flexibility. Noted economists Rebecca Blank and Richard Freeman note that there are several margins along which an economic agent can be flexible, but the most common understanding of flexibility refers to the speed with which price and quantity adjust to changes in the economic environment. Flexibility viewed through an economist’s lens is only desirable in so far as it contributes to productivity and
economic growth. The pressing question therefore becomes whether social protection systems facilitate economic stability and adjustment in order to reinforce productivity and economic growth.

The short answer is that social protection systems reinforce individuals’ coping capacity so that they are more adaptable to changing economic circumstances and crises. For instance, child support measures can encourage greater labor force participation by women, while unemployment insurance and job training can assist individuals in finding a workplace that allows them to realize their full productive potential.

And social protection programs and services themselves can be a powerful source of generating employment in a period where high unemployment or informal employment plagues countries around the world. Government spending on social protection systems amid an economic downturn can help boost public-sector employment—investing in people to enhance their productive potential and bolster and rebalance national and global economies.
The case against deregulation

There is a large body of literature that argues that labor market policies such as unemployment insurance or job protection, in particular, hinder an economy’s flexibility. For instance, those opposing an extension of unemployment benefits in the United States continually evoke this argument. The debate over labor market policies pits those who push for deregulation of labor market policies, and greater employment and wage flexibility against those who do not buy into the claim that deregulation is a solution to employment problems.

Economists have failed to reach a consensus on the effect of labor market policies on aggregate economic performance and on the potential for deregulation to improve outcomes, despite decades of empirical analysis. Freeman, for example, presents several reasons for the lack of consensus on the relationship between labor market policies and flexibility.

He argues that there is no sound way of quantifying the social impacts and multiplier effects of labor market policies. It is hard, he says, to quantitatively capture the positive effects of food stamps that ensure that a worker is more productive because she or he has had enough to eat. He similarly points to the multiple positive returns of an unemployment benefit given to a laid-off worker who then spends this money to buy books for his child’s upcoming school year. The fact that the child’s education was not interrupted means the child will be a positive contributor to the economy later on, but these benefits are difficult to account for in empirical terms.

Freeman also argues that those in favor of deregulation of labor market policies, and increased employment and wage flexibility, operate under the notion that markets work nearly perfectly in the absence of labor market policies. These preconceived notions—“priors” as Freeman calls them—influence the way scholars analyze data and interpret empirical results.

Whatever the state of debate over labor market flexibility, the current economic crisis has all but confirmed that unfettered free markets do not work perfectly and that
there is a real need for social protection systems to compensate for the deficiencies of an imperfect market. The most recent global economic crisis underscores the fact that social protection systems do not hamper dynamic economic growth. It highlights that the cost of not having adequate protections in place can be more detrimental than the costs associated with putting them in place and sustaining well-planned systems, and that more regulation of the labor market does not hinder productivity. Social protection systems are clearly a necessary investment in people that enhances equitable economic growth. Social protections enhance economic growth and foster productivity if designed and governed appropriately.¹⁵
It is imperative as the global economy starts its shaky ascend out of the Great Recession that national governments, donor countries, and multilateral institutions shift focus to build and reinforce long-term social protection systems and policies. This will help protect workers, create the conditions for sustainable economic growth, safeguard against a future economic crisis, and rebalance the global economy by cultivating aggregate demand and nudging, especially emerging markets, away from an export-led model of growth toward one based on domestic consumption.

A number of countries that could afford it enacted a series of economic stimulus packages that were largely successful in constraining an even bigger global recession. The time is now ripe for an international reform agenda that ensures that short-term solutions seamlessly lead into sustainable long-term policies to promote sustainable and equitable economic growth worldwide.

To this end, all national governments must make establishing social protection systems a priority, and all wealthy countries should provide technical and financial assistance through bilateral and multilateral channels to emerging and developing countries that require help in establishing these social protection institutions.

Trade liberalization and technological advancements have allowed for the evolution of global production systems and new international divisions of labor. They have introduced new sources of competition and led to churning and shifts in employment and skill requirements by allowing new entrants into the global economy. Losses and gains occur in varying sectors, firms, and regions within a country or between countries.

Globalization also plays its role in altering family structures as people move from rural to urban areas, or to different countries in search of better employment opportunities. It is important to note that, in light of this increasingly
interconnected world, one country’s social protection policies also bear on those in other countries. This makes it imperative that donor countries make transfers to fund social protection systems in countries that cannot afford to do so adequately on their own.

Multilateral institutions such as the International Labor Organization, the World Bank, and regional development banks must coordinate their efforts to achieve maximum and lasting broad-based economic growth, which is not possible without adequate and appropriate social protection mechanisms. The ILO sets social protection systems as one of the strategic pillars of its ongoing Decent Work campaign—along with rights at work, employment, and social dialogue—all of which is designed to promote opportunities for work that are just and productive. Yet the ILO’s approach to social protection is focused more on the supply side (labor), and is somewhat limited in its handling of other functions of social protection systems such as health insurance, retirement, and disability pensions. The Asian Development Bank, however, outlines five categories of social protection:

- Labor market interventions, including active policies such as infrastructure projects, and passive policies such as unemployment insurance
- Social insurance such as retirement pensions and disability pensions
- Social assistance such as food stamps
- Micro- and area-based programs
- Child protection laws and regulations

The World Bank sets the importance of social protection in the context of a social risk assessment and management framework, making the standard distinction between social insurance and social assistance programs. The World Bank also now acknowledges that “growth and sound macroeconomic policies, while necessary, are insufficient for sustained poverty reduction.”

The World Bank’s approach differs from that of the ILO and the Asian Development Bank in that it is focused on targeted protection for vulnerable groups such as the very poor, migrants, women, and children as opposed to a universal approach that applies to everybody. The ILO focuses on workers, and the ADB on societies as a whole. These different approaches mean that efforts aren’t always easy to coordinate. But coherence when implementing social protection systems across these international organizations would significantly enhance their respective efforts and is therefore necessary.
One promising approach is a proposed Social Insurance System Catalytic Revolving Fund to help developing countries finance the creation or expansion of basic social insurance systems.

The ILO and World Bank should work in cooperation to create a well-capitalized fund. But it is up to world leaders—whether in the G8, the G8+5, or especially the G20—to back their rhetoric up with action.

The G20 must make good on financial support to build social protection systems in developing countries. It must mandate that international organizations coordinate their social protection efforts in a specific group of pilot countries and present the results at the next leader’s summit to be held in France in February 2011.
Endnotes


9 Ibid.


20 For a discussion of reforms to establish the IMF’s independence to conduct country and multilateral surveillance as a basis for improving macroeconomic cooperation and the functioning of the exchange rate system, see Richard Samans, “Transitioning to a New U.S. International Economic Policy: Toward a “Global Deal” to Revive and Broaden the Benefits of Growth” (Washington: Center for American Progress, 2008), p. 27-28.
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