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The political economy of labor market liberalization

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THE POLITICAL ECONOMY OF LABOR MARKET LIBERALIZATION

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by

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2009

The dissertation of Jinhee Lee Choung is approved, and it is acceptable in quality and form for publication on microfilm and electronically:

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ABSTRACT OF THE DISSERTATION

The Political Economy of Labor Market Liberalization

by

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Doctor of Philosophy in Political Science

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Professor J. Lawrence Broz, Co-Chair

Professor Stephan Haggard, Co-Chair

This dissertation examines the role of policy tradeoffs in labor market liberalization. Countries with a rigid labor market and restrictive employment protection laws can raise the likelihood of liberalization by offering unemployment insurance as an alternative means of labor protection. Contrary to prevailing assumptions, employers are supportive of social welfare policies when doing so would help achieve a more flexible labor market—defined by the ease of hiring and firing—by ameliorating labor opposition through policy compensation.

Moreover, the likelihood of labor market liberalization rises in times of labor weakness and waning power. Heightened market competition generated through increased economic openness, economic downturns, and financial crises negatively affect labor's bargaining power. On the other hand, democratization that enhances labor mobilization, protectionist policies that limit market competition, and favorable

economic conditions that increase national wealth, all strengthen labor's bargaining power and thus its ability to resist liberalization.

Thus, this dissertation examines the recent *changes* in employment protection laws in a sample of 84 countries in the world through a quantitative analysis (Chapter 2); in the middle-income countries in East Asia through a comparative case study (Chapter 3); and in the Republic of Korea through an in-depth historical-institutional case study (Chapter 4). The results of this empirical investigation provide strong support for the proposed theory.

Chapter 1: Introduction

With the present financial crisis in the US and the economic downturns in other parts of the world, the role of government in managing the economy is again the question of the day. How much regulation is desirable? What determines how governments go about ensuring the economic security and prosperity of its citizens? In this dissertation, I investigate the political economy of labor market institutions in the area of employment protection, which has stirred up much academic and popular controversy both as a causal factor behind a country's economic performance and also for the protection it provides to labor in volatile and globalizing market environments.[1] Employment protection legislation regulates hiring and firing procedures and thus largely determines the overall flexibility (or rigidity) of the labor market and the level of job security for workers.

This dissertation examines the recent *changes* in employment protection in a sample of 84 countries in the world through a quantitative analysis (Chapter 2); in the middle-income countries in East Asia through a comparative case study (Chapter 3); and in the Republic of Korea through an in-depth historical-institutional case study (Chapter 4). I have collected new data to carry out the analysis, through which we also

[1] Employment protection legislation (EPL), by stabilizing employment relationships, may help determine a country's comparative advantage and competitiveness in international trade. See Riboud et al. 2002, Lindauer 1999, OECD 2004, Hall and Soskice 2001, Cuñat and Melitz 2007. Too much protection, however, may cause high unemployment; the strictness of employment protection is often blamed for the poor employment performance of European countries. For the effects of employment protection on economic performance, see Lazear 1990, Bertola and Rogerson 1997, Saint-Paul 1997, Bertola, Boeri, and Cazes 2000, Heckman and Pages 2004.

learn of the cross-national variance in employment protection in the present. Undergirding the analysis is a fresh take on the political economy of labor market liberalization in particular and of institutional change in general.

My argument is that the choice of labor market institutions—employment protection regimes in particular—results from a political bargain between business and labor, a bargain that is conditioned not only by labor power, but also by the existing set of labor market institutions that shape the policy preferences of labor and business. Where the policy status quo exhibits little employment protection, an increase in labor power—brought on most prominently by democratization—prompts workers to bargain for more protection, raising the likelihood that there will be more employment protection. Where workers already enjoy substantial employment protection, however, a decline in labor power—brought on most prominently by economic competition—encourages employers to demand labor market flexibility. Under this scenario, employers may reverse their traditional opposition to social policy commitments in their pursuit of labor market liberalization and offer unemployment insurance (UI) to overcome labor opposition.[2] Thus, countries that adopt or expand UI are more likely to reduce employment protection since labor is appeased through social policy concessions. This bargain, however, forces both employers and labor to settle for their second-best policy choice. I develop the logic of this argument more systematically in the following chapter.

In order to assess these arguments with quantitative methods, I have compiled

[2] Unemployment insurance provides assistance to the unemployed through payroll and other taxes paid by employers and/or employees.

data on labor market institutions in 84 countries at two points in time, 1997 and 2006. Given the infrequent changes in labor laws, extending the points of analysis to ten years apart allows sufficient variation in the dependent variable for making associational inferences through a first differences analysis. I also employ a qualitative analysis on a subset of East Asian economies and a detailed case study on Korea to further test the plausibility of my arguments. The East Asian chapter compares six middle-income countries of Indonesia, Korea, Malaysia, the Philippines, Thailand, and Singapore, with the core of the chapter focusing on a comparative analysis of Indonesia and Malaysia. I probe the impact of regime change brought on by the East Asian financial crisis in 1997-98 (or lack thereof in the case of Malaysia) on the shifting balance of political power between business and labor as reflected on the policy outcomes of employment protection. A detailed look into the Korean case further clarifies the causal mechanisms at work, particularly of the bargain over employment protection and unemployment insurance between business and labor. This introductory chapter proceeds with an explanation of the dependent variable and a discussion of the larger scholarly literature that inspired this dissertation project.

1.1. Employment protection legislation

Employment protection legislation (EPL) refers to a set of regulations that govern the hiring and firing processes of workers and the rigidity of working hours, *i.e.*, the laws on unfair dismissals, termination of employment for economic reasons, severance payments, minimum notice periods, administrative authorization for dismissal, and prior consultations with trade union and/or labor administration representatives (Bertola, Boeri, and Cazes 2000). The purposes of these regulations are to protect the welfare of workers against the excessive power of employers, improve employment conditions, and insure workers against the risk of job loss and income insecurity (Lindauer 1999, Riboud, Sanchez-Paramo, and Silva-Jauregui 2002, OECD 2004). EPL focuses on the protection of *existing* jobs and income, and it can be provided through both labor legislation and collective bargaining.[3]

For example, hiring restrictions may specify whether term contracts can be used only for temporary tasks, and stipulate the maximum cumulative duration of term contracts. On firing, some countries do not even allow redundancy as a basis for terminating workers, and others require the employer to notify a third party (such as a government agency) to terminate one redundant worker. Advance notice informs workers of layoff plans and gives them time to search for new jobs, while severance payments provide financial compensation for hardship connected with layoffs.

Similarly, offering internal redeployment and cooperating with the trade unions on the re-employment of redundant workers may strengthen longer-term attachment of workers to their jobs and employers, which could benefit employers as workers invest in human capital and improve their productivity. Thus, stricter EPL may enhance aggregate productivity through better enterprise adaptation, technological progress, and vocational training accompanied by rising incomes.[4]

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[3] While these restrictions benefit workers already in the formal sector with employment, they tend to lower entry opportunities for those outside the formal sector.

[4] Stricter EPL may also provide better employment protection to certain vulnerable groups—older workers, pregnant women, and parents of small children, etc.—who in the case of dismissal would face

These restrictions, however, are costly to employers; they compromise the employer's ability to control labor costs by imposing severance payments and other administrative costs. Stricter EPL reduces an employer's ability to restructure the firm in a timely manner and respond quickly to changing economic environments. They can be costly to labor as well, especially to those who are outside the formal sector seeking to enter the labor market. The growing dichotomy between workers in regular or permanent jobs enjoying high employment security through EPL and those in temporary jobs (fixed-term, seasonal, or any type of informal employment) may contribute to increasing labor market rigidity, inequality, and higher unemployment.

Most advanced industrialized countries enacted various employment protection provisions in the 1960s and 1970s. Greece was first to legislate individual severance pay and advance notice requirements among the OECD countries in 1955, followed by Germany in 1969, Italy in 1970, and Canada and Switzerland in 1971 (OECD 1993). While most OECD countries began regulating their labor markets once they already attained relatively high income per capita, East Asia, Latin America, and other countries started regulating their markets much earlier in the development process, as early as the beginning of the twentieth century (Heckman and Pagés 2004). The Mexican Constitution of 1917, for instance, articulated the principle that protecting workers was one of the duties of the state, and by the 1930s and 1940s, most Latin American countries had developed a labor code. Under the centrally planned economic system in the former Communist countries, workers enjoyed a high degree of employment

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difficulty in finding a new job and another source of income. The analytic focus of this dissertation, however, is on redundancy layoffs or dismissals due to economic reasons such as corporate restructuring.

protection in their jobs. Similarly, Korea and Taiwan had instituted highly pervasive labor regulations during the authoritarian developmental era.

Table 1.1 lists the employment protection scores in the order of protectiveness as developed by Botero et al. (2004) for a sample of 84 countries as of 1997. Higher values correspond to more extensive legal protection of workers in the areas of alternative employment contracts (*e.g.*, limitation on fixed-term contracts), cost of increasing hours worked (*e.g.*, cap on overtime), cost of firing workers (*e.g.*, notice period, severance pay), and dismissal procedures (*e.g.*, third party approval). The mean employment protection score is 0.49 with a standard deviation of 0.19, and the minimum score is 0.15 (Zambia) and the maximum is 0.83 (Russia). As of 1997, Zambia, for instance, imposed no restrictions of any kind on firing and only required that part-time workers enjoy the mandatory benefits of full-time workers.[5] Russia, on the other hand, was restrictive in almost every aspect. It had, for instance, a legally mandated notice period of two months and severance pay of another two months.

How stable are these laws, and how and why do countries liberalize or strengthen EPL? Even more interesting than the cross-national variation are the policy changes and reforms taking place on these rules as the issue of employment protection has become a focal point of contention between labor and management in recent years all throughout the world. Spain, for instance, has the European Union's highest unemployment rate of 18% presently, with most of the newly unemployed comprising of workers let go from their temporary contracts (*The Economist*, 7/9/2009). The

[5] The level of benefits for full-time workers was very minimal in Zambia.

Socialist Prime minister, José Luis Rodríguez Zapatero, has ignored the calls for labor market reform from academics and employers, not wanting to provoke a general strike and destabilize his already precarious hold on power. The core of Spain's unemployment problem is its two-tier labor market in which two-thirds of workers have permanent contracts with extensive job security (that creates labor market rigidity) while the remaining third has virtually no security. In times of expansion this dual labor market provides flexibility to employers and opportunities for workers, but the burden of recession is disproportionately born by workers on temporary contracts.

Spain's two-tier labor market has resulted from labor market reforms of earlier years in which the recourse to temporary forms of employment was eased while leaving existing provisions for regular or permanent contracts practically unaltered. In fact, the OECD *Employment Outlook* 2004 notes that a process of convergence across the OECD countries has taken place in regards to EPL over the past 15 years, driven by an easing of regulation on temporary contracts in the countries where EPL was relatively strict at the end of 1980s. In other parts of the world, Argentina, Colombia, Peru, and Uruguay liberalized the labor market, while Chile and Brazil increased the legal protection of workers in the context of a democratic transition in the past two decades (Heckman and Pagés 2004). In East Asia, Korea and Japan liberalized, while Indonesia and Thailand strengthened their employment protection regimes over the past decade.[6]

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[6] By one account, non-regular workers currently account for more than a third of the employed in Japan, a country that made company-centered 'life-time' employment and job security the centerpiece of its labor market institutions in the post-war period (Chatani 2008).

This study is an effort to explain the trends and causal factors behind the changes in labor market institutions in a systematic way, a topic that has received surprisingly scant attention in political science. The question of employment protection is a central concern in the political economy of both advanced and developing countries, as it affects economic performance and the stability of labor relations in a significant way. Scholarly attention, however, has been dominated by the outcomes of government spending as the measure of the government's role and involvement in the economy. Though important in its own right, government spending is an inadequate measure of social and labor policy development from an empirical standpoint.[7] The core hypothesis that drives the globalization-welfare state theory, for instance, centers on spending directed at mitigating labor market risk and not so much on health, education, pension or other social and public spending categories that dominate the overall size. Aggregate spending measures in fact may have little relevance to market volatility and compensatory spending, driven instead by factors such as demographic changes. Moreover, the most direct form of protection may take discrete labor policy outcomes

[7] I make the argument that government spending is an inadequate measure of social and labor policy development from an empirical standpoint because labor market social expenditures correspond primarily to the severity of unemployment rates. Utilizing OECD's disaggregated public social expenditures database by member countries between 1980 and 2001 (SOCX 2004), I examine spending patterns specific to the amelioration of labor market risks. Table 1.2 shows expenditures on labor welfare calculated as combined spending on unemployment and active labor market policies (ALMP) for select OECD countries, averaged over two-year periods from 1980 to 2001. The years with the highest spending levels are highlighted to emphasize trends. Among European countries except Germany, labor welfare expenditures peaked around the first half of the 1990s, while in the UK and US it peaked during the first half of the 1980s. In Korea and Japan, expenditures peaked in the late 1990s, reflecting the impact of the East Asian financial crisis as well as Japan's prolonged recession. Mexico, on the other hand, shows no trending and spends the least among OECD countries on labor market policies at 0.1% of GDP. Comparing these spending patterns to widely-suggested explanatory variables such as trade openness and deindustrialization, Table 1.3 shows that government spending correlates strongest with unemployment rates, followed by trade openness and the proportion of employment in services between 1980 and 2001 (an indicator of deindustrialization).

and other regulatory measures not captured in spending. Labor market institutions have not received sufficient scholarly attention, and this dissertation is an attempt to fill that gap in the literature.

Additionally, I advance an argument that is conditional. It applies primarily to non-Western, middle-income countries that have already developed extensive labor protection during the earlier years of industrialization. There is an important gap in the literature on the political economy of labor market institutions in the middle-income countries in general and East Asia in particular, and with this dissertation I seek to add to our theoretical and empirical understanding of the changing patterns of employment regulation.

1.2 Existing explanations

What explains possible variance in the extent of employment protection? I use the welfare state literature as a guide, since the question of employment protection concerns the role of government in managing the economy and the welfare of workers. There are three major competing theories that explain the divergent outcomes in social protection: 1) the power resources theory, which credits labor mobilization or organizational capacity for welfare state expansion; 2) the globalization theory, which holds that external risks associated with economic openness generates compensatory pressures; and 3) the varieties of capitalism theory, which emphasizes the employers' need for a skilled workforce as the driver of welfare state consolidation. In this section I review and assess these arguments and the stock of empirical evidence amassed so far, identifying their strengths and shortcomings to help develop my thesis and working hypotheses.[8]

First, labor strength is the core causal variable for the power resources theory. Institutions are designed to transfer resources from those out of political power to those in power, as well as to entrench those already in political power (Olson 1993). Thus, welfare states would develop the farthest in nations where labor was strongest as measured by high rates of unionization and the organization of unions into a cohesive labor central or confederation (Korpi 1983).[9] The balance of power between labor and capital is fluid and variable, and while capital would always have the upper hand within a capitalist framework, labor could have potential access to political resources that may increase its power, and thereby allow it to implement social reform and alter distributional inequalities to a significant degree (Esping-Andersen 1985, O'Connor and Olsen 1998).[10] As such, where labor movements are weak, unions have been unable to make fiscal demands on the state (*e.g.*, East Asia). Union membership in Western

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[8] One of the more comprehensive studies on the regulation of labor by Botero et al. (2004)—whose data I utilize in this dissertation—finds that the effects of legal origins on labor regulations and social security systems are the most significant and larger than the effects of the political power of the left. Countries with French and socialist legal origins are the most interventionist—and the common law countries, least—in various areas of labor law. Choung (2007) challenges their finding, however, showing that when employment protection and unemployment insurance are jointly considered, the explanatory power of legal origins largely disappears. Instead, the study finds that the level of development is the strongest driver of the institutionalization of UI, that political factors such as the power of the left, collective labor rights, and unionization are associated with more stringent (labor-friendly) regulations, and that openness to trade is not significant as an explanatory factor in the development of labor market institutions. Moreover, a longer history of democracy is linked to less employment protection, reflecting the legacy of socialist regimes and the need for stability in labor relations in other types of authoritarian regimes.

[9] The organizational and mobilization capacities of the working class are largely credited for the growth of the European welfare state.

[10] Revisions to the original formulations include the application of Barrington Moore's class coalition thesis to the transformation of the modern state, tracing the origins of the Keynesian full-employment commitment and the social-democratic welfare state edifice to the capacity for the labor-agriculture alliance (as in Sweden), or a working class-white collar coalition (as in Austria) (Esping-Andersen 1990).

Europe averaged 40 percent of the labor force in the late 1990s, which is more than double the East Asia average of 17 percent (Garrett and Nickerson 2001).

As the literature on welfare state has expanded beyond developed countries, scholars have examined the impact of regime type on social spending and found mixed results (Adsera and Boix 2002; Kaufman and Segura 2001; Rudra and Haggard 2001; Haggard and Kaufman 2008). Although increased electoral competition and interest group activities may generate pressures to expand social programs and labor protections, new democracies differ in terms of the strength of left-leaning parties, centrally-organized labor unions, and other forms of social organizations, all of which lead the fight for social welfare states in advanced industrialized countries.

Second, much scholarly work has focused on globalization as the primary explanatory variable for social protection or welfare states, looking at government transfers and consumption or aggregate social spending as the dependent variable (Cameron 1978; Ruggie 1982; Katzenstein 1985; Rodrik 1998; Swank 1998; Garrett 1998; Esping-Anderson 1999; Stephens, Huber & Ray 1999; Pierson 2001; Avelino, Brown, and Hunter 2005). They ask: How has international economic integration affected the ability of governments to use the policy tools of the state to redistribute wealth and risk within their countries? Do governments respond to globalization with social policy choices that are oriented more toward protecting people's welfare (compensation) or cutting costs (efficiency)?

Proponents of the compensation hypothesis argue that the role of government expands in response to demands for protection by those who lose out in international competition. Compensation becomes necessary to maintain political support for trade openness as well as the politicians' hold on power. Domestic interests trump pressures of economic integration, and social insurance and other mechanisms of social protection expand as a result. In this story, it is not only labor that demands government intervention. Businesses also seek protection in the face of market volatility caused by globalization, and pressures from all types of domestic interest groups increase government spending.

Proponents of the efficiency hypothesis, in contrast, assume that high levels of social spending reduce corporate competitiveness in global markets by increasing the cost of labor through higher payroll and income taxes. Increasing fiscal expenditures crowd out private investment and increase the value of the real exchange rate through higher interest rates. Hence, business groups exposed to increasing international competition pressure their governments to reduce social expenditures. Governments find raising taxes or borrowing unpalatable in the face of capital mobility, and thus cut social programs and reduce spending.

Challenging globalization as the source of welfare state expansionism, Iversen and Cusack (2000) and Iversen (2001) argue that there are no compelling theoretical reasons to expect trade openness and welfare spending to be linked, and that welfare state expansion since the early 1960s—measured primarily as government transfers and consumption—has in large measure been driven by deindustrialization and the decline of the blue-collar working class. The division between agriculture and industry on the one hand, and services on the other, presents a major skill boundary in the economy.

The threat of having to relocate across this boundary is a major risk factor for individual workers because their skills will be downgraded and they will lose employer-provided social benefits. Therefore people turn to the state for insurance against these risks.

Crediting either globalization or deindustrialization, most studies focusing on OECD countries find stronger empirical support for the compensation hypothesis. In Europe, both the inception of social insurance in the first decades of the twentieth century as well as the expansion of the welfare state in the second half of the century took place in the context of expanding trade.[11] Similarly, increasing capital mobility did not affect government spending for a sample of nearly one hundred developed and developing nations (Garrett 2001). Reviewing the literature on globalization and the role of government, Brune and Garrett (2005) conclude that the evidence for compensation is marginally stronger but not compelling.

Lastly, the 'varieties of capitalism (VOC)' approach emphasizes the progressive role of employers in social policy development. The class-based perspective that has dominated social policy studies posits that employers have played a reactive role in welfare state development by opposing the demands of labor associations for the expansion of social programs. Using the conceptual devices of comparative institutional advantage and institutional complementarities, Estevez-Abe, Iversen, and Soskice (2001) contend that social protection aids the market by helping economic actors overcome market failures in skill formation. Highly portable skills are generally less

[11] A recent study challenges the compensation hypothesis. Kim (2007) finds a consistent effect of external risk on volatility of the major economic aggregates but a largely insignificant effect of openness. This study suggests that economic volatility may be a mistaken link in explaining the openness-spending nexus, calling for further research on the causal mechanisms linking the two.

risky than highly specific skills; in the former case, the market value of the skill is not tied to a particular firm or industry. In turn, expectations of higher future job insecurity will lead a rational worker to invest in general rather than firm- or industry-specific skills. Thus, they argue, firms may seek to satisfy their need for specific skills by insuring against workers' exposure to risks through employment and unemployment protection.[12]

Mares (2003) similarly argues that profit-maximizing firms—facing competition in domestic or international markets—support social policies when doing so would induce workers to invest in skills and lower their exposure to labor market risks. A number of features of social policies—such as the wage indexation of social policy benefits, and the conditionality of social policy benefits on a broad set of factors related to employment performance—reinforce their investment in the provision of skills and reproduce the skill and wage differentiation established at the firm level during moments in which the employment relationship is temporarily interrupted. Hence, while firms employing high-skilled workers are expected to favor the participation of employers in the administration of social insurance, firms that do not rely on skilled workers are expected to be uninterested in these institutional characteristics of social policy. Also, firms in industries strongly affected by risk are expected to favor the

[12] Moreover, the coupling of social protection and skill requirements elucidates the likely product market strategies of companies. Where there is a large pool of workers with advanced and highly portable skills with low social protection, companies enjoy considerable flexibility in attracting new workers, laying off old ones, and starting new production lines. Unlike in economies centered on a combination of firm- and industry-specific skills, the flexibility in the labor market allows for high responsiveness to new business opportunities, and facilitates the use of rapid product innovation strategies. The advantage of asset-specific welfare-production regimes, on the other hand, facilitates the development of deep competencies within established technologies and the continuous upgrading and diversifying of existing product lines.

expansion of the risk pool, while firms characterized by a lower incidence of risk are expected to oppose highly redistributive social policies in fear of becoming subsidizers of high-risk industries. The incidence of risk and the skill intensity of the workforce together predict the preferences of employers.

The VOC literature argues that employers are not singularly opposed to social policy development, and some may even support costly policies that protect their skilled workforce. The suggested positive role of employers in the development of unemployment insurance policy, however, awaits more empirical evidence. For instance, Mares (2003) credits the divergence in outcomes between France and Germany to different political alliances supporting these policies, often around a policy outcome that is a second-best choice for some actors.[13] Reformist policy entrepreneurs played a critical role in the formation of these strategic alliances by using the process of social policy design to further the political compromise among unions and employers.[14]

Employers play a key role in social policy development, I argue, but for a different reason in developing countries. When the employers' main concern is profit maximization, labor market flexibility becomes a policy priority. Accomplishing this goal in countries with rigid labor markets, however, may require employers to support

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[13] France established one of the first national-level policy of unemployment compensation by introducing a Ghent policy in 1905, while Germany initiated a means-tested policy of unemployment assistance as an attempt to cope with the labor market disturbances of World War I and established contributory unemployment insurance in 1927 (Mares 2003).

[14] Esping-Andersen (1990) also emphasizes political coalition-building. In the Nordic countries, a broad red-green alliance produced policy compromises on a full-employment welfare state in exchange for farm price subsidies. In contrast, although the New Deal in the US was premised on a similar coalition forged by the Democratic Party, the labor-intensive South blocked a truly universalistic social security system and opposed further welfare state development. In general, where no one party is dominant, advancing policy interests requires making political compromises and building coalitions across the aisle. It may even be the case that labor and business forge a partnership to change an undesirable policy status quo.

social policy development to cushion any fallout from labor adjustments. The next chapter elaborates on this and other conjectures more in depth.

In this dissertation, I build on the various insights gathered from the existing literature to develop a theory of preferences over the choice of labor market institutions and of the conditions under which political actors are either forced to compromise and settle for their second-best policy choice or singularly able to advance their agendas. A key argument is that the status quo institutions condition the nature and direction of the institutional change by shaping actor preference. Changes in the power balance between business and labor arising from factors such as democratization and globalization, trigger fresh negotiations over policy outcomes, and depending on the extent of the shift, new equilibrium labor market institutions may entail the strengthening of employment protection legislation, a stasis, or its weakening supplemented by an adoption or expansion of unemployment insurance. My argument on preferences conditioned by the status quo is a compelling perspective from which to understand and predict the inter-temporal variation in labor market institutions.

Table 1.1: Employment protection scores, 1997 (Botero et. al, 2004)

Country	Employment Protection	Country	Employment Protection
Russian Federation	0.83	Chile	0.47
Tunisia	0.82	Madagascar	0.47
Portugal	0.81	Sri Lanka	0.47
Mozambique	0.79	Peru	0.46
Kazakhstan	0.78	Korea	0.45
Georgia	0.77	Switzerland	0.45
Kyrgyz Republic	0.75	Taiwan	0.45
Finland	0.74	Burkina Faso	0.44
France	0.74	India	0.44
Slovenia	0.74	China	0.43
Spain	0.74	Thailand	0.41
Sweden	0.74	Ecuador	0.40
Netherlands	0.73	Turkey	0.40
Latvia	0.72	Hungary	0.38
Germany	0.70	Bolivia	0.37
Jordan	0.70	Egypt	0.37
Norway	0.69	Kenya	0.37
Indonesia	0.68	Australia	0.35
Tanzania	0.68	Uganda	0.35
Mali	0.67	Argentina	0.34
Slovak Republic	0.66	Colombia	0.34
Ukraine	0.66	Ireland	0.34
Italy	0.65	Pakistan	0.34
Venezuela	0.65	Mongolia	0.33
Poland	0.64	Romania	0.33
Lithuania	0.62	South Africa	0.32
Panama	0.62	Singapore	0.31
Armenia	0.60	Ghana	0.29
Dominican Republic	0.60	Israel	0.29
Mexico	0.59	United Kingdom	0.28
Brazil	0.57	Uruguay	0.28
Denmark	0.57	Canada	0.26
Vietnam	0.54	Morocco	0.26
Bulgaria	0.52	Zimbabwe	0.25
Czech Republic	0.52	United States	0.22
Greece	0.52	Malaysia	0.19
Belgium	0.51	Nigeria	0.19
Senegal	0.51	Malawi	0.18
Austria	0.50	Jamaica	0.16
Lebanon	0.50	Japan	0.16
Croatia	0.49	New Zealand	0.16
Philippines	0.48	Zambia	0.15

Source: Botero, Juan C., Simeon Djankov, Rafael La Porta, Florencio Lopez-de-Silanes, and Andrei Shleifer. 2004.

Table 1.2: Labor welfare expenditures (Unemployment + ALMP) – Select OECD countries (% GDP)

	1982 - 83	1984 - 85	1986 - 87	1988 - 89	1990 - 91	1992 - 93	1994 - 95	1996 - 97	1998 - 99	2000 - 01
Denmark	6.1	5.6	4.9	5.3	5.6	6.7	6.5	5.7	5.0	4.5
Finland	1.9	2.0	2.5	2.3	2.8	6.0	5.8	4.9	3.7	3.0
France	0.0	1.5	3.0	2.7	2.7	3.2	3.1	3.2	3.1	2.9
Germany	3.5	4.1	4.6	4.1	3.8	4.1	4.1	4.0	3.7	3.5
Hungary	n/a	n/a	n/a	n/a	n/a	2.8	1.6	1.1	1.0	0.9
Japan	0.5	0.4	0.3	0.2	0.6	0.6	0.7	0.7	0.8	0.8
Korea	n/a	n/a	n/a	n/a	0.0	0.1	0.0	0.1	0.8	0.5
Mexico	n/a	n/a	n/a	n/a	0.0	0.0	0.1	0.1	0.1	0.1
Turkey	0.4	0.4	0.5	0.6	0.7	0.7	0.7	1.0	0.9	--
UK	2.4	2.5	2.4	1.4	1.4	1.8	1.4	1.0	0.8	0.6
US	0.9	0.5	0.8	0.7	0.7	0.8	0.6	0.5	0.4	0.4

Sources: OECD (2004) Social Expenditure database (SOCX), 1980-2001.
Notes: Included in unemployment expenditures are all cash expenses that compensate for unemployment, such as redundancy payments out of public resources as well as pensions to beneficiaries before they reach the 'standard' pensionable age if these payments are made because they are out of work or otherwise for reasons of labor market policy. The category of active labor market programs (ALMP) contains all social expenditure (other than education) which is aimed at the improvement of the beneficiaries' prospect of finding gainful employment or to otherwise increase their earnings capacity (Employment Outlook, OECD, 2002).

Table 1.3: Correlation among the key variables – Select OECD countries (1980-2001)

	LMP	Unemp.	Trade	Services	Industry	Govt cons
Labor market policy expenditures (% GDP)	1.0000					
Unemployment rate	0.5339	1.0000				
Trade (% of GDP)	0.3703	0.2084	1.0000			
Employment in services (% total employment)	0.3420	0.2149	-0.0002	1.0000		
Employment in industry (% total employment)	-0.0552	-0.1107	0.0899	0.0257	1.0000	
Government consumption expenditures (% GDP)	0.8185	0.4798	0.1470	0.5414	0.0603	1.0000

Sources: Labor market expenditures data from OECD (2004) Social Expenditure database (SOCX), 1980-2001; World Development Indicators.

Chapter 2: Globalization, Unemployment Insurance, and Labor Market Liberalization

A central issue in political economy at the present is the effect of globalization on social and labor policy and welfare. While globalization—the growing integration of economies and societies around the world through trade, financial flows, and movement of people and ideas—is often credited for reducing poverty and fueling growth in several Asian countries, its impact on inequality and economic stability is hotly debated. In particular, the issue of employment law has become a focal point of contention between labor and management in recent years as the global recession is forcing companies to cut their workforce and productions. In France, efforts to legislate a youth labor law—the *contrat première embauche* (CPE), or first employment contract—generated intense street protests against the bill which would have allowed employers to terminate employment of workers under the age of twenty-six without cause within their first two years of employment. In Korea, a law aimed at protecting the rights of "non-regular workers" has become the cause of protest among the very people the law is designed to protect. Japan's defining social institution of lifetime employment has been dismantled, and even in the United States, many hanker for laws that would keep jobs in the country and away from foreigners by limiting outsourcing, offshoring, and immigration.

Is globalization the source of these societal ills? Are these developments inevitable if globalization prevails? What can domestic politics do to mitigate the pressures? The international integration of markets for goods and services over the past two decades has accelerated beyond the confines of developed countries. The pundits thus predict that market economies throughout the world would converge on the path of deregulation and liberalization as increased capital mobility allows employers to seek out the least expensive and restrictive labor regimes in the face competitive pressures in the global market. On the other hand, observations are made that convergence and homogenization have not materialized, and varieties of capitalism and labor politics persist in both developed and developing countries (Thelen, 2001, Hall and Soskice 2001, Wood 2001).

This chapter examines the impact of globalization on labor protection in general and employment protection (EP) in particular. Countries adopt various labor market institutions—job security regulations, minimum wages, unemployment benefits, and the like—to mitigate the impact of market volatility on labor welfare. Some nations focus on providing workers with job security through employment protection, while others develop institutions that provide government assistance to workers when they lose their jobs, of which the most common form is unemployment insurance (UI). Some have both and many have neither, and the particular combination or focus of policies varies across time and space.

This chapter analyzes the changes in a country's employment protection laws between the mid-1990s and the present. While the time frame is largely determined by data availability, the decade leading up to the present has witnessed far-reaching changes in both economic and political spheres. Many have opened up their economies, though at different paces. Several rising economies experienced financial crises that wiped out years of progress, and even some of the advanced economies stagnated for years, unable to lower the long-term unemployment rates. The study asks how these various dynamics affect employment protection policies which are designed to protect the welfare of workers against the excessive power of employers and to insure workers against the risk of job loss and income insecurity (Lindauer 1999). What global trends do we see in the development of labor market institutions and what best explains these changes? Is labor market liberalization more likely in a globalizing economy, and if so, does that provide support for the efficiency hypothesis? What kind of role do domestic politics play in this process?

My argument is that globalization affects the relative power of workers negatively in their struggle to find accommodation on labor market institutions. Economic openness enhances producer mobility and their political leverage through the mechanization of production, the relocation of labor-intensive manufacturing to lower-cost neighbors, or the importation of cheaper labor from abroad. Also, the liberalization of trade and capital flows reduces various protective barriers, causing companies to strive for greater competitiveness and cost effectiveness. Thus, the pressures of international competition and the declining capacity to shift costs forward through mark-up pricing may combine to generate strong pressures toward greater labor market flexibility.

These dynamic shifts in power balance between business and labor, however, play out not in a political vacuum but in a policy context with established sets of labor market institutions. The policies that are already in place, *i.e.*, the status quo institutions, condition the political bargain between business and labor by shaping their policy preferences and circumscribing the range of available options and likely outcomes. For instance, where there is little employment protection, an increase in labor power prompts workers to bargain for more protection, raising the likelihood that there will be more employment protection. Where workers already enjoy substantial employment protection, however, a decline in labor power encourages employers to demand labor market flexibility. To overcome labor opposition, employers may compensate them by offering unemployment insurance (UI), reversing their traditional opposition to social policy commitments. Under this scenario, countries that adopt UI are more likely to reduce employment protection since they are better able to gain labor's support on market liberalization. This bargain, however, forces both employers and labor to settle for their second-best policy choice.

This chapter finds several empirical patterns. First, countries that initiate unemployment insurance (UI) are more likely to reduce overall employment protection, driven by the easing of rules on firing. Second, globalization, measured as changes in trade openness and inward flows of foreign direct investment (FDI), surprisingly does not have any discernable impact on employment protection. Third, the partisanship variable comes up insignificant in every model, which indicates that labor market liberalization is not any more or less likely under partisan dominance. Fourth, contrary to prevailing expectations, economic growth in general and growth in manufacturing in particular are associated with labor market liberalization. Lastly, the higher the initial level of employment protection in 1997, the more likely it is that there will be labor market liberalization in the following ten years.

Building on the existing theoretical and empirical literature discussed in Chapter 1, I proceed with a discussion of arguments put forth and a description of the data and the model I employ. Next, I present the results and their interpretations, leading to a discussion of important unanswered questions that call for further research.

2.1 Arguments and hypotheses

Employment protection legislations refer to a set of regulations that govern the hiring and firing process. It has the objective of protecting the welfare of employees by reducing their exposure to the unfair actions of employers and to the risk of fluctuating incomes, and can be provided through both labor legislation and collective bargaining (Riboud et al. 2002, OECD Employment Outlook 2004). Throughout Latin America, for instance, labor codes determine the types of contracts, the lengths of trial periods, and the conditions of part-time work (Heckman and Pagés 2004). Employment protection (EP) creates a zone of protection around existing jobs and income, limiting the severity of job and income loss in the face of economic shocks. These restrictions, however, are costly to employers; they compromise the employer's ability to control labor cost by imposing severance payments and other administrative costs.

In places where market competition is the operating principle, employers seek to maximize business profits and employees seek to maximize wages and benefits. In a competitive product and financial market environment, flexibility in the hiring and firing of labor aids the goal of profit maximization by allowing employers to better control operating costs. In contrast, where government protects these markets, employers need not be as sensitive to labor costs since they are more able to shift costs forward through mark-up pricing. When these protections disappear as part of the liberalization of trade and capital flows, employers or the management must find the means to enhance operational efficiency by raising productivity and lowering costs. With the phasing out of import-substitution industrialization policies in Latin America, for instance, there are greater pressures for public as well as private enterprises to operate more efficiently according to market principles. As a result, employers seek to enhance their ability to adjust the workforce through the liberalization of employment protection laws.

Labor, on the other hand, opposes efforts to increase labor market flexibility because they prefer job security to all else, including social security. This is because labor seeks to maximize income earned from work (wages, bonuses, and benefits) and, even if unemployment compensation is available, being out of work is a far inferior outcome for workers. Losing a job means lesser pay, fewer or no benefits, and a blow to one's sense of identity and security. Labor organizations fight hard against liberalization measures for these obvious and natural reasons. Thus, on the policy demand side, I argue that employers and labor hold opposing preferences. Employers want more flexibility and labor wants more restrictions.

For a policy outcome to materialize, demand must be met by supply. On the policy supply side, I build on the assumption that all politicians are office-seeking, and parties and politicians compete against one another to capture the support and votes of their core constituency as well as the median of the electorate. Thus, the conventional wisdom suggests that left governments pay more heed than right governments to the preferences of labor (and vice versa). The organizational capacity of interest groups matters as well—as evidenced by centralized and encompassing labor movements analyzed in the neocorporatist and class power literatures; the better organized they are, the more influence they are likely to exert over policies.

As such, the likelihood of labor market deregulation increases in the context of declining demand for industrial labor, since it reduces the organizational strength of labor and, in the long-run, the size of the electoral base from which left-leaning parties draw support. Globalization enhances producer mobility and their relative political leverage by enabling the mechanization of production, the relocation of labor-intensive manufacturing to lower-cost neighbors, or the importation of cheaper labor from abroad (Rodrik 1997).[15] In other words, globalization generates deregulatory pressures not only by shifting the relative power balance between business and labor in favor of business, but also by shaping and intensifying the actors' divergent interests.

Achieving labor market flexibility, however, requires a political bargain between business and labor, unless a government's hold on power is so dominant that it can ignore labor opposition without serious consequences. In most situations where labor market liberalization is desired, however, the status quo of a rigid labor market through extensive labor regulations was previously established through the strength of labor's political power, which likely means that labor preference cannot be entirely ignored in negotiations over labor policies.

Combining these insights, I argue that the choice of labor market institutions results from a political bargain between business and labor, a bargain that is conditioned

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[15] Foreign capital and international financial institutions have also intensified pressure to rationalize business operations, particularly in Asia in the wake of the East Asian financial crisis of 1997-98.

not only by labor power, but also by the existing set of labor market institutions. In other words, the policy status quo shapes the preferences of labor and business. Where there is little employment protection, an increase in labor power resulting from democratization, industrialization, or other labor-friendly developments, prompts workers to bargain for more protection, raising the likelihood that there will be more employment protection. Where workers already enjoy substantial employment protection, however, a decline in labor power combined with pressures for profitability—as caused by globalization, mechanization of production, or other factors—encourages employers to demand labor market flexibility. In an effort to realize labor market liberalization, employers can reverse their usual opposition to social policy commitments and offer unemployment insurance (UI) to cushion worker dislocation and loss of income.[16] Under this scenario, countries that adopt UI have a better chance of liberalizing their employment protection laws. This bargain or compromise, however, means that both employers and labor have to settle for their second-best policy choice, given that employers now pay higher social security taxes and workers face a more precarious employment environment. Moreover, a close partisan balance—and not partisan dominance—better facilitates such political compromise.

The availability of a social insurance instrument in the form of unemployment insurance has indeed facilitated the political support and rationale for introducing labor

[16] Moreover, for those who care about the stability of the workforce and their skills, UI is a more attractive alternative to accomplishing the goal of skill protection. Employers may support the development of social policy when programs such as UI allow them skill protection (Mares 2003).

market flexibility in several middle-income and developing countries. Expanding social policy has become a means to an end for labor market deregulation.

In response to the pressures of globalization, then, both compensation and rationalization (raising efficiency) take place. Governments liberalize the labor market to help make firms more competitive while compensating those who get laid off through social policy. The liberalization of labor markets in globalizing economies goes hand in hand with social policy development. This study probes these arguments by measuring the changes in the level of employment protection between the years 1997 and 2006, and testing them against globalization, social policy development, and political variables. Based on the theoretical considerations discussed above, I develop and test the following hypotheses:

Hypothesis 1: Countries with increasing trade and financial openness are also more likely to liberalize their labor market.

Hypothesis 2: Countries that adopt unemployment insurance programs are more likely to liberalize their labor market.

2.2 Data and measures

The focus of this analysis is on *changes* in employment protection laws, rather than on level. The employment protection data for 84 countries at two discrete points in time—the beginning of 1997 and 2006—come from two main sources, Botero et al. (2004) and the World Bank's *Doing Business* (2007). Employment protection laws govern the individual employment contract, including the alternatives to the standard employment contract, the termination of employment, and the cost associated with laying off workers, resulting in the following three subindices: (1) difficulty of hiring index (DHI); (2) difficulty of firing index (DFI); and (3) cost of firing index (CFI). The Appendix at the end of this chapter provides a detailed explanation of data sources and modified coding methodology.

The first subindex on hiring difficulty captures the strictness of protection against the use of alternative employment contracts, *i.e.*, part-time or temporary workers, which carry fewer benefits and bear lower termination costs. Modifying slightly the World Bank's *Doing Business* methodology, the difficulty of hiring index (DHI) measures (1) whether fixed term contracts are prohibited for permanent tasks, and (2) the maximum cumulative duration of fixed term contracts. A country is given a score of 1 if fixed term contracts are prohibited for permanent tasks and a score of 0 if they can be used for any task. For the duration, a score of 1 is assigned if the maximum cumulative duration of fixed term contracts—which includes renewals—is less than 3 years; 0.5 if it is 3 years or more but less than 5 years; and 0 if fixed term contracts can last 5 years or more. Averaging the two values and scaling the index to 100 gives each country their DHI score.

The second subindex measures the difficulty of firing redundant workers. Among the countries studied, three countries Bolivia, Egypt, and Venezuela prohibit redundancy layoff all together (*Doing Business* 2007). For the remaining countries, the index measures (1) whether the employer needs the approval of a third party to terminate one redundant worker; (2) whether the employer needs the approval of a third party to terminate a group of redundant workers; (3) whether the law requires the employer to reassign or retrain a worker before making the worker redundant; (4) whether priority rules apply for redundancies; and (5) whether priority rules apply for reemployment. For the 'yes' answers, a score of one is assigned; otherwise a score of zero is given. I assign heavier weight (3/10) to components (1) and (2) each, given that requiring an outsider's approval is more restrictive than prioritizing who should be let go and rehired. The third component on reassignment and retraining receives the weight of 2/10, and the remaining two components receive 1/10 each. Adding up the weighted scores and scaling the index to 100 gives each country their DFI score.

Lastly, the cost of firing index tries to capture the direct cost of termination arising from the notice period and severance pay requirements to a worker who has worked at the same company for three years. Measured in weeks of payment required by law, it ranges from a score of 0 weeks in the US to 39 weeks in Mozambique in 2006. Normalizing the data and scaling the index to 100 using the minimum (0) and maximum (39) gives each country their CFI score.

Table 2.1 lists the employment protection (EP) scores of the 84 countries in the sample for 1997 and 2006 from the highest to lowest scores in 1997. The third column indicates the difference between the two years. The fourth column indicates whether a country had an unemployment insurance (UI) program in 1995, and the fifth column shows whether there has been unemployment insurance (UI) program adoption, *i.e.*, an implementation of the program for the first time, between 1995 and 2006.[17] Countries that already had UI prior to 1995, as well as countries that did not have UI at the

[17] I include Korea and Armenia in the UI adoption category even though they adopted UI up to two years prior to 1997, given that countries may adopt UI in anticipation of labor market liberalization. No labor laws have changed in either country between 1995 and 1997.

beginning of 1995 and did not adopt the program in subsequent years are coded 0, while countries that adopted UI during this period are coded 1. Table 2.2 shows the three subindices that make up the overall employment protection index for each country for 1997 and 2006.

Table 2.3 shows the descriptive statistics of employment protection scores for 1997 and 2006, as well as the changes between those years. In 1997, New Zealand, the US, and Zambia together scored the lowest at 0, while Panama topped the chart at 77. The mean score was 32 with a standard deviation of 20. In 2006, the US was the sole standard bearer of labor market flexibility with the lowest score of 0, and at the other end Venezuela pushed the job security score to a new high of 95. The mean score was 34 with a standard deviation of 21. Between 1997 and 2006, the mean score went up by 2 points, reflecting a slight increase in protectiveness. Both the median and the mode of the change values are zero, which indicates that the most frequent change was in fact ‘no change’ and that there is an equal probability of countries undergoing changes in either direction. Georgia liberalized its employment laws most extensively between 1997 and 2006, moving from a score of 49 to 4, a decrease of 45 points. On the other hand, Morocco tightened its laws most extensively, moving from a score of 10 to 60, an increase of 50 points. Four other countries, Bolivia, Egypt, Latvia, and Venezuela, also made their laws more strict, all recording changes above 30 points. The majority of countries in the data set experienced relatively modest changes, the standard deviation of change being 16.

The key difference between the methodology used in this project from the widely used Doing Business data set is that the cost of firing is incorporated into the employment protection scores here—following Botero et al. (2004)—while the World Bank's Doing Business separates it out and instead includes the "rigidity of hours" index, which measures restrictions placed on workweek, working days, night work, weekly holiday work, and paid vacation days. Future iterations of the project will incorporate the rigidity of hours index.

Given this difference in scope, a discussion on the validity of these new measures of labor market policies is warranted. Table 2.4 gives summary statistics of the two measures in 2006, and Table 2.5 lists the top ten and the bottom ten cases in employment protection from the new data set and their corresponding Doing Business rigidity of employment scores. Along with a correlation score of 0.8582, it is evident that these two measures largely converge with each other. Venezuela, for instance, tops the chart in both data sets, and three other countries, Bolivia, Latvia, and Morocco, are also in the top ten most regulated in Doing Business. The other six countries in top ten also exhibit high scores on Doing Business—over 51 in all cases when the mean of Doing Business is 37.7. The case for similarity between these two data sets is even stronger when looking at the bottom ten least regulated economies. Seven countries show up in both lists and the other three also have low scores in Doing Business.

Panel data sets are useful for policy analysis and program evaluation. This two-period panel data, though limited in scope, is first of its kind and allows causal inferences to be made by modeling first differences. It also differences away time invariant variables, eliminating the need to include fixed effects in the model by controlling for unobserved effects. Also, labor laws do not change frequently as evidenced by the World Bank's Doing Business project. By extending the points of analysis to ten years apart from each other, this data set allows sufficient variation in the dependent variable.

Figures 2.1 to 2.3 illustrate the bivariate relationship between the dependent variable, *i.e.*, the change in employment protection, and an explanatory variable and other variables of interest. Figure 2.1 compares the mean value of the dependent variable in my 'treatment' group, *i.e.*, countries that experienced a change (adoption) in UI, with the mean value in my 'control' group, *i.e.*, countries that did not experience such a change. As the graph shows, countries that adopted UI between 1995 and 2006 experienced an average a decline of 6.8 points in employment protection.

Figure 2.2 and Figure 2.3 also demonstrate interesting patterns in changes in labor market policies. Looking at the changes in employment protection by national income, the lower middle-income countries (second quartile) increased employment protection the most, but this may be due to the fact that several of the largest positive changes in employment protection occurred in middle-income countries such as Venezuela and Egypt. Looking at the changes by region, Europe and the former Communist block of countries liberalized on average, while the Middle and North Africa region and the Sub-Saharan Africa region experienced an extensive rise in labor market regulation. This indicates that the slight movement towards more regulation—the increase of 2 points reported earlier—is driven by changes occurring in Africa.

Rather than estimating a standard cross-sectional relationship, the following equation explicitly considers how changes in the explanatory variables over time affect the change in the explained variable over the same period. Two of the control variables used in some of the models, however, are in a 'level' form as of 1997, the status quo *ante* in consideration. The reason for their inclusion is theoretical. An argument made in this dissertation states that the status quo policies or institutions shape actor preferences and the likelihood that there will be reform pressures. Where the labor market is already rigid, for instance, there will likely be a greater demand for liberalization, *ceteris paribus*, than where the labor market is already flexible. I account for this underlying pressure towards liberalization by controlling for the existing level of employment protection and union density, which partially reflects the existing level of labor power to resist such pressures. I discuss these and other control variables further below.

The baseline equation in first differences is:

$$\begin{aligned}\Delta \mathrm{EP}_i = {} & \beta_0 + \beta_1 \Delta \mathit{Trade\ Openness}_i + \beta_2 \Delta \mathit{Financial\ Openness}_i + \beta_3 \Delta \mathit{UI}_i \\ & + \beta_4 \Delta \mathit{Partisanship}_i + \beta_5 \Delta \mathit{Democracy}_i + \beta_6 \Delta \mathit{GDP\ growth}_i \\ & + \beta_7 \Delta \mathit{Manufacturing}_{,i} + \beta_8 \mathit{EPL}_{i,1997} + \beta_0 \mathit{Level\ of\ Development}_{i,1997} \\ & + \Delta \mu_i,\end{aligned}$$

where "Δ" denotes the change from t = 1 (1997) to t = 2 (2006), the βs are the parameter estimates, and μ represents the error term.

Change in employment protection is the dependent variable, in both aggregate and disaggregate (subindices) terms. A positive change reflects the strengthening of employment protection laws, leading to more regulations and a more rigid labor market. A negative change reflects the weakening of employment protection laws, resulting in fewer or less strict regulations and a more flexible labor market.

Globalization consists of trade openness and financial openness in the realm of foreign direct investment (FDI).[18] Trade openness is the sum of exports and imports of goods and services measured as a share of gross domestic product (Exports + Imports/GDP), and the change variable is derived by taking the difference between the average of trade openness between 1997 and 2006 and the average between 1987 and 1996. For instance, Argentina's average trade openness between 1987 and 1996 is 17, which increased to 32.1 between 1997 and 2006, producing a difference value of 15.1. Inward FDI as a percentage of GDP represents the other component of globalization and is calculated in the same manner as the trade openness variable.

The other key explanatory variable is the adoption of unemployment insurance. Most advanced industrialized countries first adopted UI in the pre-World War II period, starting with France in 1905. The spread of the program to countries in other regions was gradual, and by the end of 1980s there were a total of 38 UI programs in the world, 20 of them in OECD countries. With the end of communism came a rush towards social policy programs, resulting in a total of 23 new programs in former Communist and Soviet Union republics by the early 1990s. In this study, unemployment insurance adoption is a binary variable, coded 1 for countries that initiated UI between 1995 and 2006, and 0 otherwise. These countries include Korea (1995), Armenia (1996),

[18] A word of caution must be noted, however, on this narrow use of the concept of globalization. In most of the previous research discussed above, globalization is operationalized as trade openness, *i.e.*, the sum of exports and imports of goods and services measured as a share of gross domestic product (Exports + Imports/GDP). Unfortunately, trade openness measured in this manner fails to capture the true extent and nature of openness of a domestic economy to foreign competition. A country could be very highly involved in world economy in imports and exports without allowing imports to compete with domestic production.

Kyrgyzstan (1998), Taiwan (1999), Turkey (2000), Thailand (2004), and Kazakhstan (2005).[19]

In addition to globalization and the adoption of unemployment insurance, I test and control for the impact of the government's partisan identity on the changes in employment protection.[20] Previous studies have demonstrated the theoretical, and in some cases empirical, impact of partisanship and regime variables on government spending and labor market institutions.[21] Beck et al.'s Database of Political Institutions (2001) identifies the partisan identity of the executive party. For this analysis, the partisanship variable measures the percentage of years a left-leaning party was in power between 1997 and 2006 for the 2006 value, and between 1975 and 1996 for the 1997 value. Taking the difference between the two time periods produces the difference measure. A positive value indicates the strengthening of left's representational power in the present decade compared to the previous two decades, and vice versa. A value of zero indicates either that the same party or the party with the same partisan leaning has been in power continually since 1975, or that the same proportion of the years indicated has been governed by a party with the same partisan identity.

Democracy is conceived as the difference in the Polity score between 2006 and 1997, a variable derived from POLITY IV data published by the Center for Systemic

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[19] Countries may adopt UI in anticipation of labor market liberalization, in which case UI adoption precedes liberalization, or around the same time as part of a negotiated pact. Thus, I include Korea and Armenia in the UI adoption category even though they adopted UI up to two years prior to 1997. No labor laws have changed in either country between 1995 and 1997.

[20] Although power is a central concept in political science, it is also notoriously difficult, almost impossible, to measure directly. Power is unobserved unless exercised, and using the outcomes of power to measure power would be circular. To get around this empirical conundrum, I rely on a host of theoretically relevant variables to measure the influence of labor power on the outcomes of employment protection.

[21] As discussed earlier, however, the partisanship measure is not without concerns of circularity.

Peace. A positive change indicates the strengthening of democratic institutions, and a negative change the reverse. For example, Bolivia's polity score went from 9 in 1997 to 8 in 2006, recording a change of -1. Democracy enhances labor power by making it more likely that the median voter will be a worker, and by improving labor's ability to organize and act collectively. Particularly if labor was excluded from the power alignments in the pre-democratic era, political liberalization would lead to improved protections of all kind, including employment protections.[22]

Additional control variables include the following. First, the proposed answer argues that employers—who are thought to usually oppose such a scheme—support the initiation and expansion of social policy programs such as UI when they seek to liberalize highly regulated labor markets. UI is compensation offered for increasing the flexibility of hiring and firing procedures. The model thus controls for the initial level of employment protection with an expectation that higher rigidity generates liberalization pressures.

Second, I control for GDP growth, calculated as the decadal average in 1997-2006 and 1987-1996 periods. The expectation is that a growing economy can better accommodate compensatory policies and enable employers to manage competitive pressures from within and without. We expect to see less pressure for liberalization in a growing economy.

Third, I control for manufacturing value-added as a percentage of GDP, calculated as the difference between the average of 1997-2006 and 1990-1996. For

[22] On the other hand, as noted earlier, democratization stemming from the fall of Communism has reduced employment protection in those countries.

example, Indonesia's 1990-1996 average was 22.8 and its 1997-2006 average was 28, yielding a difference value of 5.2. Expansion in manufacturing is thought to increase the organizational power base of labor unions; thus it is used as a proxy for the waning or growing influence of unions on labor market policies.

Lastly, I account for the level of economic development, defined as the log of the Gross Domestic Product per capita in 1997. This and other 'level' variables as of 1997 are included to control for the possible differences in behavior according to the differences in the initial or the status quo level of employment protection and development.

I test six models with the overall change in employment protection as the dependent variable (Table 2.6) and with the subindices—the difficulty of hiring index (DHI), the difficulty of firing index (DFI), and the cost of firing index (CFI)—as the dependent variable (Tables 2.7 through 2.9). Models 1.1 and 1.2 test the impact of trade openness on employment protection, with the former being a first-differenced regression and the second an OLS regression that includes level variables. Models 2.1 and 2.2 test the impact of financial openness (inward FDI) on employment protection in the same manner as trade openness. Models 3.1 and 3.2 test the impact of UI adoption as the key causal variable on employment protection again using both the first-differences regression and OLS regression. I control for the common causes of UI adoption and the dependent variable (change in employment protection), particularly trade openness and FDI. By increasing market competition, trade and financial openness may generate political pressures from employers to liberalize the labor market while also facilitating the adoption of UI to smooth out the transition.

2.4 Findings and analysis

The regressions reported in Tables 2.6 through 2.9 yield five important findings: first, countries that newly adopt unemployment insurance (UI) are more likely to reduce the overall employment protection, driven by the easing of rules on firing. Second, globalization, measured as changes in trade openness and inward flows of foreign direct investment (FDI), surprisingly does not have any statistically significant impact on employment protection. Third, the partisanship variable comes up insignificant in every model, which indicates that labor market liberalization is not any more or less likely under partisan dominance. Fourth, contrary to prevailing expectations, the strengthening of democratic institutions has a negative impact on employment protection—on the cost of firing specifically. Also contradicting popular assessment, economic growth in general and growth in manufacturing in particular are associated with labor market liberalization. Lastly, among the level variables that are tested to show the impact of the status quo policy environment, the higher the initial level of employment protection in 1997, the more likely it is that there will be labor market liberalization in the following period.

First, countries that adopt UI are more likely to reduce the overall employment protections, driven by the relaxing of the rules on firing. The coefficients on the UI bivariate (dummy) variable in models 3.1 and 3.2 in Table 2.6 are significant at the 10% level if a one-sided test is used, and the coefficients on the UI bivariate (dummy) variable in models 3.1 and 3.2 in Table 2.8, which examine the changes in the difficulty of firing index (DFI), are significant at the 5% and 10% levels, respectively, in a twosided test. The coefficients indicate that adopting UI leads to a decline of approximately 12 points in the aggregate employment protection score, and of 29 points in DFI over time.[23] The result on the subindex of DFI is particularly interesting and robust, given that the statistically significant result does not depend on model specification. Moreover, the proposed explanation on the relationship between labor market liberalization and the adoption of UI is centered on the argument that employers prefer and demand flexibility in firing as they face competitive pressures and offer UI as a concession to labor. Thus, the statistically significant result on this particular subindex is particularly noteworthy.

Second, globalization, measured as changes in trade openness and inward flows of foreign direct investment (FDI), surprisingly does not have any statistically significant impact on employment protection—a result which fails to confirm Hypothesis 1 (*i.e.*, the study fails to reject the null hypothesis on the impact of globalization on employment protection). While there are concrete examples of countries switching from import substitution industrialization (ISI) to export-oriented industrialization (EOI) and in the process liberalizing their labor markets,[24] there does not appear to be a statistically significant relationship between increasing trade and financial openness and labor market liberalization in the short- to medium-run. This outcome calls for a more precise and rigorous theoretical investigation and empirical testing on what globalization means and what it entails.

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[23] The adoption of UI is not statistically significant on the other two subindices.

[24] Brazil, for instance, increased its average trade openness by 42 percent between the two periods, and it has reduced the employment protection score by 28.6, from 74.4 in 1997 to 45.9 in 2006, by eliminating the requirements for outside approvals for redundancy dismissal.

For instance, even when exports and imports may add up to a high percentage of GDP, this does not necessarily imply that the domestic economy is open and welcoming of foreign competition. Imports primarily consisting of raw materials, which are then turned into finished products for exports, are not a satisfying indicator of openness if those products are protected from competition from abroad. The domestic product markets of East Asian Newly Industrialization Countries (NICs), for instance, were closed off for a long time even as they aggressively expanded imports of raw materials and machinery and exports in finished goods. Workers in these countries were shielded from market competition and the governments had little trouble protecting the workers from market volatility.

The lack of significance in the FDI variable similarly calls for an investigation into the theoretical and empirical relationship between FDI as a measure of globalization and policy outcomes.[25] This failure to reject the null hypothesis that FDI does not matter is surprising and puzzling given the rich theoretical conjectures on the policy impact of mobile capital. The problem may lie with the way financial openness is operationalized in this and other studies, particularly pointing to the problem of over-generalization in using the FDI data. At minimum, the politics of FDI is another area in the study of globalization that demands a closer look.

Third, another notable and interesting outcome is the failure to reject the null hypothesis on partisanship; the coefficient is not statistically significant, indicating that partisanship of the executive did not affect the outcomes in a systematic manner. The

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[25] Avelino, Brown, and Hunter (2005) also find capital openness to be statistically insignificant on government spending.

coefficient, however, is surprisingly negative, *i.e.*, political domination by left-leaning (communist, socialist, social democratic, etc.) parties in the 1997-2006 period compared to the previous years raises the probability of deregulation, if statistically significant. The fact that left-leaning governments neither helped nor impeded the process of labor market liberalization, may suggest a political bargain between labor and business and between parties that champion their causes. We would predict bargains precisely where there is a close partisan balance, or where partisan alteration has no impact. If one side dominates, there is no need to bargain.

Fourth, economic growth and manufacturing growth are associated with weakening employment protection rules (Table 2.6). In particular, countries that experienced higher average growth rates in the 1997-2006 period compared to the 1987-1996 period liberalized the rules on firing (Table 2.8). These results are puzzling because we would expect workers to be better able to defend, if not enhance, general labor protections (including employment protections) in good economic times and under expanding manufacturing base through collective action.

A reverse causality may be at work, *i.e.*, labor market liberalization leads to economic and manufacturing growth, and not the other way around. Investor preference for a more flexible labor market environment may encourage governments to liberalize their labor markets, which then generates growth in manufacturing and economic expansion. Alternatively, governments and reformers may be better able to liberalize the labor market in a growing economy since the pain of liberalization is not felt immediately, producing weak resistance from labor. The first conjecture can be tested through a quantitative study, while the second conjecture would require a case-study approach. I plan to assess these findings in future iterations of this project.

Also contradicting popular assessment, the democracy term is negative and significant when assessing the changes in the cost of firing index (Table 2.7), indicating that the strengthening of democratic institutions or the deepening of democracy may have a short-term negative effect on cost of firing, a finding which contradicts the conjecture that democracy should increase employment protection by encouraging labor mobilization and political representation and also by making it more likely that the median voter will be a worker.[26] The study in Chapter 3 of this dissertation, for instance, finds that democratization has indeed played a significant role in strengthening employment protections in Indonesia and Thailand, while a lack of regime change or democratization in Singapore and Malaysia resulted in the maintenance of the policy status quo. Thus, the negative outcome in this quantitative study is surprising and puzzling.

A possible explanation is that the result may be driven by regime transitions that took place in the former Communist countries in the beginning of the 1990s, given that Communist regimes provided secure employment as part of their centrally planned economy even if they did not pay the workers well or help develop skills. Alternatively, the need for stability in labor relations for economic and security reasons in other types of authoritarian regimes meant that they did not necessarily treat their working citizens worse, and in fact produced extensive labor regulations that protected the core male

[26] Interestingly, however, more democracy produces less employment protection but more social spending (Avelino, Brown, and Hunter 2005)

laborers. I explore this conjecture in a case study on Korea in Chapter 4, where extensive employment protections developed in an authoritarian context and were subsequently dismantled by democratic governments.[27]

Lastly, among the level variables that are tested to show the impact of the status quo policy environment, the initial level of employment protection exhibits negative and statistically significant coefficients on employment protection rules, *i.e.*, higher levels of employment protection and union density at the starting period are associated with labor market liberalization in the following period. It is logical to expect that highly regulated labor markets face more opportunities or room for deregulation than markets that are already flexible. As argued earlier, the issue of employment protection is a policy priority for both business and labor. When the status quo become untenable due to the shifting power balance, the party whose power rises in relative terms pressures the other side to accept their preferred policy outcomes. In most situations where the change in policy involves deregulation, compensating labor is necessary to make the bargain possible and the new policy status quo stable. Business concedes and offers unemployment insurance—although theoretically it could be something else desired by labor—to gain labor's consent on their reform agendas. In other words, governments adopt unemployment insurance to aid the liberalization of employment protection regulations.

[27] Another possible explanation may be that a well-functioning democracy enhances interest mediation and representation, increasing the likelihood of the aforementioned policy compromise between labor and capital, which produces a more flexible labor market in exchange for social policy commitments.

2.5 Conclusion

Using the newly generated employment protection laws data for the years 1997 and 2006, this study tests whether the compensation or the efficiency hypothesis best describes changes in the labor market institutions in the present era of globalization. Unlike previous studies that analyze the government spending data, the focus of this study is on employment protection provisions, *i.e.*, rules that govern the hiring and firing procedures and restrictions. While trade and financial openness as measures of globalization are not directly found to be statistically significant in the regressions, the statistically and theoretically significant findings on the role of unemployment insurance on labor market liberalization warrant continued consideration of globalization as a factor in labor politics. It appears probable that both the efficiency and compensation arguments have merit in explaining the recent changes in employment protection laws, as governments that liberalize their labor markets tend to also adopt unemployment insurance programs to compensate those who lose out from liberalization. In other words, capital wins in one area (*i.e.*, employment protection regulations) but labor wins in another (*i.e.*, social policy of unemployment insurance), and this bargained outcome is most likely in a nonpartisan environment.

Thus, while globalization itself does not come up statistically significant in this study, its theoretical relevance cannot be dismissed given the significant findings on unemployment insurance and other variables. Globalization intensifies the influence of market principles such as efficiency and profitability on labor and possibly other corporate regulatory policies, even as it expands the governments' role in response to the challenges of economic integration through increased social programs and spending on social welfare. A policy tradeoff between labor market liberalization on the one hand and expansion of social insurance on the other may just be the political compromise between capital and labor that stabilizes and reinforces a government's commitment to international integration and openness. This dynamic is particularly pronounced when looking at the effect of UI adoption on the difficulty of firing index. Given the direct impact of easing the firing regulations on the incidence of layoff, it is not surprising to see such a strong connection between the two.

While this study is limited in the timeframe of the data, it is one of the first of its kind to investigate the impact of globalization on how countries change the laws that protect a worker's job security. There are several avenues for future research, some of which are taken up in the subsequent parts of my dissertation. First, extending the data on employment protection to previous decades would help clarify the trends in labor and social policy and further illuminate the causal impact of globalization, democratization, and partisanship on the development of labor market institutions. The World Bank's Doing Business project dates back only to 2003, and OECD's data on employment protection legislation is limited to its member states and to laws as of late 1980s. Developing more refined and comparable data on employment protection, labor unions, business associations, and the like, which extend beyond the developed countries would greatly aid a better understanding the politics of globalization. There is a great need for more in-depth case studies also, as they reveal the political logic or rationale behind these policy developments in a rich and nuanced way.

2.6 Appendix: Coding methodology for employment protection scores

The employment protection data for 84 countries at two discrete points in time—the beginning of 1997 and 2006—come from two main sources, Botero et al. (2004) and the World Bank's *Doing Business* (2007). Botero et al. (2004) has compiled an extensive set of information on the regulation of labor in 85 countries throughout the world, developing, among others, an Employment Laws index which "Measures the protection of labor and employment laws as the average of: (1) alternative employment contracts[28]; (2) cost of increasing hours worked[29]; (3) Cost of firing workers[30]; and (4) dismissal procedures[31]." Their methodology became the basis on which the World Bank's *Doing Business* project developed its Employing Workers index, which

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[28] "Measures the existence and cost of alternatives to the standard employment contract, computed as the average of: (1) a dummy variable equal to one if part-time workers enjoy the mandatory benefits of full-time workers; (2) a dummy variable equal to one if terminating part-time workers is at least as costly as terminating full time workers; (3) a dummy variable equal to one if fixed-term contracts are only allowed for fixed-term tasks; and (4) the normalized maximum duration of fixed-term contracts."

[29] "Measures the cost of increasing the number of hours worked. We start by calculating the 'maximum number of hours of work in a year before overtime' per year in each country (excluding overtime, vacations, holidays, etc.). Normal hours range from 1,758 in Denmark to 2,418 in Kenya. Then we assume that firms need to increase the hours worked by their employees from 1,758 to 2,418 hours during one year. A firm first increases the number of hours worked until it reaches the country's maximum normal hours of work, and then uses overtime. If existing employees are not allowed to increase the hours worked to 2,418 hours in a year, perhaps because overtime is capped, we assume the firm doubles its workforce and each worker is paid 1,758 hours, doubling the wage bill of the firm. The cost of increasing hours worked is computed as the ratio of the final wage bill to the initial one."

[30] "Measures the cost of firing 20 percent of the firm's workers (10% are fired for redundancy and 10% without cause). The cost of firing a worker is calculated as the sum of the notice period, severance pay, and any mandatory penalties established by law or mandatory collective agreements for a worker with three years of tenure with the firm. If dismissal is illegal, we set the cost of firing equal to the annual wage. The new wage bill incorporates the normal wage of the remaining workers and the cost of firing workers. The cost of firing workers is computed as the ratio of the new wage bill to the old one."

[31] "Measures worker protection granted by law or mandatory collective agreements against dismissal. It is the average of the following seven dummy variables which equal one: (1) if the employer must notify a third party before dismissing more than one worker; (2) if the employer needs the approval of a third party prior to dismissing more than one worker; (3) if the employer must notify a third party before dismissing one redundant worker; (4) if the employer needs the approval of a third party to dismiss one redundant worker; (5) if the employer must provide relocation or retraining alternatives for redundant employees prior to dismissal; (6) if there are priority rules applying to dismissal or lay-offs; and (7) if there are priority rules applying to re-employment."

comprises two separate parts: the rigidity of employment index and the firing cost. The rigidity of employment index is a simple average of the following three indices: (1) difficulty of hiring index (applicability and maximum duration of fixed-term contracts and minimum wage for trainee or first-time employee); (2) rigidity of hours index (scheduling of nonstandard work hours and annual paid leave); and (3) difficulty of firing index (notification and approval requirements for termination of a redundant worker or a group of redundant workers, obligation to reassign or retrain, and priority rules for redundancy and reemployment). The firing cost indicator measures the cost of advance notice requirements, severance payments, and penalties due when terminating a redundant worker expressed in weeks of salary.[32] The source information utilized to develop my two observation employment protection (EP) scores (or index) per country comes primarily from these two datasets.[33]

While these two datasets contain similar information, however, they are not directly comparable. For instance, the Botero index includes the cost of firing, while the World Bank index does not. Also, the information contained in the Botero index's "alternative employment contracts" is not identical to the information contained in the World Bank index's "difficulty of hiring index." In other words, while there are many

[32] See http://www.doingbusiness.org/MethodologySurveys/EmployingWorkers.aspx for the World Bank's detailed coding methodology. It relies on a detailed survey of employment regulations that is completed by local lawyers and public officials.

[33] As it is noted below, however, I have made some adjustments and collected new information to make these two datasets consistent and comparable. Also, I corrected the data where I found errors. For example, the Botero et al. data recorded that Indonesia required priority rules on re-employment following layoffs in 1997, but Caraway data (2007) suggest otherwise. Given that Caraway data is specific to East Asia and that she is considered an expert on Indonesian labor issues, I followed her coding and corrected my data accordingly.

overlapping components, their coding methodology differs significantly enough that these indices cannot be directly compared against each other.

To make the Botero et al. and World Bank data consistent for inter-temporal comparison, I have made the following adjustments.[34] First, the difficulty of hiring index (or what Botero et al. calls the "alternative employment contract") contains information only on the ability of companies to hire workers using non-standard contracts. My employment protection index omits the ratio of the minimum wage for a trainee or a first-time employee to the average value added per worker (included in the World Bank index) and also omits two questions concerning the mandatory benefits for and the costliness of terminating part-time workers (included in the Botero et al. data).

Second, the difficulty of firing index (or what Botero et al. calls the "dismissal procedures") replicates most of the key questions except whether the employer must notify a third party to dismiss one or a group of workers. The emphasis is instead placed on whether the employer needs the approval of a third party.

Third, I have omitted in its entirety the rigidity of hours index (or what Botero et al. calls the "cost of increasing hours worked"). The difference in their coding methodology on this subindex was significant, making it nearly impossible to cull any comparable information from the Botero et al. data. I left the task of incorporating the difficulty associated with increasing hours worked for future iterations of the project.

Lastly, I incorporated the cost of firing into the overall calculation of the employment protection score following the lead of Botero et al. Given that the Botero

[34] The Botero index is for labor laws as of 1997 and the World Bank index has annual data starting from 2004. I chose 2006 to compare against 1997 because the variation in the World Bank index between 2004 and 2006 was minimal and because a ten-year interval seemed straightforward.

index used three years of tenure and the World Bank index used twenty years for calculating the cost of firing, I adjusted the World Bank data to reflect the cost of an advance of notice and severance pay in weeks for a worker with three years of tenure with the firm.[35] I consulted the International Labour Organization's labor law database (including the Termination of Employment Legislation Digest), the Economist Intelligence Unit Country Commerce reports, the OECD Employment Outlook reports, and government websites to obtain the needed information.

These modifications have resulted in an employment protection index that assesses a country's employment laws that govern the individual employment contract, including the alternatives to the standard employment contract, the termination of employment, and the cost associated with laying off workers. The index comprises of the following three subindices: (1) difficulty of hiring index (DHI); (2) difficulty of firing index (DFI); and (3) cost of firing index (CFI).

First, the difficulty of hiring index (DHI) measures: (1) whether fixed-term contracts are prohibited for permanent tasks, and (2) the maximum cumulative duration of fixed-term contracts. A country is given a score of 1 if fixed-term contracts are prohibited for permanent tasks and a score of 0 if they can be used for any task. For the

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[35] For data comparability across economies, the World Bank uses the following assumptions about the worker and the business: the worker (1) is a 42-year-old, nonexecutive, full-time, male employee; (2) has worked at the same company for 20 years; (3) earns a salary plus benefits equal to the economy's average wage during the entire period of his employment; (4) is a lawful citizen who belongs to the same race and religion as the majority of the economy's population; (5) resides in the economy's largest business city; and (6) is not a member of a labor union, unless membership is mandatory. The business (1) is a limited liability company; (2) operates in the economy's largest business city; (3) is 100% domestically owned; (4) operates in the manufacturing sector; (5) has 201 employees; (6) is subject to collective bargaining agreements in economies where such agreements cover more than half the manufacturing sector and apply even to firms not party to them; and (7) abides by every law and regulation but does not grant workers more benefits than mandated by law, regulation, or (if applicable) collective bargaining agreement.

duration, a score of 1 is assigned if the maximum cumulative duration of fixed-term contracts—which includes renewals—is less than 3 years; 0.5 if it is 3 years or more but less than 5 years; and 0 if fixed term contracts can last 5 years or more. Averaging the two values and scaling the index to 100 gives each country their DHI score.

Second, the difficulty of firing index (DFI) measures (1) whether the employer needs the approval of a third party to terminate one redundant worker; (2) whether the employer needs the approval of a third party to terminate a group of redundant workers; (3) whether the law requires the employer to reassign or retrain a worker before making the worker redundant; (4) whether priority rules apply for redundancies; and (5) whether priority rules apply for reemployment. For "yes" answers a score of one is assigned; otherwise, a score of zero is given. I assign a heavier weight (3/10) to components (1) and (2) each, given that requiring an outsider's approval is more restrictive than prioritizing who should be let go and rehired. The third component on reassignment and retraining receives the weight of 2/10, and the remaining two components receive 1/10 each. Adding up the weighted scores and scaling the index to 100 gives each country their DFI score.

Lastly, the cost of firing index tries to capture the direct cost of termination arising from the notice period and severance pay requirements to a worker who has worked at the same company for three years. Measured in weeks of payment required by law, it ranges from a score of 0 weeks in the US to 39 weeks in Mozambique in 2006. Normalizing the data and scaling the index to 100 using the minimum (0) and maximum (39) gives each country their CFI score.

The employment protection score is calculated by averaging the three subindices, with a higher score reflecting greater rigidity or protection in the employment relationship. Taking the difference between the two observations—one for 1997 and another for 2006—for each country produces the change measure, for which we can obtain first-differenced estimators.

Table 2.1: Employment protection (EP) scores (1997 and 2006) and unemployment insurance (UI) adoption

EP scores: 0 to 100; countries are listed from highest to lowest EP in 1997.
UI present in 1995: countries that had UI at the beginning of 1995 are coded 1, 0 otherwise.
UI adoption: 0 indicates no change, 1 indicates program adoption between 1995 and 2006. Countries that adopted UI during the period are highlighted.

Country	EP 1997	EP 2006	EP change	UI present in 1995	UI adoption
Panama	77	69	-8	0	0
Mexico	75	49	-26	0	0
France	75	65	-10	1	0
Russia	70	45	-25	1	0
Brazil	68	48	-20	1	0
Tanzania	66	63	-3	0	0
Peru	63	50	-13	0	0
Venezuela	62	95	33	1	0
India	60	53	-7	1	0
Portugal	57	59	2	1	0
Spain	56	64	8	1	0
Vietnam	55	41	-14	0	0
Taiwan	54	50	-4	0	1
Mozambique	53	58	5	0	0
Kazakhstan	53	19	-34	0	1
Ukraine	51	61	10	1	0
Georgia	49	4	-45	0	0
Korea	48	28	-20	0	1
Croatia	48	49	1	1	0
Tunisia	46	50	4	1	0
Greece	46	44	-2	1	0
Kyrgyzstan	46	38	-8	0	1
Netherlands	45	42	-3	1	0
Pakistan	44	58	14	0	0
Finland	42	34	-8	1	0
Romania	42	32	-10	1	0
Madagascar	41	49	8	0	0
Italy	41	39	-2	1	0
Ecuador	40	55	15	1	0
Bolivia	39	81	42	0	0
Slovenia	39	47	8	1	0
Lebanon	38	37	-1	0	0
Turkey	38	42	4	0	1
Latvia	37	71	34	1	0
Norway	37	42	5	1	0
Sweden	37	29	-8	1	0
Slovakia	37	32	-5	1	0
Armenia	36	34	-2	0	1

Table 2.1: Employment protection (EP) scores (1997 and 2006) and unemployment insurance (UI) adoption (continued)

EP scores: 0 to 100; countries are listed from highest to lowest EP in 1997.
UI present in 1995: countries that had UI at the beginning of 1995 are coded 1, 0 otherwise.
UI adoption: 0 indicates no change, 1 indicates program adoption between 1995 and 2006. Countries that adopted UI during the period are highlighted.

Country	EP 1997	EP 2006	EP change	UI present in 1995	UI adoption
Jordan	35	24	-11	0	0
Chile	32	32	0	1	0
Philippines	32	32	0	0	0
Indonesia	31	56	25	0	0
Germany	30	36	6	1	0
Sri Lanka	30	27	-3	0	0
Argentina	29	32	3	1	0
Senegal	29	45	16	0	0
Uruguay	28	28	0	1	0
Belgium	27	3	-24	1	0
Burkina Faso	27	38	11	0	0
Lithuania	26	41	15	1	0
Mali	26	36	10	0	0
Czech Republic	25	42	17	1	0
China	25	25	0	1	0
Ghana	24	24	0	0	0
Uganda	24	4	-20	0	0
Kenya	22	12	-10	0	0
Japan	20	12	-8	1	0
Hungary	20	8	-12	1	0
Thailand	19	35	16	0	1
Bulgaria	15	32	17	1	0
Dominican Republic	15	31	16	0	0
Israel	14	18	4	1	0
Egypt	14	52	38	1	0
Ireland	13	31	18	1	0
Denmark	12	11	-1	1	0
Malaysia	11	11	0	0	0
Morocco	10	60	50	0	0
Poland	10	17	7	1	0
Zimbabwe	10	24	14	0	0
Colombia	10	17	7	1	0
Singapore	9	9	0	0	0
Canada	9	2	-7	1	0
Austria	9	16	7	1	0
Australia	8	2	-6	1	0
Mongolia	7	11	4	0	0

Table 2.1: Employment protection (EP) scores (1997 and 2006) and unemployment insurance (UI) adoption (continued)

EP scores: 0 to 100; countries are listed from highest to lowest EP in 1997.
UI present in 1995: countries that had UI at the beginning of 1995 are coded 1, 0 otherwise.
UI adoption: 0 indicates no change, 1 indicates program adoption between 1995 and 2006. Countries that adopted UI during the period are highlighted.

Country	**EP 1997**	**EP 2006**	**EP change**	**UI present in 1995**	**UI adoption**
Switzerland	7	7	0	1	0
Jamaica	7	7	0	0	0
South Africa	6	33	27	1	0
Nigeria	5	5	0	0	0
United Kingdom	4	4	0	1	0
Malawi	4	7	3	0	0
New Zealand	0	7	7	1	0
United States	0	0	0	1	0
Zambia	0	10	10	0	0

Source: Author's calculation for employment protection scores. Unemployment insurance (UI) adoption data are coded from *Social Security Programs Throughout the World*, published by Social Security Administration (SSA) and the International Social Security Association (ISSA).

Table 2.2: Employment protection (EP) scores subindices (1997 and 2006)

EP and subindices scores: 0 to 100; countries are listed from highest to lowest overall EP in 1997.

	1997				2006			
Country	**Diff. of Hiring Index (DHI)**	**Diff. of Firing Index (DFI)**	**Cost of Firing Index (CFI)**	**EP**	**Diff. of Hiring Index (DHI)**	**Diff. of Firing Index (DFI)**	**Cost of Firing Index (CFI)**	**EP**
Panama	100	80	50	77	100	80	26	69
Mexico	100	80	46	75	50	50	47	49
France	100	70	56	75	100	40	56	65
Russia	75	90	44	70	50	30	56	45
Brazil	100	60	45	68	100	0	45	48
Tanzania	75	70	53	66	100	70	18	63
Peru	75	70	45	63	50	100	0	50
Venezuela	100	0	85	62	100	100	85	95
India	50	80	50	60	50	80	28	53
Portugal	75	50	45	57	50	70	56	59
Spain	75	60	33	56	100	60	33	64
Vietnam	25	90	50	55	0	90	34	41
Taiwan	100	20	41	54	100	10	41	50
Mozambique	50	10	100	53	75	0	100	58
Kazakhstan	25	90	44	53	0	0	56	19
Ukraine	50	70	33	51	50	100	33	61
Georgia	25	90	33	49	0	0	11	4
Korea	0	100	44	48	0	40	44	28
Croatia	75	30	39	48	75	40	33	49
Tunisia	75	40	24	46	25	100	24	50
Greece	75	30	33	46	50	60	22	44
Kyrgyzstan	75	30	33	46	50	30	33	38
Netherlands	0	70	66	45	25	90	11	42
Pakistan	100	20	11	44	100	40	33	58
Finland	75	30	22	42	50	30	22	34
Romania	100	20	6	42	50	40	6	32
Madagascar	50	50	24	41	75	50	22	49
Italy	100	20	2	41	75	40	3	39
Ecuador	50	60	11	40	50	70	45	55
Bolivia	50	0	67	39	75	100	67	81
Slovenia	50	40	26	39	75	40	26	47
Lebanon	50	20	45	38	50	50	11	37
Turkey	50	10	54	38	50	30	45	42
Latvia	0	90	22	37	100	90	22	71

Table 2.2: Employment protection (EP) scores subindices (1997 and 2006) (continued)

EP and subindices scores: 0 to 100; countries are listed from highest to lowest overall EP in 1997.

Country	1997				2006			
	Diff. of Hiring Index (DHI)	Diff. of Hiring Index (DFI)	Cost of Firing Index (CFI)	EP	Diff. of Hiring Index (DHI)	Diff. of Hiring Index (DFI)	Cost of Firing Index (CFI)	EP
Norway	50	40	22	37	75	40	11	42
Sweden	50	40	22	37	25	40	22	29
Slovakia	25	30	56	37	25	50	22	32
Armenia	25	40	44	36	50	20	33	34
Jordan	50	10	45	35	0	60	11	24
Chile	50	0	45	32	50	0	45	32
Philippines	50	0	45	32	50	0	45	32
Indonesia	0	60	34	31	75	60	34	56
Germany	50	30	11	30	50	30	28	36
Sri Lanka	0	80	11	30	0	70	11	27
Argentina	50	10	28	29	50	0	45	32
Senegal	25	40	21	29	75	40	21	45
Uruguay	50	0	34	28	50	0	34	28
Belgium	50	0	32	27	0	0	10	3
Burkina Faso	50	30	0	27	75	40	0	38
Lithuania	25	10	44	26	50	30	44	41
Mali	50	10	18	26	50	40	18	36
Czech Republic	0	20	56	25	50	20	56	42
China	0	30	45	25	0	30	45	25
Ghana	0	60	11	24	0	60	11	24
Uganda	0	60	11	24	0	0	11	4
Kenya	0	40	27	22	0	10	27	12
Japan	50	0	11	20	25	0	11	12
Hungary	25	10	24	20	0	0	24	8
Thailand	0	0	56	19	50	0	56	35
Bulgaria	25	10	11	15	75	0	22	32
Dominican Rep	0	10	34	15	50	10	33	31
Israel	0	10	33	14	0	10	45	18
Egypt	0	30	11	14	0	100	56	52
Ireland	0	10	28	13	25	40	28	31
Denmark	0	20	16	12	0	0	34	11
Malaysia	0	0	32	11	0	0	32	11
Morocco	0	20	11	10	100	70	11	60
Poland	0	20	11	10	0	40	11	17
Zimbabwe	0	20	11	10	0	60	11	24
Colombia	0	30	0	10	0	30	22	17
Singapore	0	0	28	9	0	0	28	9
Canada	0	20	7	9	0	0	7	2
Austria	0	0	27	9	0	20	27	16
Australia	0	0	23	8	0	0	5	2

Table 2.2: Employment protection (EP) scores subindices (1997 and 2006) (continued)

EP and subindices scores: 0 to 100; countries are listed from highest to lowest overall EP in 1997.

Country	1997				2006			
	Diff. of Hiring Index (DHI)	**Diff. of Hiring Index (DFI)**	**Cost of Firing Index (CFI)**	**EP**	**Diff. of Hiring Index (DHI)**	**Diff. of Hiring Index (DFI)**	**Cost of Firing Index (CFI)**	**EP**
Mongolia	0	0	22	7	0	10	22	11
Switzerland	0	0	22	7	0	0	22	7
Jamaica	0	0	21	7	0	0	21	7
South Africa	0	0	18	6	50	30	18	33
Nigeria	0	10	5	5	0	10	5	5
United Kingdom	0	0	13	4	0	0	13	4
Malawi	0	0	11	4	0	10	11	7
New Zealand	0	0	0	0	0	20	0	7
United States	0	0	0	0	0	0	0	0
Zambia	0	0	0	0	0	20	11	10

Source: Author’s calculation for employment protection and subindices scores.

Table 2.3: Summary statistics of EP scores, 1997-2006

	1997				2006				Change			
	DHI	DFI	CFI	EP	DHI	DFI	CFI	EP	DHI	DFI	CFI	EP
Mean	35	31	30	32	38	35	28	34	4	4	-2	2
Median	25	20	28	31	50	30	25	33	0	0	0	0
Mode	0	0	11	37	0	0	11	32	0	0	0	0
Std Dev	35	30	20	20	35	32	19	21	29	31	23	16
Min	0	0	0	0	0	0	0	0	-50	-90	-53	-46
Max	100	100	100	77	100	100	100	95	100	100	89	50

Source: Author's calculation for employment protection (EP) scores.

Table 2.4: Summary statistics of EP scores and the World Bank's *Doing Business* Rigidity of Employment Index, 2006

	Mean	Std Dev	Min	Max
EP	34	21	0	95
Doing Business	38	18	0	76

Source: Author's calculation for employment protection (EP) scores, and the World Bank Doing Business 2007 (for data as of 2006).

Table 2.5: Comparison between EP scores and the World Bank's *Doing Business* Rigidity of Employment Index, 2006

Top ten (most regulated) in EP			Bottom ten (least regulated) in EP		
	EP	DB		EP	DB
Venezuela	95	76	United States	0	0
Bolivia	81	74	Australia	2	3
Latvia	71	59	Canada	2	4
Panama	69	56	Belgium	3	20
France	65	56	Georgia	4	7
Spain	64	63	Uganda	4	7
Tanzania	63	67	United Kingdom	4	14
Ukraine	61	55	Nigeria	5	21
Morocco	60	63	New Zealand	7	7
Portugal	59	51	Jamaica	7	4

Source: Author's calculation for employment protection (EP) scores, and the World Bank Doing Business 2007 (for data as of 2006).

Table 2.6: Regression Results for Change in the Overall Employment Protection Index

	(1.1)	(1.2)	(2.1)	(2.2)	(3.1)	(3.2)
Difference variables						
Unemployment insurance					**-11.75**	**-10.14**
					(7.45)	**(7.12)**
Trade openness	**0.03**	**0.04**			0.05	-0.01
	(0.11)	**(0.10)**			(0.11)	(0.10)
FDI			**-0.21**	**-0.19**	-0.37	-0.27
			(0.21)	**(0.21)**	(0.23)	(0.22)
Partisanship	-4.29	-2.70	-4.30	-2.81	-3.90	-3.83
	(5.52)	(5.58)	(5.45)	(5.52)	(5.46)	(5.32)
Democracy	-0.34	-0.48	-0.47	-0.60	-0.56	-0.70
	(0.44)	(0.45)	(0.44)	(0.45)	(0.46)	(0.44)
GDP growth	-0.86**	-0.95**	-0.92**	-1.00**	-0.86**	-0.65*
	(0.38)	(0.38)	(0.38)	(0.38)	(0.38)	(0.38)
Manufacturing	-1.03*	-1.06*	-0.98*	-1.00*	-0.95	-0.70
	(0.58)	(1.18)	(0.55)	(0.55)	(0.57)	(0.56)
Level variables (1997)						
Initial Level of EPL						-0.25***
						(0.09)
GDP/capita (logged)		-1.72		-1.58		-1.76
		(1.17)		(1.25)		(1.12)
Constant	1.85	15.72*	2.79	16.04*	3.40	26.00**
	(2.54)	(9.81)	(2.07)	(9.59)	(2.64)	(9.92)
Observations	80	80	81	81	80	80
Adjusted R^2	0.02	0.04	0.03	0.05	0.04	0.14

Standard errors in parentheses; *p<0.1; **p<0.05; ***p<0.01.

Table 2.7: Regression Results for the Difficulty of Hiring Index (DHI)

	(1.1)	(1.2)	(2.1)	(2.2)	(3.1)	(3.2)
Difference variables						
Unemployment insurance					**-5.83**	**-3.28**
					(14.43)	**(14.09)**
Trade openness	**0.04**	**0.06**			0.07	-0.02
	(0.20)	**(0.20)**			(0.20)	(0.20)
FDI			**-0.41**	**-0.37**	-0.51	-0.34
			(0.40)	**(0.40)**	(0.45)	(0.44)
Partisanship	0.18	2.95	0.14	2.65	-0.37	0.61
	(10.52)	(10.67)	(10.38)	(10.54)	(10.56)	(10.53)
Democracy	0.26	0.02	0.01	-0.20	0.00	-0.24
	(0.84)	(0.86)	(0.85)	(0.86)	(0.88)	(0.87)
GDP growth	-0.01	-0.17	-0.15	-0.29	-0.13	0.19
	(0.72)	(0.72)	(0.72)	(0.72)	(0.74)	(0.76)
Manufacturing	-0.40	-0.45	-0.32	-0.36	-0.37	0.02
	(1.10)	(1.10)	(1.05)	(1.05)	(1.11)	(1.10)
Level variables (1997)						
Initial Level of EPL						-0.39**
						(0.18)
GDP/capita (logged)		-2.99		-2.76		-2.95
		(2.25)		(2.21)		(2.21)
Constant	2.24	26.40	3.93	26.30	3.60	40.90**
	(4.84)	(18.75)	(3.94)	(18.33)	(5.11)	(19.62)
Observations	80	80	81	81	80	80
Adjusted R^2	-0.06	-0.05	0.13	-0.04	-0.07	-0.01

Standard errors in parentheses; *p<0.1; **p<0.05; ***p<0.01.

Table 2.8: Regression Results for the Difficulty of Firing Index (DFI)

	(1.1)	(1.2)	(2.1)	(2.2)	(3.1)	(3.2)
<u>Difference variables</u>						
Unemployment insurance					**-28.83****	**-28.24***
					(14.11)	**(14.31)**
Trade openness	**0.03**	**0.04**			0.06	0.03
	(0.20)	**(0.20)**			(0.20)	(0.21)
FDI			**-0.09**	**-0.07**	-0.46	-0.40
			(0.40)	**(0.41)**	(0.44)	(0.45)
Partisanship	-13.69	-12.35	-13.67	-12.26	-12.76	-12.00
	(10.49)	(10.74)	(10.44)	(10.68)	(10.35)	(10.70)
Democracy	-0.62	-0.74	-0.68	-0.80	-0.94	-1.07
	(0.84)	(0.87)	(0.85)	(0.87)	(0.86)	(0.89)
GDP growth	-2.53***	-2.60***	-2.52***	-2.59***	-2.34***	-2.28***
	(0.71)	(0.73)	(0.72)	(0.73)	(0.73)	(0.77)
Manufacturing	-2.19**	-2.22**	-2.14**	-2.16**	-1.97*	-1.86*
	(1.09)	(1.10)	(1.06)	(1.06)	(1.09)	(1.11)
<u>Level variables (1997)</u>						
Initial Level of EPL						-0.12
						(0.18)
GDP/capita (logged)		-1.46		-1.54		-1.62
		(2.26)		(2.24)		(2.25)
Constant	5.66	17.40	6.11	18.61	8.62*	25.66
	(4.82)	(18.88)	(3.97)	(18.58)	(5.00)	(19.93)
Observations	80	80	81	81	80	80
Adjusted R^2	0.11	0.10	0.10	0.10	0.13	0.12

Standard errors in parentheses; *p<0.1; **p<0.05; ***p<0.01.

Table 2.9: Regression Results for the Cost of Firing Index (CFI)

	(1.1)	(1.2)	(2.1)	(2.2)	(3.1)	(3.2)
Difference variables						
Unemployment insurance					**-1.47**	**0.24**
					(7.36)	**(7.17)**
Trade openness	**0.02**	**0.02**			0.03	-0.03
	(0.10)	**(0.10)**			(0.10)	(0.10)
FDI			**-0.15**	**-0.14**	-0.17	-0.09
			(0.20)	**(0.20)**	(0.23)	(0.22)
Partisanship	0.49	1.16	0.47	1.02	0.55	-0.25
	(5.34)	(5.47)	(5.29)	(5.41)	(5.40)	(5.36)
Democracy	-0.68	-0.74*	-0.78*	-0.83*	-0.77*	-0.84*
	(0.43)	(0.44)	(0.43)	(0.44)	(0.45)	(0.44)
GDP growth	-0.05	-0.09	-0.10	-0.13	-0.09	0.13
	(0.36)	(0.37)	(0.36)	(0.37)	(0.37)	(0.38)
Manufacturing	-0.53	-0.54	-0.49	-0.51	-0.52	-0.28
	(0.56)	(0.56)	(0.53)	(0.54)	(0.56)	(0.56)
Level variables (1997)						
Initial Level of EPL						-0.23**
						(0.09)
GDP/capita (logged)		-0.72		-0.60		-0.72
		(1.15)		(1.13)		(1.13)
Constant	-2.49	3.29	1.76	3.15	-2.07	11.59
	(2.45)	(9.60)	(2.00)	(9.41)	(2.61)	(9.99)
Observations	80	80	81	81	80	80
Adjusted R^2	-0.02	-0.03	-0.01	-0.02	-0.04	0.02

Standard errors in parentheses; *p<0.1; **p<0.05; ***p<0.01.

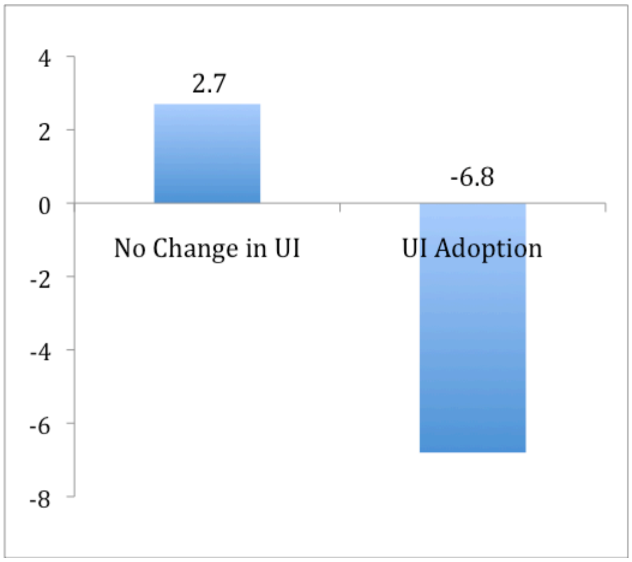

Figure 2.1: Average change in EP based on UI adoption

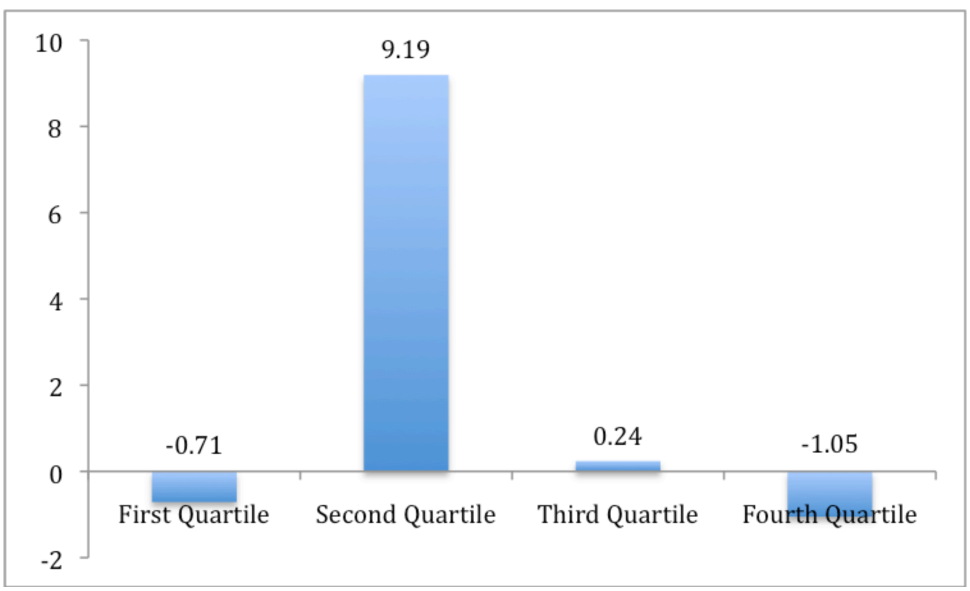

Figure 2.2: Average change in EP by income

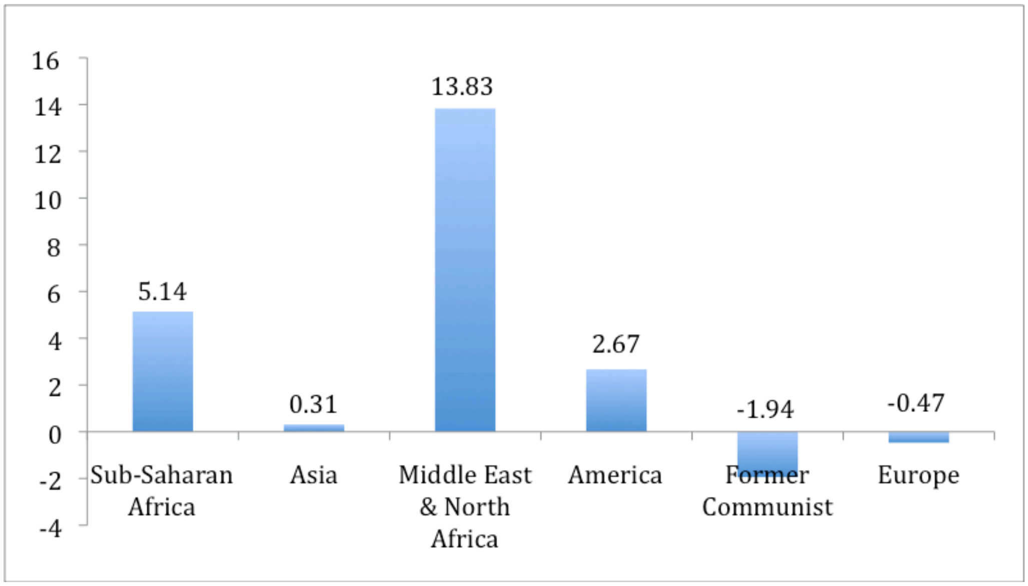

Figure 2.3: Average change in EPL by region

Chapter 3: Democratization and employment protection in East Asia

Employment protection legislation (EPL) does not change frequently or widely despite expectations by some that with globalization, there will be a 'race to the bottom' in labor regulations and protections. While greater trade and financial openness may generate competitive pressures on the labor market, factors that raise labor's political and economic bargaining power vis-à-vis employers can mitigate such pressures. Democratization, election of a left-leaning government, and tight labor markets are some of the more prominent of these factors.

I find that for East Asia, democratization stands out as the most significant causal factor behind the strengthening of EPL, and openness in trade and finance as a causal factor is largely subsumed under the authoritarian governments' export-oriented industrialization strategy.[36] Although the region as a whole has made steady and significant progress towards freer trade and investment flows since the 1960s and 1970s, the authoritarian governments' heavy-handed pursuit of import-substitution, followed by export-oriented industrialization meant that the control over trade, investment, and labor market policies also resided in the hands of the rulers. Governments established labor market policies, including employment protection laws,

[36] Although economic openness may not directly account for changes in EPL in East Asia over time, this does not suggest that the international investor community did not play any role at all. Singapore and Malaysia pursued foreign direct and financial investments in their domestic economies by establishing, in part, liberal labor regimes; and Indonesia's reform efforts in post-Suharto years eyed the approval of the International Labour Organization and other foreign audiences (Caraway 2004). The impact of foreign influences on domestic labor policies, however, seems to be greater under democratic settings. Indonesia's reform credentials to the international community mattered precisely because the new democratic government tried to distinguish itself from the authoritarian Suharto regime.

to support their chosen industrialization strategy. As long as authoritarian regimes stayed in power, economic openness did not exert any independent or notable pressure on employment protection policies. The impact of the East Asian financial crisis on EPL likewise depended on whether there was a regime change.

This chapter analyzes the impact of democratization on EPL by comparing Indonesia and Malaysia in a comparative case study, after briefly surveying four other East Asian countries (Korea, the Philippines, Thailand, and Singapore) and their history with EPL under increasing economic openness. I find that democratization in Indonesia, prompted by the financial crisis in 1997-98, raised Indonesian labor's political and organizational power, which they used to consolidate and enhance EPL in their favor through the 2003 Manpower Law. It further maintained the new rights against employer pressure to liberalize them in 2006 by staging mass strikes and disrupting business operations. Democratization similarly had positive causal impact on Thailand and Korea's EPL, although in the latter case EPL did not actually change after democratization because of the already high level of protection given to labor. Korea's authoritarian governments established strict EPL in favor of workers, which subsequent democratic regimes were unwilling or unable to dismantle until the East Asian financial crisis. I analyze the Korean case in depth in the following chapter.

Countries that maintained an authoritarian style of government (*e.g.*, Malaysia and Singapore), on the other hand, did not experience any changes in the type and level of employment protection provided to labor. The Malaysian authorities withstood democratization pressures during the height of the crisis, which in turn allowed the authoritarian (or semi-authoritarian) government to maintain its liberal labor market policies. Labor market policies in general and EPL in particular have not been a major political issue in either of these countries.

The Philippines, however, is an anomaly. Democratization did not enhance EPL in the Philippines even though there was potential for improvement given the moderate level of pre-democracy EPL (see Figure 1). The reason for this appears to be the structure of the Philippines economy, which is dominated by informal and service sectors (Ofreneo 1995, Bacungan and Ofreneo 2002). Throughout the 1980s and 1990s, employment in industry accounted for on average only 15% of total employment. In 2001, for instance, agriculture accounted for 37%, industry 16%, and services 47% of total employment (World Development Indicators). Its weak trade union movement is due to the small size of industry and manufacturing and not to any legal restrictions, which makes democratization less relevant as an explanatory variable.

This chapter proceeds with an explanation of the dependent variable (EPL), followed by an elaboration and analysis of the proposed explanatory variables (economic openness and democratization). An in-depth analysis of Indonesia and Malaysia follows, with an empirical focus on the change (or lack thereof) in labor power and its impact on the policy-making process.

3.1 The dependent variable: inter-temporal variation in employment protection legislation (EPL)

The analytic focus of this chapter is on inter-temporal variation in employment protection legislation (EPL) in East Asia between the mid-1980s (prior to democratization) and the present, as shown in Figure 3.1. I utilize the two-period panel

EPL data developed in Chapter 2 of this dissertation—which was extended to the 1980s through additional research—to show variation in EPL at three points in time—the mid-1980s, 1990s and 2000s—in Indonesia, Korea, Malaysia, the Philippines, Singapore, and Thailand.[37] EPL did not change in any of the countries between the mid-1980s (pre-democracy period) and 1997. Between 1997 and 2006, however, EPL increased in Indonesia and Thailand, it declined in Korea, and it remained the same in Malaysia, the Philippines, and Singapore. What accounts for these divergent developments in EPL? How are these laws and institutions significant to contemporary political economy in East Asia?

As discussed in Chapter 1 and 2, employment protection legislation (EPL) provides job security by limiting the freedom of employers in matters of hiring and firing. The OECD has developed the most extensive and detailed methodology for measuring the degree of flexibility or rigidity of labor markets in its Job Study and Employment Outlook (1994, 1999, 2004). The EPL index quantifies the strictness of the protection of existing jobs—or limitations placed on the employer's freedom to hire and fire—based primarily on labor legislation, while also trying to consider judicial practices and court interpretations of these rules. To provide detailed explanation of EPL in East Asia and highlight the specific contents and political significance of the laws that are the focus of this dissertation, I have constructed the EPL index for four non-OECD countries (Malaysia, the Philippines, Singapore, and Thailand) as of 2008

[37] Teri Caraway generously shared her inter-temporal data on individual labor rights, which allowed me to check and confirm the accuracy of data for the 1980s. She also calculated the severance pay rate for Indonesia as of 1986 for this chapter.

according to the OECD methodology.[38] This section proceeds with an explanation of the coding methodology and presentation of the new EPL data, which sets up the discussion on the inter-temporal variation in EPL since the 1980s leading up to the present.[39]

Employment protection is a composite index which aims "to reflect the cost implications of various regulatory provisions for employers," assessed according to eighteen elementary indicators covering three areas: 1) employment protection of individual workers with regular or permanent contracts against individual dismissal; 2) regulations of temporary forms of employment (fixed-term contracts and temporary work agencies); and 3) specific requirements for collective dismissals (OECD Employment Outlook 2004, 65).[40] Regular contracts do not generally specify the end date of the employment relationship, whereas temporary contracts establish the duration as well as the type of work at the outset of the relationship. Thus, particularly from the perspective of the employee, an abrupt end to a regular employment relationship ideally entails a justified or fair reason and some type of financial provision for the period of transition or unemployment that follows. When just causes or serious reasons are

[38] The OECD has already developed the EPL index for Korea (as of 2003) and Indonesia (as of 2006).
[39] The data was collected using each country's most current labor legislation obtained through official government sources, the International Labour Organization (ILO) employment laws database, and correspondences with local lawyers.
[40] Some of the regulatory components of EPL are readily available in quantitative form (*e.g.*, notice period in days or severance payment in months), while others are constructed from qualitative information (*e.g.*, difficulty of dismissal). Calculations follow a four-step procedure: first, convert the elementary information into cardinal scores ranging from 0 to 6 (higher is more strict); second, construct subindices within the three underlying areas by weighing and adding up the scores of the elementary indicators; third, construct indices for the three areas by weighing and adding up the subindices; and fourth, calculate the overall summary indicators by weighing and adding up the indices for the three areas, applying less weight on collective dismissal (2/12) than permanent and temporary contracts (5/12 each), given that regulations on the latter are considered primary for employment protection. The resulting cardinal indicators of EPL strictness range between 0 and 6, with 0 indicating the lowest and 6 the highest level of rigidity.

absent, the employee may desire an opportunity to challenge the layoff decision and seek compensation. Employment protection regulations thus establish legal parameters within which employers can hire and fire workers involving various types of contracts and working relationships.

Table 3.1 presents the overall EPL scores as of the mid-2000s[41] along with the breakdown (or subindices) for the six East Asian countries of interest. As it shows, Singapore has the lowest EPL score (1.0 on a scale of 0 to 6) and thus the least restrictive employment protection regime among the countries in this study, followed by Malaysia (1.4), the Philippines (1.4), Thailand (1.9), and Korea (2.0). Indonesia (2.8) has the highest EPL scores among the East Asian countries. The East Asian average is 1.8. In comparison, the OECD average is 2.1, the OECD emerging market country average is 2.4, the lowest EPL score among the OECD countries is 0.7 (the United States), and the highest is 3.9 (Luxembourg). This comparison of the means indicates that East Asia as a whole have established employment protection schemes that are on par with the average of advanced countries.

In analyzing the subindices or components of EPL, Singapore scores the lowest (indicating flexibility) with respect to the termination of regular or permanent contracts with a score of 1.5, while Indonesia scores the highest at 3.3.[42] The remaining countries score all similarly on this subindex with scores that range from 2.2 to 2.5. What these numbers represent is the strictness of the conditions under which it is possible for an

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[41] OECD's EPL data on Korea is as of 2003 and Indonesia is as of 2006; the EPL data on the remaining countries are as of 2008.

[42] Unlike temporary contracts, regular contracts do not generally specify the duration of the employment relationship.

employer to dismiss a regular employee under the protection of the law for "just causes" or "serious reasons"; the extent of the sanctions applicable to the employer for violation and recourse available to the dismissed employee;[43] and the generosity of required compensation through notice and severance pay provisions in case of fair dismissal.[44] In Indonesia's case, for instance, its high score is driven by procedural inconveniences, which require that the employer receive authorization from the government to initiate dismissal and wait in excess of 45 days to start the notice process.

In addition to regulating regular contracts, countries establish laws to protect temporary or fixed-term contract (FTC) employees by delineating the valid cases for use of FTC, the maximum number of successive FTC, and the maximum cumulated duration of successive FTC. In addition, some countries also regulate temporary work agency (TWA) in terms of the types of work permitted under TWA employment, the restrictions on number of renewals, and the maximum cumulated duration of TWA contracts. The underlying assumption here is that temporary jobs carry lower pay, fewer benefits, and fewer opportunities for learning and skills improvement. Thus, the goal of these regulations is to lower employers' incentive to substitute regular contracts with temporary work by limiting its use to legitimate cases and situations such as seasonal or

[43] Most countries maintain a mid-range difficulty of dismissal of workers with regular contracts (with scores of 3.0 to 3.5). This subindex includes a definition of justified or unfair dismissal, the length of trial period, compensation following unfair dismissal, and the possibility of reinstatement following unfair dismissal. In most cases, worker capability or redundancy of the job is an adequate and sufficient ground for dismissal, and the right to compensation or reinstatement following unfair dismissal is the standard rule and practice in East Asia. As for the length of trial period, Korea and Singapore do not officially regulate it, while Malaysia, the Philippines, and Thailand have set it at four to six months.

[44] In terms of the cost of firing associated with notice and severance pay for regular contracts, Singapore and Korea maintain the least restrictive legal requirements. In Singapore, for instance, the notice period is capped at 4 weeks for employees who have worked for more than 20 years, and it does not require any severance pay at all. In contrast, Thai law requires a minimum of one payment period—and up to three payments period—notice of termination, or payment in lieu of notice, resulting in the highest notice and severance pay score in the region at 3.4.

occasional activities. In East Asia, countries with strict rules on regular contracts tend to also regulate temporary contracts and work agencies. Singapore and Malaysia, for instance, score low on temporary contracts as they do on regular contracts, and Indonesia scores the highest in both categories.[45]

The last of the three subindices of EPL concerns collective dismissals. There are four components to this subindex: 1) additional requirements that define collective dismissal; 2) additional notification requirements to labor unions, works councils or employee representatives, and to government authorities; 3) additional delays for notice to start; and 4) additional severance pay requirements and obligatory social compensation plans, *e.g*., measures of reemployment, retraining, or outplacement. Of the countries in the East Asian sample, Singapore, Malaysia, and Indonesia have no additional requirements to what is already applicable to individual dismissal, while Korea has established specific guidelines that define collective dismissal as a percentage or number of employees based on the size of the firm. The employer also has to follow a specific procedure to carry out collective or redundancy layoffs, including notifying the government and labor unions of the plan and negotiating with affected employees.

The new EPL data presented here provides a detailed and comparative look into the current legal set-up of employment protection schemes in East Asia.[46] On one end of the spectrum is Singapore, which has established a liberal, business-friendly

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[45] Unlike FTC, regulating TWA employment is in its infancy in East Asia, with only Korea having any legal guidelines at all. The OECD reports that in Korea, at least in principle, TWA employment is allowed in only 26 occupations requiring professional knowledge, skills, or experiences (up to two years, renewable once). For temporary and intermittent cases, however, all occupations are allowed for up to three months, renewable once.

[46] Also see Edwards and Manning (2001).

employment protection regime that allows entrepreneurial freedom in the hiring and firing of workers. At the other end of the spectrum is Indonesia, which has established a more stringent, labor-friendly employment protection regime that limits such freedom on both regular and temporary contracts. Although the issue of collective dismissal is of lesser importance to most, a major exception is Korea, where both its symbolic and practical importance have produced detailed guidelines on the definition of collective dismissal and how freely employers are able to dismiss workers.[47]

Each of the six East Asian countries considered in this study has developed a customized set of employment protection schemes that reflects its unique political and economic history. The data on employment protections developed in Chapter 2 of this dissertation and graphically represented in Figure 3.1 shows that Singapore, Malaysia, and the Philippines have not changed their EPL since the 1980s (and only in minor aspects prior to the 1980s). Indonesia, Korea, and Thailand, on the other hand, experienced significant changes between 1997 and 2006, with Indonesia and Thailand strengthening the provisions (by 30 and 27 points, respectively) and Korea liberalizing them (by 29 points).[48] Indonesia and Thailand both instituted new rules on fixed-term contracts and raised the severance pay through new laws—the Manpower Law 13/2003 for Indonesia and the Labor Protection Act in 1998 for Thailand. Korea liberalized the rules that once required outside approval for layoff in 1998, legalizing redundancy or collective layoffs for the first time in its modern history. What explains these inter-

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[47] The issue of collective dismissal was at the center of the bitter political battle between business and labor over the direction of labor market liberalization before and during the financial crisis of 1997-98.

[48] The coding methodology used for the two-period data is much simpler than the OECD EPL methodology that was used to code the cross-national data. The OECD EPL scores range from 0 to 6, while the two-period data range from 0 to 100. See Chapter 2 for the details on the coding methodology.

temporal changes in EPL? Under what conditions are countries more likely to strengthen or liberalize their employment protection regimes? What, on the other hand, accounts for policy stasis in Malaysia, the Philippines, and Singapore? The following section explores possible explanations and assesses explanatory propositions by looking at the politics of globalization and democratization in two of the six East Asian countries in particular, Indonesia and Malaysia.[49]

3.2 Theoretical expectations on the determinants of EPL

One of the core arguments of this dissertation is that labor markets in general and employment protection provisions in particular are more likely to be liberalized when the relative bargaining power of business vis-à-vis labor increases. Employers generally prefer to keep the cost of operations low and the management of labor flexible, especially as competitive pressures rise in an open-market economy. Thus, globalization, or increased economic openness in trade and finance, is one such condition that makes labor market liberalization more likely. Chapter 2 of this dissertation explains the theory in depth.

Similarly, labor markets in general and employment protection provisions in particular are more likely to be strengthened (or *less* likely to be liberalized) when the relative bargaining power of labor vis-à-vis business increases. Labor prefers to institute as many protective measures as possible—both in collective, individual, and social security rights—in order to maximize their income from employment (wages and

[49] Korea is dealt separately in chapter 4, and the Philippines, Singapore, and Thailand will be analyzed in depth in future studies.

benefits) and from unemployment benefits if and when they are laid off. Democratization is one such condition that raises the likelihood of increased employment protection through labor's newfound electoral and organizational power, consolidated through unionization and expressed through mass demonstrations, lockouts, and picketing.

A key qualification to these general expectations has to do with the policy status quo, the status quo ante at the start of the relevant period or event of analysis. Labor market liberalization is more likely where labor markets are rigid already, since countries with a liberal labor market will not face the same level of pressure from employers to enhance flexibility. On the other hand, an increase in EPL is more likely where existing protections are minimal. An interesting twist to this proposition is that where labor markets are rigid, increased business power may be associated with not only labor market liberalization but also the initiation of unemployment insurance. In order to achieve greater flexibility and freedom in their hiring and firing practices, which labor opposes, employers may reverse their usual opposition to unemployment protection and offer it as a policy concession to labor in exchange for labor market flexibility.[50] I explore this dynamic in Chapter 4 of this dissertation as an in-depth case study on Korea.

Based on these theoretical considerations, I first investigate whether increasing trade and financial openness increases the likelihood of labor market liberalization by analyzing the experiences of Indonesia, Korea, Malaysia, the Philippines, Singapore,

[50] In these cases, business power is associated with both labor market liberalization and the expansion of social policy through the adoption or expansion of unemployment insurance.

and Thailand in the post-war period.[51] The second and main part of the chapter focuses on Indonesia and Malaysia in a comparative case study, exploring whether democratization increases the likelihood of stronger employment protections by empowering labor in the policy-making process.[52]

3.3 The impact of globalization on labor market liberalization

East Asia is famous for the region-wide progress it has made in economic growth through export-oriented industrialization (see Figure 3.2). Except for Singapore and Malaysia, which by the early 1960s had already integrated deeply into the global economy with total trade reaching 242% and 83% of GDP, respectively (as a five-year average; see Figure 3.3), the remaining East Asian countries in consideration here "globalized" since the 1960s and 1970s, recording significant growth particularly in the value of trade as a percentage of GDP and making conscious policy decisions to promote manufactured goods exports. Malaysia, for instance, doubled its trade value in less than 20 years between 1979 (102%) and 1998 (209%). Both the Philippines and Thailand doubled their trade values between 1986 and 1997/1998, going from 49% to 108% (the Philippines in 1997) and 102% (Thailand in 1998).

These changes in the total value of trade are driven by the policy shift from import-substitution industrialization or resource-based trade to export-oriented industrialization and manufactured goods-driven trade. In 1957, for instance, Malaysia's

[51] Hypothesis 1: Increasing trade and financial openness increases the likelihood of labor market liberalization.
[52] Hypothesis 2: Democratization increases the likelihood of stronger employment protections by empowering labor in the policy-making process.

export of tin and natural rubber accounted for a third of GDP (Burton et. al, 1993). Import substitution was its core industrialization strategy between 1950 and the 1970s, while also promoting the processing of natural resources to create industrial employment opportunities (World Bank 1993). Triggered by the 1969 ethnic conflicts, however, Malaysia launched the New Economic Policy (NEP) in 1971 to promote growth with equity. In addition to natural resource exports in rubber, timber, palm oil, and petroleum, the government promoted light manufactured exports in textiles, footwear, and garments through export incentives such as taxable income deductions linked to export performance and domestic input content, tax allowances for export-related promotional expenses, accelerated depreciation for firms exporting more than 20 percent of their output, guarantees and automatic rediscounting of export financing at low interest rates, and export-processing zones, free trade zones, and licensed manufacturing warehouses that permitted duty-free import of materials to be assembled or processed for export (World Bank 1993). Particularly with the enactment of the Promotion of Investments Act of 1986, the Malaysian government provided incentives for private investment in agriculture, industry, and tourism, reducing tariffs and liberalizing imports along the way.

In terms of the financial measure of globalization, FDI net inflows do not exhibit any consistent pattern over the years, other than that Singapore and Malaysia also lead in the area of FDI receipt in a cross-sectional comparison among East Asian countries (see Figure 3.4). The only notable pattern perhaps is that since the mid-1990s, FDI net inflows have decreased in all six countries.

What conclusions can be drawn based on trade and FDI patterns presented here? For East Asia, trade and financial openness does not carry strong explanatory power for the inter-temporal variance in EPL. None of the countries changed their EPL even as they opened up their economies to global trade and finance through the mid-1990s, *i.e.*, there is no variance in the dependent variable even though the variance in the independent variable is pronounced. The long-run, inter-temporal pattern of increasing openness in trade has not resulted in a region-wide rush to more flexible and liberal employment protection regimes.[53]

One seemingly obvious reason why this may be the case is that four of the six East Asian countries studied here—Malaysia, the Philippines, Singapore, and Thailand—have established generally flexible EPL to begin with, *i.e.*, their status quo EPL is low enough that there is not much room or need to liberalize further (see Figure 3.1). Policy changes are path-dependent, and rules established in earlier periods set the tone and scope of discussions on future reforms. Having already established flexible EPL, Singapore in particular and Malaysia and Thailand to a lesser extent, most likely did not face internal or external pressures towards further labor market liberalization. On the other hand, Korea in particular and Indonesia to a lesser extent likely faced greater pressures for liberalization given their relatively high status quo EPL through the mid-1990. Korea had established one of the most stringent rules on collective dismissal in East Asia during its developmental, authoritarian years, and Indonesia

[53] In terms of cross-national variation, however, an interesting pattern is discernable. Singapore and Malaysia, the two countries with a long history of trade and financial openness, have developed the more liberal employment protection regimes; whereas Korea and Indonesia, the two countries who were often the least open economies in the region, have developed the more restrictive employment protection regimes.

required government approval on layoff plans even if such rules were frequently violated under Suharto's authoritarian government. As it turned out, Korea liberalized its EPL in the aftermath of the financial crisis in 1998, while Indonesia strengthened its EPL in 2000 and 2003, making it costlier to lay off workers. What best explains this these divergent developments?

3.4 The impact of democratization on employment protections: a comparison of Indonesia and Malaysia

I argue that for East Asia, democratization stands out as the most significant causal factor behind the strengthening of EPL, and economic (trade and finance) openness as a causal factor is largely subsumed under the (authoritarian) government's export-oriented industrialization strategy. Although the region as a whole has made steady and significant progress towards freer trade and investment flows since the 1960s and 1970s, the authoritarian governments' heavy-handed pursuit of first import-substitution, and then export-oriented industrialization, meant that the control over trade, investment, and labor market policies also resided in the hands of the rulers. Governments established labor market policies, including employment protection laws, to support their chosen industrialization strategies. As long as the authoritarian regimes stayed in power, economic openness did not exert any notable pressure on employment protection policies. The impact of the East Asian financial crisis on EPL likewise depended on whether there was a regime change.

Prior to 1986, all of the East Asian countries in consideration here were autocracies or semi-autocracies with some façade of—or brief encounters with—

representative politics, whose polity score ranged from -8 (the Philippines) to 4 (Malaysia) in 1981 (See figure 3.5). After a wave of democratization in the 1980s and 1990s, with Indonesia joining the democracy club most recently in 1998, Malaysia and Singapore are presently the only semi-authoritarian countries with the polity score of 3 and -2, respectively. Thailand's recent descent into the autocracy territory with the 2006 military coup after 14 years of democratic politics is also a major exception to the general trend of democratization and democratic consolidation seen among the middle-income countries in East Asia.

An argument put forth here is that democratization increases the likelihood of policy reform towards stronger employment protections by empowering labor in the policy-making process. Given labor's preference for greater protection in collective, individual (*i.e.*, employment), and social security rights, any political development that tips the balance of power between business and labor in the latter's favor makes it more likely that labor-friendly policies will result. Such tipping of balance under democratization happens through the following two mechanisms: changed electoral incentives to respond to labor, and new freedom for labor to organize for strikes and militancy.[54] Labor's influence on political outcomes rises under democracy through its appeal as a large and identifiable voting constituency and through its newfound ability to stage large-scale public protests and demonstrations when sensitive political and legislative issues are at stake. With democratization and democratic consolidation, then, we expect to see greater protection of labor's rights and interests.

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[54] For democracy's positive impact on the welfare state and redistribution of wealth, see Meltzer and Richards (1981), Boix (1998), Brown and Hunter (1999), Grossman and Helpman (2002), Bueno de Mesquita, Smith, Siverson, and Morrow (2003), and Lake and Baum (2001).

In East Asia, there is strong evidence that this conjecture is plausible. In terms of the level of employment protection, the countries that democratized—Indonesia, Korea, the Philippines, and Thailand (until 2006)—are also the ones at the middle to higher end of the EPL spectrum (indicating less labor market flexibility) in East Asia. On the other hand, the two long-running semi-autocracies of Malaysia and Singapore are at the lower end of the EPL spectrum (indicating greater labor market flexibility). Even after instituting labor market liberalization measures in 1998, for instance, Korea still has one of the more stringent employment protection regimes in the region.[55]

The most salient evidence in favor of the conjecture that democratization leads to increased employment protection through the rise in labor power is found in Indonesia and Thailand. Indonesia, in particular, strengthened its EPL and other labor rights through the enactment of the Manpower Law in March of 2003 (Law 13, or 13/2003), which consolidated scores of outdated and overlapping legislation and decrees—including a 1997 law that had never been fully implemented—with a proposed intention of making the labor code more transparent, systematic, and balanced between the concerns of employers and trade unions. In contrast, where there has not been a regime change, *i.e.*, Malaysia and Singapore, there is continuity in employment protection and other labor policies (which also happen to be on the "liberal" or employer-friendly side). What is the causal significance of regime change (democratization, more specifically) in the politics of labor market liberalization or

[55] As it will be shown in Chapter 4, however, Korea developed stringent rules on EPL prior to democratization in 1987 during its developmental years. Democratization enhanced collective labor rights without affecting EPL positively or negatively.

increased protection? I explore this question through a comparative analysis of Indonesia and Malaysia.

3.4.1 Democratization and Indonesia's Manpower Law 13/2003

For Indonesia, the financial crisis played a key role in toppling the authoritarian Suharto government and setting a democratic 'reform' agenda that included improving protections to labor. Under democracy, labor was successful in their use of organizational power (and electoral power to a lesser extent) through mass demonstrations, strikes, and disruption of business operations to obtain and maintain favorable labor policies. In this section, I examine the causal impact of democratization on EPL and provide evidence of increased labor power by analyzing the content and legislative history of the Manpower Law.

The East Asian financial crisis, which began in Thailand in the summer of 1997, spread to Indonesia with a vengeance, resulting in the stunning investment reversal, a contraction in GDP of 13 percent in 1998, and a traumatic shakeout in the corporate and banking sectors with about half of Indonesia's 128 banks closing down (see Figure 3.6).[56] Leading up to the crisis the fundamentals of the Indonesian economy were considered sound, with moderate inflation, low current account deficits, stability in capital flows, a stable stock market, and an upward pressure on the rupiah. Despite problems such as nonperforming loans in the banking sector, extensive short-term borrowing from foreign lenders, artificially stabilized exchange rate, and most

[56] For a more detailed discussion of Indonesia and the financial crisis, see Hill 1999, Robinson and Rosser 1998, and Soesastro and Basri 1998.

prominently, pervasiveness of corruption and rent-seeking activities, the authoritarian and business-friendly Suharto government enjoyed a reputation for generally sound macroeconomic management and had demonstrated in the past that it is capable of rapidly undertaking far-reaching structural reforms (MacIntyre 2001).

Social unrest intensified over the course of the financial crisis, starting in small towns in Central and East Java which then spread to Sulawesi, West Java, and Sumatra in early 1998 (Suryadinata 2002). Protesting against the hike of food prices and basic commodities, university students in Java and the Outer Islands staged demonstrations demanding that the government introduce both economic and political reforms and that Suharto should resign. On May 1, substantive fuel and electricity subsidies were removed, sending the price of gasoline from Rp600 to Rp1,200 per liter. Food prices rose immediately, and in response, students in the Sumatran city of Medan rioted. While Suharto was out of the country in Cairo to attend the G-15 Summit of non-aligned leaders, large anti-Suharto demonstrations developed. Following the killing of four students from Trisakti, a private university in Jakarta, by the Army Special Forces, the unemployed, workers, the urban poor, gangsters, as well as intellectuals joined the students in massive demonstrations against the government. Thanks to a split in the military that boosted the standing of the moderate and anti-violence faction of General Wiranto and pressed by the defection of supporters such as fourteen cabinet ministers on May 20, Suharto resigned on May 21, opening the door to Indonesia's democratization.

Suharto's vice-president, B. J. Habibie, took over the presidency until October 1999, when Abdurrahman Wahid, a moderate Islamic cleric, was democratically elected to the office. After only 21 months in office, however, Abdurrahman was impeached on grounds of incompetence and replaced by his vice-president, Megawati Soekarnoputri in July 2001. It was during her presidency and under the leadership of pro-labor Manpower minister Jacob Nuwa Wea that the Manpower Law 13/2003 was enacted.[57]

The general assessment is that Indonesia's new Manpower Law 13/2003 has strengthened workers' bargaining power by recognizing their right to "legal, orderly and peaceful" strike, specifying minimum standards for working conditions, and setting clearer rules for severance and compensation payments, among other things.[58] Looking at the changes from the employers' perspective, however, the new law has significantly raised wage costs and reduced flexibility in the management of labor in Indonesia's formal sector (Manning and Roesad 2007). In particular, the articles related to employment protection have drawn criticism and negative responses from employers and investors, forcing the then-new Susilo Bambang Yudhoyono administration to consider revising the law within mere three years of its enactment in the spring of 2006.

The provisions of the Manpower Law that relate to EPL are dismissal procedures, severance pay, temporary work arrangements, and minimum wage entitlements.[59] As noted earlier, authorization for dismissal from the local Manpower Department (Institution for Settlement of Industrial Relations Disputes) is required, and

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[57] Bambang Widianto, Deputy for Poverty, Labour, and Small and Medium Enterprises in the Ministry of National Development Planning, recollected the enactment of the Manpower Law in the following way: "When we made Labour Law No. 13 in 2003, we were under the euphoria of democracy after a very repressive political system. Before the 1998 reforms movement, there was only one labour union in Indonesia. But by 2000, even 10 people in a company could come together to form a union and each company could have several unions" (*The Straits Times*, Marcy 4, 2006). He also noted that then-manpower minister Jacob Nuwa Wea, under whose leadership the 2003 law was passed, was a labor activist.

[58] See Manning (2006) for a general review of Indonesia's labor regulation.

[59] Minimum wage is not part of the EPL calculation.

even for violations of work rules, bargaining agreements, or the terms of individual contracts, employers must issue three warnings within six months of each other before applying for a dismissal authorization. Difficulty in terminating employment, however, is not new as the Ministry of Manpower Decree 363/1967 and Regulation 150/2000 had already established stringent rules concerning layoff because of the high unemployment rate. In addition to many legal restraints on firing a worker who has been employed continuously for three months, the worker could not be discharged without the approval of the Ministry of Manpower even if a production cutback is needed or the worker is found to be unfit. An agreement on severance pay also must be reached between employer and worker (the Economist Intelligence Unit (EIU) Country Commerce Indonesia 2003).[60]

Once layoffs are authorized, severance and long-term service payments are due when layoffs result from economic reasons, enterprise bankruptcy, voluntary separation following an enterprise takeover, minor offenses, retirement, death, disability, or chronic illness (Articles 156-72). The two exceptions are voluntary departure and dismissal stemming from major offenses, such as theft, violent behavior, drunkenness, etc.[61] While the standard severance pay is calculated as one month of salary per year of service (capped at nine months), it is doubled in the case of dismissals for economic

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[60] The 2004 EIU report under the heading "Termination of employment" further notes that, "A ruling issued in June 2000 mandates higher compensation for dismissed or resigning employees. The decree came about based on an agreement among labour unions, the Indonesian Employers Association (Apindo) and a number of private employers. Employers must obtain permission from the Ministry of Manpower and Transmigration in Jakarta before laying off more than ten workers, but they may go to a regional office if dismissing fewer." http://www.eiu.com/index.asp?layout=displayIssueArticle&issue_id=1376908737&article_id=986908898 (accessed October 16, 2009).

[61] Workers were entitled to a long-term service pay of up to 10 months of salary between 2000 and 2003, prior to the new Manpower Law.

reasons, retirement, death, or disability. Although the severance pay rates for workers employed fewer than five years remained constant—which is reflected in the data used in this study for using a tenure of three years as the basis for calculating the severance pay and notice periods—the long-term service pay has increased from 0 to 2 months for these workers with the new law, to 4 months for workers with a tenure of 10 years, and to 7 months for workers with a tenure of 20 years. Thus, if an employee who has worked for the same employer for 20 years gets laid off for economic reasons, such as efficiency increases or changes in the ownership of the firm, then he is now entitled to a combined 25 months of severance and long-term service pay.[62]

Lastly, the law limits flexible work arrangements, such as temporary work, FTC, and sub-contracting in order to promote the transition of short-term workers into the permanent workforce of a company. Temporary work is allowed for three months, which is the statutory duration of probation in long-term contracts. FTCs are limited to three years, comprising an initial two-year contract and a single one-year extension (Articles 59-60). Sub-contracting is also limited to three years and to non-core activities, one-off tasks, seasonal work, or jobs related to the introduction of new projects or products (Articles 64-6).[63] Despite the legal limitations, however, the use of short-term contract workers and outsourcing has in fact further increased since the passage of the law, and there is little evidence that the new law has achieved its goal of moving contract workers into permanent staff (World Bank 2006).

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[62] According to the laws in effect in 1996, this amount would have been 15 months, and for 2000, it would have been 21 months.

[63] Not discussed here are the minimum wage entitlements that contribute to the burden of severance pay, given that the OECD EPL calculations do not include minimum wages.

Domestic capital, as well as many in the international financial community, sees the new law as an impediment to investment and a source of stagnation on employment creation. For instance, the Economic Intelligence Unit's 2007 edition of *Country Commerce Indonesia* notes: "The present law promotes reassignment rather than dismissal of underperforming employees. As a result, it dampens the prospects for qualified job applicants and promotes hiring by referral since companies are less willing to take a chance on employees they do not already know. As it stands, the law is a severe impediment to increased investment" (60). Facing pressures from the business establishment and with concerns over the rate of formal sector job creation, the government prepared revisions to the Manpower Law in 2006 to relax regulations for dismissing workers, reduce the required amount of severance payments, and relax the rules on fixed labor contracts. Following labor disputes and demonstrations by the trade union movement in March and April 2006, however, the government backed out of its plan.

The question is then how the controversial Manpower Law 13/2003 was enacted in the first place and why the government was compelled to revise it within such a short period of time. This upward shift in EPL was in some ways unexpected since Indonesia's EPL was on the more stringent side to begin with—the status quo EPL prior to 2003 already heavily restricted the employers' freedom to adjust the workforce as needed. The theory proposed in this dissertation would suggest that the stringency of status quo EPL would make labor market liberalization more likely, *ceteris paribus*, but Indonesia in fact moved in the opposite direction.

The primary reason for this upward shift, I argue, lies in democratization and the subsequent rise in organized labor's organizational power (and to a much lesser and subtle extent, the electoral power). First, the Habibie administration, which took over the government after Suharto's fall, gave labor unions the legal right to collective action by first ratifying the International Labour Organization (ILO) Convention No. 87 on Freedom of Association and Protection of the Right to Organize in June 1998, in an attempt to bolster its reformist credentials to the international community and enhance the legitimacy of the new administration (Caraway 2004). The government then implemented the Trade Union Act 21/2000 in order to provide a legal framework to enforce the provisions of Convention No. 87, including freedom of association, the right to organize, and collective bargaining. Under the new law, groups of ten or more workers could form a union; business sectors could unionize; discrimination against union members and employer obstruction of unionization efforts would be sanctioned; and unions are designated as authorized bargaining agents. While the contribution of ILO and other international actors to the strengthening of collective rights is undeniable, the Indonesian government's responsiveness to both international and domestic interest groups stems from the context of democracy and the processes of protest, and to a lesser extent, electoral politics.

As a result, labor unions proliferated in "the reform era" since Suharto's fall in 1998, aided by a 1997 law that sanctioned strikes and a 1998 regulation that made it easier to register workers' organizations by eliminating numerical and other impediments (EIU Country Commerce Indonesia 2004).[64] Some 75 unions and dozens of other unofficial labor groups sprang up since the legislative changes, and the number of strikes jumped from 19 in 1989 to 273 in 2000 according to Ministry of Manpower and Transmigration, as protesters demanded better wages, rights, and benefits from their employers. Although the sheer number of unions by itself does not indicate greater bargaining power of labor, it nonetheless suggests a heightened level of organizing and activities that were not possible during the Suharto era.

Examples of increased labor power include a highly publicized strike in November 2001 at Semen Gresik, the state-owned cement company, when workers protested successfully against the government's planned sale of the entity to Cemex of Mexico (*Suara Merdeka*, December 5, 2001; *Kompas Cyber Media*, December 11, 2001). Then in February 2003, Dirgantara Indonesia, the ailing aircraft producer, faced violent demonstrations over plans to sack workers. Although more than 9,000 workers were initially laid off, some 4,000 were later reinstated with a salary cut of 25% (which caused more demonstrations in November 2003) (*The Jakarta Post*, July 15, August 20, and November 20, 2003). In September 2003, workers at Kaltim Prima Coal went on a three-week strike demanding a bonus following the sale of the company; the strike cost the company nearly US$0.5m a day and government nearly US$10m total. In the end, KPC's shareholders agreed to pay a so-called "goodwill payment" worth Rp 50 billion or about $6 million to all KPC workers (*The Jakarta Post*, September 4, September 18, and September 23, 2003). Many strikes in those years were not only violent, but unions

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[64] The Suharto government imposed peaceful labor relations by allowing only one government-sanctioned union, the All-Indonesian Workers Association (SPSI).

also got away with ignoring government regulations to give prior notice of any job actions. It is in this context of increased labor militancy that the Manpower Law was hammered out amongst labor, business, and government leaders.

Aiding labor's success in influencing the Manpower Law to its favor is the policy status quo, or more specifically, what the public and many in the new government perceived as the failure of the status quo (*i.e.*, Suharto's) economic and labor policies. Even though on paper Indonesia's EPL—even before KEP-150—favored workers, the sentiment in Indonesia during and after the crisis was that labor was exploited and deprived of basic rights and protection, and the crisis was brought on by greedy business and political elites, both domestic (Chinese-Indonesians in particular) and foreign (Chua 2003). For instance, Caraway (2004) documents the role of the Minister of Manpower, Bomer Pasaribu, who issued a little-noticed decree regulating dismissals (Ministerial Decree 150/2000, better known as Kep-150), which raised the long-service and severance pay obligations towards dismissed and resigning workers, even the workers found guilty of serious violations. As a Minister he conducted a study of Suharto's ministerial decrees and concluded that all 197 favored the government and employers. This perceived anti-labor status quo, combined with massive layoffs taking place in the wake of the financial crisis, prompted Pasaribu to issue a decree that enhanced employment protection to fill the void caused by the freezing of the 1997 labor law. Perceiving that the new Indonesian government is biased against capital and wary of Kep-150 and labor strikes, many foreign investors closed factories and shifted their investment out of the country and potential investors and buyers stayed away from Indonesia (*The Jakarta Post*, August 3, 2002).[65]

In this context, negotiations over what was to become the Manpower Law dragged on for two years, with employers, unions, and even foreign chambers of commerce strongly criticizing the draft legislation for disagreements over outsourcing, contract labor, strikes, layoffs, and severance pay (*The Jakarta Post*, July 4, 2002; September 25, 2002).[66] Employers opposed "provisions that would pay workers when they go on strike, allow jail time for employers who violate labour regulations, limit night work to 35 hours per week and require severance pay even when an employee quits,"[67] while unions opposed "a proposed cap on the minimum wage and limits on strike activities, and a provision establishing tribunals that would be charged with settling disputes between employees and employers" (EIU Country Commerce Indonesia 2003). In the end, however, major labor unions such as the Federation of All Indonesian Workers Union (SPSI) and Reform SPSI accepted the new law, even as some unions not involved in the negotiation continued to protest provisions such as the use of child labor, dismissal for committing crimes, etc. (*The Jakarta Post*, March 26, 2003).

In the end, the Manpower Act—endorsed by the House of Representatives on February 25 and became effective on March 25—was surprisingly favorable to workers despite employers' participation in the negotiation. Although employers gained stricter

[65] Between 1998 and 2003, Indonesia recorded an average FDI net inflow of negative 1.1 percent of GDP.
[66] See Caraway (2004) for details on the negotiation process.
[67] Secretary General of Apindo Hasanuddin Rahman complained that the severance payment of nine times the monthly salary was too high for employers as it was higher than the current payment of seven month's salary; the House in fact originally proposed 12 times the monthly salary (The Jakarta Post, February 26, 2003).

sanctions against illegally striking workers and the right to fire workers for serious violations without the dispute-resolution procedure and severance pay, they still had to receive permission for dismissal and layoffs that come with high severance and long-term service pay. Dismissal for serious violations can also be appealed to the dispute-resolution institution. While it was not a total loss, employers failed to roll back much of the employment protection provisions that trace their legal roots to the progressive Sukarno-era legislation, Kep-150, and other decrees. With the rise of labor's prominence and influence in the new democratic era, the government's labor-friendly leanings in reaction to the Suharto-era repression, and concerns over high unemployment since the financial crisis, Indonesia's EPL became even more strict with the new Manpower Law.

Although employers gave their eventual consent to the enactment of the new law through their peak organization Apindo (a branch of the chamber of commerce and industry), they began voicing concerns about the cost and burden of dismissing workers in 2005 as research on investment climate by University of Indonesia and the World Bank garnered attention (Manning and Roesad 2007). As a presidential candidate in 2004, Yudhoyono was seen as the candidate of business leaders and the financial markets and had pledged to boost Indonesia's feeble economy by cracking down on corruption, overhauling the unpredictable commercial courts, and wooing investors for job creation (*The Economist*, September 16, 2004; July 9, 2004).[68] Thus in early 2005,

[68] Yudhoyono became Indonesia's first directly-elected president on October 20, 2004 by winning a landslide victory (in the run-off election) against the incumbent, Megawati Soekarnoputri, despite the fact that a five-party coalition, accounting for 55% of seats in the House of Peoples' Representatives (DPR), backed Megawati.

the Ministry of Manpower began seeking comments from unions and employers on possible revisions, and in February 2006, the Coordinating Ministry of Economic Affairs issued the Investment Climate Reform Package that included proposed revisions of the Manpower Law with the goal of boosting private investment from both domestic and foreign sources.[69]

The proposed revisions to the Manpower Law included a significant reduction in severance pay rates (down from the maximum of 28 months to 13 months), the use of fixed-term contracts (FTCs) for all activities for up to five years (previously three years), and the use of outsourcing or subcontracting in all types of work and production (Manning and Roesad 2007). Employers have argued that the revisions are necessary to reinvigorate the sluggish economy and increase competitiveness with other countries in the region (*The Jakarta Post*, April 7, 2006). Djimanto, secretary-general of Apindo (the Employers Association of Indonesia), said that the proposed bill would “save this country from further degradation, to bring in more investment and create jobs” (*The Straits Times*, April 6, 2006).

The Confederation of the All-Indonesian Workers Union (KSPSI), the National Labor Union (SPN), the Federation of Democratic Workers and other unions quickly denounced the government's plan to revise law and began staging large-scale demonstrations in March 2006. Although tripartite negotiations on the bill were still underway, labor unions took to the street to protest the “impending review” of the law,

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[69] Speaking to European businesspeople, Coordinating Minister for the Economy Boediono said the government was reviewing the country's labor legislation to accommodate investor concerns, especially in the areas of severance pay and outsourcing (*The Jakarta Post*, February 23, 2006). Others in the government were also sympathetic to the concerns of employers, including Bambang Widianto, Deputy for Poverty, Labour, and Small and Medium Enterprises in the Ministry of National Development Planning, who said the changes were justified (*The Straits Times*, March 4, 2006).

reaching the height of protest in on April 4 and 5 with over 20,000 protesters marching to the presidential palace to demand a meeting with President Yudhoyono. Thousands of others held rallies in Surabaya in East Java, Bandung in West Java, and Medan in North Sumatra (*The Straits Times*, April 6, 2006).

Bowing to pressure, President Yudhoyono announced on April 8 that the government would sit down with labor unions and representatives of the business community in a three-party forum to seek a resolution to the crippling dispute over the draft of a new labor law (*The Jakarta Post*, April 8, 2006). It would also enlist five state universities to evaluate the current law and give their opinion to the tripartite forum. While he did not completely close the door on possible future revision, in essence the proposed draft was abandoned in its entirety and plans postponed indefinitely. Further weakening the momentum, in early June, the House of Representatives Speaker Agung Laksono—who was also the deputy chairman of Golkar, the nation's largest party with 129 seats in the House—requested that the government drop the plan to revise the 2003 labor law (*The Jakarta Post*, June 5, 2006). Finally in August 2006, the vice president Jusuf Kalla announced that there would be no revisions to the Manpower Law following the completion of an ‘independent’ report by a committee of experts (*Financial Times*, December 9, 2006).

Given that Yudhoyono’s cabinet was broadly reformist and that he was elected on a reformist agenda, it is all the more remarkable that he ended up dropping the labor law reform proposal so quickly. One explanation for this may be that he did not have large enough support base in the Parliament (DPR), which made it difficult to withstand labor opposition. Manning and Roesad (2007) suggest that there was not a strong commitment to labor market reform on the part of the president or within the economic team, reflected in the fact that the reform package was prepared in haste and the government lacked a clear strategy for pushing through a controversial policy change. What is indisputable is that the government backed down because of opposition from the union movement and their ability to disrupt business activities and cause significant financial losses to the business community through a series of massive rallies across the country.[70] Labor's enhanced power to act collectively under democracy was critical in swinging the policy outcome to its favor.

3.4.2 Malaysia's policy stasis

The inverse of the argument that democratization increases the likelihood of policy reform towards stronger employment protections by empowering labor in the policy-making process, is that without democratization and under autocracy, labor's relative bargaining power vis-à-vis employers or its influence on the government is likely to be weak. Under autocracy, labor's potential influence on policy as an identifiable voting block and its ability to stage mass demonstrations, strikes, and lockouts to press its political or economic agendas are curtailed. Without democratization, then, we expect to see either a stasis in employment protection policies or a weakening of existing rights given that labor's ability to defend its entitlements is relatively weak.

[70] Employers have claimed that workers who left their jobs to join demonstrations against the draft law in major cities on April 4 and 5 caused billions of rupiah in losses to businesses, with West Java's Apindo chairman Dedi Wijaya claiming, for instance, that 90 percent of 4,000 plants in West Java halted their operations due to the massive strikes with estimated losses of Rp 70 billion (US$7.7 million) (*The Jakarta Post*, April 9, 2006).

In autocracy, moreover, it is the will and preferences of the government or the ruling elites that prevail in terms of policy outcomes. Thus, the relevant question becomes: what kind of policy preference towards EPL did the East Asian authoritarian regimes have as they developed and consolidated the laws? What, if any, constraints did they face in instituting and maintaining their preferred policies?

For Malaysia, the overriding objective of its labor market policies, including EPL, has been to pursue racially-equitable economic growth and industrialization through government-led, private, and foreign investment, which required fostering harmonious and peaceful industrial-relations practices.[71] Without democracy and its usual guarantees of various collective rights, Malaysian labor has had only limited influence on policies that affect its interest and welfare, including employment protections (Kuruvilla and Arudsothy 1995).

During the 1977-80 period, for instance, the government relaxed labor laws or did not enforce existing ones—*e.g.*, it excluded unions from key industries and the export sector—as it focused on promoting foreign investment, which resulted in massive investment in the electronics sector by US and Japanese companies (Kuruvilla 1995). Following a second-wave push towards low-cost, labor-intensive EOI in 1987, FDI again grew dramatically. In 1989, total FDI in Malaysia exceeded US$1.86 billion, representing a 157% increase over the previous year and accounting for roughly 12% of GDP. In the first half of 1989, foreign enterprises accounted for 80% of the proposed

[71] The predominant concern in terms of the national economic policy has been tensions between the three dominant ethnic groups: the Malays (accounting for 50.4% of the population), the Chinese (23.7%), and Indians (7.1%) (based on census data from 2000 in CIA The World Factbook Malaysia: https://www.cia.gov/library/publications/the-world-factbook/geos/my.html).

equity investment in the country; 85% of these investments were in export-oriented industries, such as electronics, electrical products, textiles, and chemicals. Labor market policies had to accommodate the government's low-cost, labor-intensive EOI-strategy.

The central pieces of legislation governing employment protection in Malaysia are the 1955 Employment Act (EA)[72], the 1967 Industrial Relations Act (IRA), and the 1980 Employment (Termination and Lay-Off Benefits) Regulations.[73] The 1955 Employment Act, which applies to all persons engaged in manual work[74], limits hours of work and overtime, provides for a minimum number of annual holidays, and deals generally with working conditions. The 1967 Industrial Relations Act regulates the settlement of disputes among employers, employees, and their trade unions (including collective bargaining); and the Employment (Termination and Lay-off Benefits) Regulations of 1980, which fall under the Employment Act, stipulate compensation levels for employees who are laid off.

Terms of dismissal vary by region. In peninsular Malaysia, Sarawak, and Sabah, employment contracts must include a clause stating the procedures for termination by either party (sec. 10(2), EA).[75] Fixed-term contracts are permitted in Malaysia, and must be in writing, if concluded for a period exceeding one month (sec. 10 (1), EA). Where such a clause is absent, the 1955 Employment Act stipulates that four weeks' notice be

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[72] The EA predates Malaysia's independence from the UK in 1957.

[73] In addition, the common law, as developed by Industrial and Appeal Courts, is an important source of law, and collective agreements and individual contracts of service may also be additional sources of regulation (http://www.ilo.org/public/english/dialogue/ifpdial/info/termination/countries/index.htm).

[74] It includes artisans and apprentices, or in the operation and maintenance of transport vehicles; certain officers engaged in any ship registered in Malaysia; those persons supervising employees engaged in manual labour; and those, regardless of occupation, earning less than M$1,250 a month.

[75] Normally, one month's notice of dismissal or one month's salary must be given, unless a longer period is stipulated in an agreement. Either party, however, may end a contract without notice if an indemnity is paid equal to the amount of wages involved (EIU Country Commerce Malaysia 1997).

given for employment of under two years; six weeks for two to five years; and eight weeks for more than five years (sec. 12(2), EA).

In the case of redundancy and operational reasons, firms have every right to terminate the employment of workers, provided the requisite notice periods are complied with (sec. 12(3), EA). The courts have protected the employer's prerogative to retrench workers, provided the retrenchment decision is in good faith and not taken to victimize the employee (ILO).

Under the Employment (Termination and Lay-off Benefits) Regulations of 1980, the minimum redundancy benefit for dismissal are: ten days' wages for each year of service under two years, 15 days' wages per year of service between two and five years, and 20 days' wages for each additional year of service (sec. 6(1)). According to EIU's Country Commerce Malaysia, the normal policy is "last hired, first fired," with most companies attempting to rehire laid-off workers when hiring again, and some labor agreements give dismissed workers first claim to any new vacancies. If termination or dismissal is deemed unjustified, the Industrial Court may award either reinstatement or compensation (including one month's wages for every year of service). The ILO report notes that in practice, however, the courts has not often awarded reinstatement and has stated it will not order reinstatement if this would not be in the interests of industrial peace within the establishment (ILO, Termination of Employment).

Lastly, because Malaysia's labor legislation makes no distinction between part-time or temporary help and permanent staff, normal rules apply to part-time and temporary workers. The EIU Country Commerce report on Indonesia (2007) notes that case law, however, "makes a distinction between casual workers (defined as those who offer services at the job site each day and are paid on a daily basis) and permanent staff. Casual workers are not entitled to termination benefits, and the courts are unlikely to order reinstatement (although such workers still cannot be dismissed without due cause). A casual worker actually paid on a monthly basis may be deemed to be a regular employee and enjoy all the benefits of regular employment."[76]

Many consider these rules to favor employers over workers, particularly when industrial relations or collective labor rights issues are also considered (Parasuraman 2001, Todd and Peetz 2001). Malaysia's labor laws have supplied the Ministry of Human Resources officials and the director-general for trade unions the power to suspend unions, forbid strikes, unilaterally intervene in any labor conflict, invalidate strike ballots, regulate relations with international labour bodies, as well as prohibit high-ranking union leaders and their organizations from engaging in political activity (EIU Country Commerce Malaysia 1997).

The 1959 Trade Unions Act, for instance, confines membership in trade unions to employees within a particular trade, occupation, or industry, and requires all trade unions to be registered with the director-general for trade unions. In 1996, unionized employees represented 10% of the total labor force of about 8.2 million (see Table 4.2). There were a little more than 500 trade unions in Malaysia in 1996 (which rose to 642

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[76] EIU Country Commerce, "Human resources: Part-time and temporary help," eiu.com, June 27, 2007. http://www.eiu.com/index.asp?layout=displayIssueArticle&issue_id=631849848&article_id=441850029 (accessed October 16, 2009)

by 2007), the majority of which are in-house unions.[77] They may apply to form a federation of trade unions or become affiliated with the Malaysian Trade Unions Congress. In 1996, the country's three umbrella labor organizations include about 220 trade unions.

Any union organizing a strike must first obtain the consent of at least two-thirds of its membership by secret ballot, then give the director-general for trade unions fourteen days' notice of a vote to strike, and then wait seven days after the notification period to commence a strike. The time lapse allows the industrial relations department of the Ministry of Human Resources to intervene and encourage an amicable settlement through arbitration and conciliation. Combined with the fact that strikes and lockouts are restricted in certain essential services, such as emergency services, all this makes strikes rare in Malaysia (Table 4.2). Between 1996 and 2001, there was an average of 10.2 strikes per year, which came down to 1.6 between 2003 and 2007. While comparable data is unfortunately unavailable for Indonesia, Malaysia's numbers are on par with Thailand (an average of 7 strikes annually between 1998 and 2007) and are low in comparison to Korea (average of 246) and the Philippines (70) (ILO, LABORSTA Labour Statistics Database).

Industrial disputes (disputes referred to the Industrial Court), however, are on the rise. In 1996 and 1997, there were 552 and 463 industrial disputes, respectively; in 2004, however, the number reached a record high of 3,406, sharply up from the 1,085 cases in 2003. Out of the 3,406 cases in 2004, 1,788 disputes were settled, and 1,902

[77] The rest are national unions (*e.g.*, the Plantations Workers' Union, the National Union of Bank Employees, the Transport and General Workers' Union).

cases were awarded a total of M$23.9m. In 2005, the court settled 1,724 cases in the first three quarters, and 1,881 cases were awarded a total of M$20.9m. In 2007 and 2008, the Industrial Court arbitrated 2,349 cases and 1,964 cases, respectively; for both years, about half of the cases concerned employment termination following alleged misconduct (EIU Country Commerce Malaysia 1996-2008).

The rising incidence of industrial disputes against the backdrop of declining incidence of strikes suggests that workers prefer to act individually, rather than collectively, to protect their rights. While the general assessment is that Malaysian labor unions are well-organized, the legal limitations placed on their collective rights to act, organize nationally, and strike make the unions largely a bystander in labor policy making. Even when there are grievances, Malaysian unions have very limited options to voice their opinions.

For example, the Malaysian Trade Unions Congress (MTUC) filed a complaint in September 2003 with the International Labour Organization (ILO) against the government for denying the formation of unions in certain sectors, such as electronics. Despite being an ILO member, the Malaysian government has refused to recognize Convention 87 on the freedom of association and other ILO conventions. Although the ILO in June 2004 urged the Malaysian government to amend its legislation to bring the laws into full conformity with ‘freedom of association’ principles, the government has not acted on these recommendations as of mid-2009 since the ILO’s recommendations are non-binding. Without concrete political or economic incentive to act—such as electoral pressures—the Malaysian government is able to ignore the demands of trade unions since there is little, if any, cost in doing so. Given that the government’s priority is in maintaining industrial harmony and peace, it would not be in its interest to enhance labor's collective or individual rights beyond what has worked thus far.

The unions' limited role in policy-making was evident in the manner with which the Employment Act was amended in May 1998, which came into force in August of the same year. Although the amendments contain some provisions that favor employees—*e.g.*, requiring the retrenchment of foreign workers employed in the same jobs as locals before terminating the service of any of the locals, the most significant provision deals with enhancing employers' rights to flexible working practices in the area of organizing shift work—*i.e.*, employers can now request exemption from the requirement that shift workers must not work more than an eight-hour day or a 48-hour week. The amended Act also gives the power to the Minister of Human Resources to make regulations concerning part-time employees to potentially reduce the benefits they receive (*New Straits Times*, October 6, 1998).

Even though labor unions may have expressed their concerns and views behind the scenes, the only reported incidence of policy input from stakeholders came from the employers' associations regarding the proposed jail sentence for employers who flout provisions under the Employment Act 1995 (*New Straits Times*, March 23, 1998). The news article reported that although initially the amendments to the Act included a jail sentence of up to one year and a fine not exceeding RM10,000 for all offenses under the Act, the Ministry of Human Resources decided to drop the proposed jail sentence after considering inputs from the Ministry of International Trade and Industry (MITI), the Malaysian Employers Federation (MEF) and the Federation of Malaysian Manufacturers (FMM). MITI had said that a jail sentence would be "investor unfriendly" and would only frighten potential investors, and the FMM and MEF commented that no other country imposed jail sentence for offences under the Employment Act.

This episode is exemplary of the level of influence and access employers have on government policy-making in contrast to labor. Given that the government had long been more attentive to the preferences of employers and investors, a policy stasis is a natural and logical outcome when there is no fundamental shift in the regime type or enhanced competition in the political arena. While the underlying dynamics of policy change may have been present, the absence of democratic regime change in Malaysia has limited the influence of labor and forestalled the policy reform in their favor.

3.5 Conclusion

In East Asia, democratization or change in regime type registers as the more significant explanatory variable for EPL than globalization or economic crisis. The impact of economic openness and crisis on policies is more pronounced when business and labor can fight it out publically (*e.g.*, through demonstrations on the streets) or through elections. While "under the table" negotiations or bargains do happen even for authoritarian regimes (as in Korea where the authoritarian rulers provided employment protection as a concession to restricting collective rights), there is generally less bargaining that goes on in non-democratic settings.

Theoretically and empirically it is widely shown that labor power (*i.e.*, their organizational and political influence) rises when countries democratize. For Indonesia, the financial crisis played a key role in toppling the authoritarian Suharto government and setting a democratic ‘reform’ agenda, which resulted in improved employment protections favorable to labor. Unions and worker movements proliferated under democracy, impressing their newfound power upon government authorities when disputes arose over employment protection and other labor policies. Indonesia’s new democratic administrations accommodated most of labor demands in two rounds of negotiations over EPL in 2003 and 2006.

In Malaysia, however, the absence of regime change resulted in the lack of major policy revisions, especially with regards to labor and EPL. Malaysia has maintained a relatively flexible labor regime since their establishment in the earlier periods of state formation. The authoritarian government structure and its restrictive policies on unions and worker movements severely limit any public discussion or contestation of government policies. Without democratization, it is unlikely that there will be any major revision to existing labor regulations since labor’s power to influence policy-making through demonstrations, strikes, lock-outs, picketing, etc., or through voting will remain unchanged.

Table 3.1: Employment protection legislation (EPL): cross-national comparison, East Asia

Scores (0-6), countries are ranked from lowest to highest overall rigidity

	Termination of indefinite contracts						
	Procedure	Notices & severance pay	Difficulty of dismissal	Average	Temporary jobs	Collective dismissal	**Overall score**
Singapore (2008)	1.0	0.4	3.0	1.5	1.0	0.0	**1.0**
Malaysia (2008)	1.0	2.5	3.5	2.3	1.0	0.0	**1.4**
Philippines (2008)	1.8	2.2	3.3	2.4	0.3	1.5	**1.4**
Thailand (2008)	1.0	3.4	3.3	2.5	1.8	0.8	**1.9**
Korea (2003)	3.3	0.9	3.0	2.4	1.7	1.9	**2.0**
Indonesia (2007)	6.0	2.5	1.5	3.3	3.4	0.0	**2.8**

Source: OECD 2008 for Indonesia, OECD 2004 for Korea, and author's calculations for the rest.

Table 3.2: Industrial labor in Malaysia

Year	Union. Rate (%)	Workforce (in mil.)	No. of trade unions	No. of in-house unions	No. of members	No. of strikes	No. of workers involved	No. of industrial disputes
1996	10	8.2	516		728,246	9		552
1997	10	8.6	526		734,685	5		463
1998	10	8.9	532		739,636	12		
1999	8	9.3	537		725,322	11		1,097
2000			563		734,037	11		1,050
2001	8	9.6	578		784,881	13		1,056
2002	9	9.8	581	373	802,260			1,092
2003	8	10.3	581	381	803,879	2		1,085
2004	8	10.5	597	380	782,659	3	279	3,406
2005	8	10.9	621	390	761,160	0		1,859
2006	10	11.1	631		801,585	1	172	2,381
2007	10	11.4	642	407	803,462	2	79	2,349

Source: EIU Country Commerce: Malaysia & Ministry of Human Resources Malaysia, from the Malaysian Trade Union Congress website (http://www.mtuc.org.my/total_union.htm).

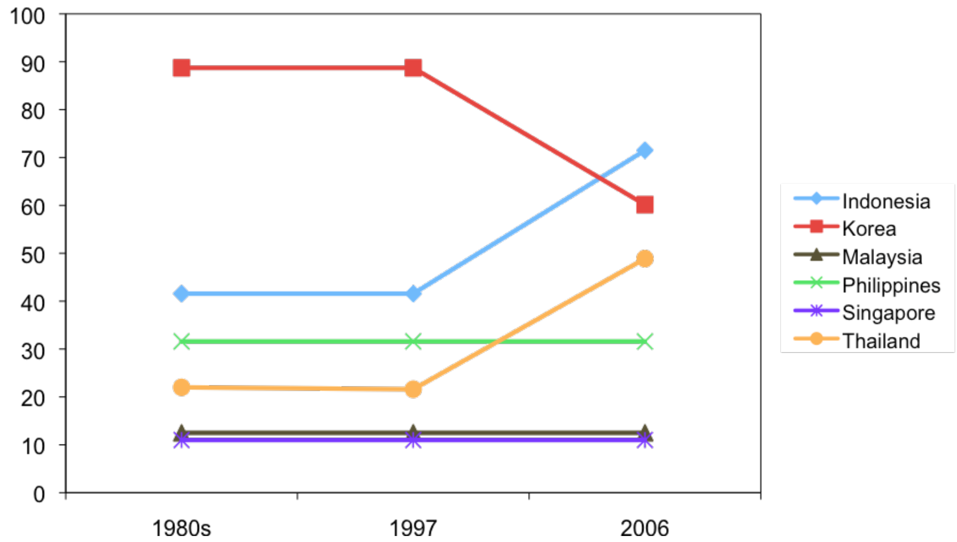

Figure 3.1: Variance in EPL over time: 1980s to 2006

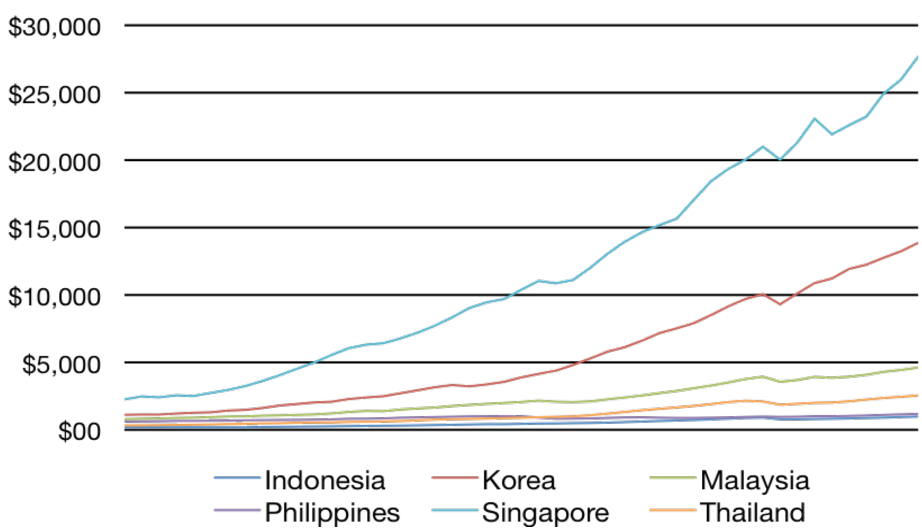

Figure 3.2: GDP per capita, 1960-2006

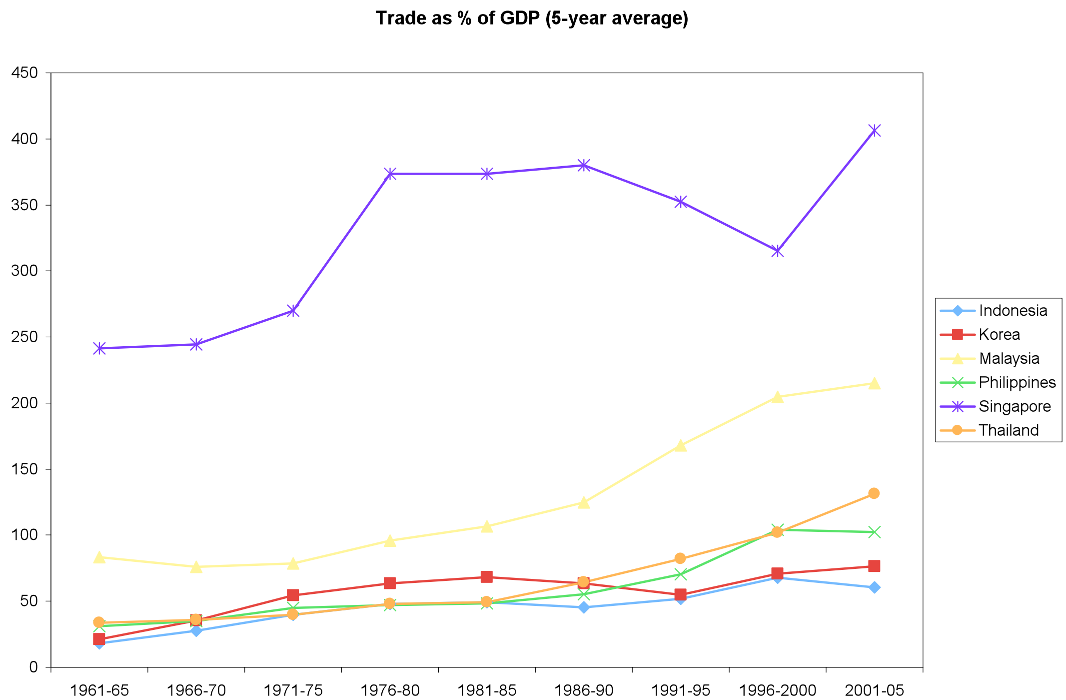

Figure 3.3: Trade as % of GDP (5-year average): 1961-2005

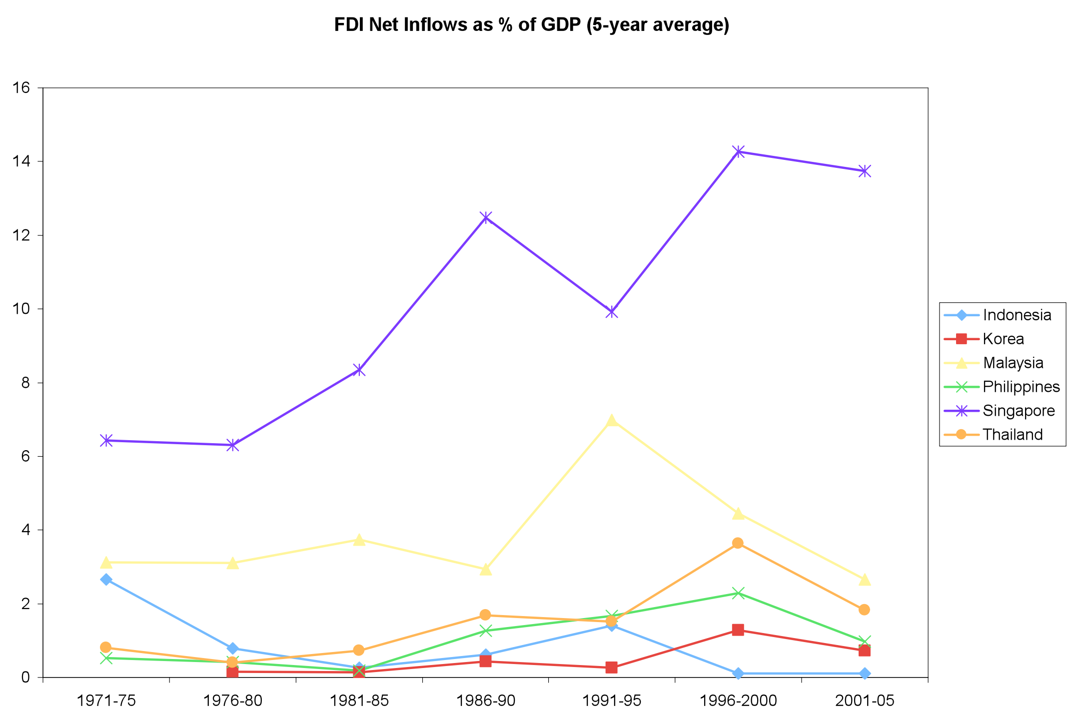

Figure 3.4: FDI net inflows as % of GDP (5-year average): 1971-2005

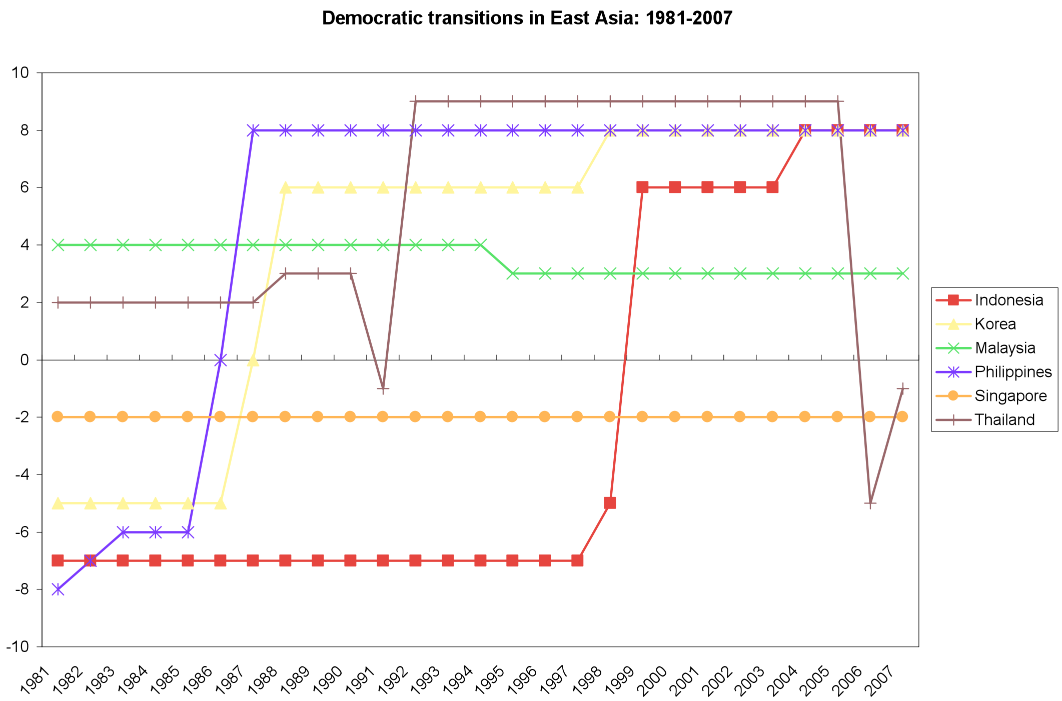

Figure 3.5: Democratic transitions in East Asia: 1981-2007

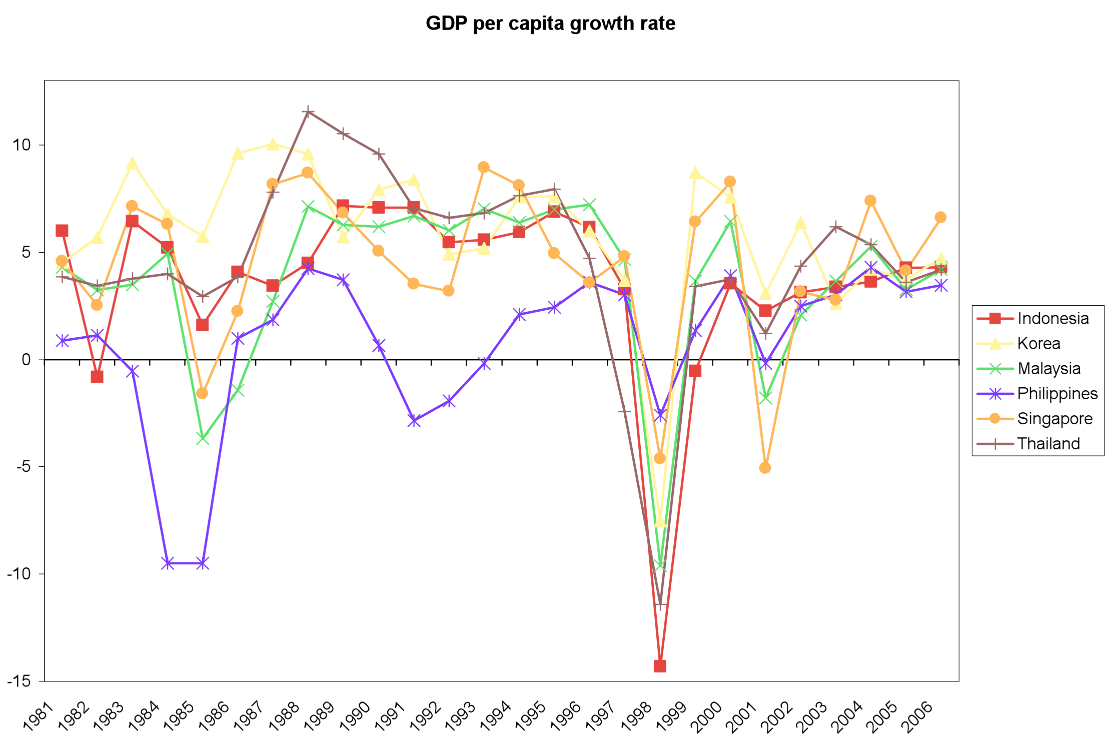

Figure 3.6: GDP per capita growth rate, 1981-2006

Chapter 4: Labor Market Liberalization and Social Policy Development: The Case of Korea

One of the core theoretical expectations of this dissertation is that the policy status quo shapes labor and business preferences by forcing them to prioritize their policy goals. In general, business prefers minimal employment and unemployment protection for cost reasons, while labor prefers maximal protection for income security. The policy preferences of labor and business take a surprising turn, however, when they struggle over the issue of liberalizing the labor market. Where stringent protections on employment constitute the policy status quo (*i.e*., the labor market is rigid), employers can support unemployment protection through unemployment insurance in order to gain greater freedom on employment protection. On the other hand, labor, reversing their usual support for the expansion of social insurance or welfare policies, may actually oppose unemployment insurance if it is offered as a means to secure greater labor market liberalization.

Also significant is a set of underlying factors that influence the bargaining conditions and process. Factors such as democratization, economic openness, competitive pressures, and economic conditions (*e.g.,* a financial crisis) change a group's relative political strength and the intensity of their preference, which raises the probability of policy reform. For instance, with democratization we would expect increasing labor strength and activism to make the development of social policies such as unemployment insurance more likely. With economic openness, however, the intensity of preferences for a more liberal labor regime and the relative bargaining power of employers are both likely to increase as they face greater competitive pressures and their cross-national mobility rises; economic openness, then, may make labor market liberalization more likely. Lastly, the prevailing economic conditions strengthen or weaken the bargaining position of one or the other by legitimizing one's demands and affecting one's capacity to comply. Demands for higher pay and greater protections, for instance, are more likely to be met under favorable business conditions.[78]

This chapter tells the story of how Korea first established restrictive labor market protections and developed practices of 'life-time employment' during the authoritarian, developmental era, and how this status quo labor regime at the time of democratization in the mid-1980s shaped the politics of labor in subsequent periods, including the dismantling of the prohibition against redundancy layoffs following the 1997-98 financial crisis.[79] A central and surprising feature underpinning Korea's remarkable growth and upgrading of its economic profile is that despite authoritarian rule that repressed collective actions by labor, the government and firms provided a stable employment relationship through strict rules on hiring and firing, *i.e.*, through

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[78] See Haggard and Kaufman (2008) for the application of this argument to welfare state development in Latin America, East Asia, and Eastern Europe countries.

[79] The story of the Republic of Korea's remarkable economic development is by now a familiar one (Amsden 1989, Haggard 1990, Song 1990). While protecting its domestic markets from foreign competition and capital, Korea adopted an export-oriented industrialization strategy, centered initially on light, labor-intensive products such as toys, clothing, and shoes. In the 1970s, the government pursued a heavy and chemical industrial drive that was more skill- and capital-intensive, focusing on petrochemical, automobile, shipbuilding, and electronics. Then from the 1980s, successes in high-tech, high-skill industries such as computer chips, cell phones, digital electronics, and biotechnology further enhanced Korea's position the global economy. For a critical assessment of Korea's development and its treatment of labor, see Ogle (1990). For state-labor relations and industrial relations, see Choi (1989), Koo (1993), Clifford (1994), Rhee and Chang (2002).

employment protection legislation (EPL). Collective dismissals were prohibited to keep the core (predominantly male) segment of labor stable, and large conglomerates (*chaebol*) did not demand the option of collective layoffs because corporate viability did not depend primarily on cost efficiency (Kim 2001). Moreover, the heavy and chemical industrialization (HCI) drive in the early 1970s increased the corporate demand for skilled labor, which was met primarily through on-the-job training and skill development that require longer-term employment commitment from both the workers and employers (Amsden 1989). As a result, the vicissitudes of business cycles did not affect the jobs of industrial and white-collar labor whose passive consent to the authoritarian rule and industrial policies was critical to the regime's claim to legitimacy.

Understanding the nature of the status quo labor institutions—employment protections as well as restrictions on labor rights—illuminates the fight over labor market liberalization that follows. The status quo shapes the policy preferences and priorities of key actors going forward as they face exogenous shocks such as democratization, economic openness, and financial crises (and economic conditions in general). These factors privilege and empower either business or labor in their struggle over social and labor policies.

This chapter finds that democratization in 1987, combined with favorable economic conditions, increased labor's bargaining power over employers, which it used to not only maintain the existing protections, but also to improve labor's collective rights, organizational capacity, as well as wages and working conditions. Democratization led to more organization, more militancy, and electoral incentives to respond to labor.[80]

Labor's continued militancy and its demands for higher wages and greater union-related political rights into the 1990s, however, prompted employers to begin demanding labor market liberalization, especially as they faced greater competition in the world market and diminishing government support domestically. In anticipation of and preparation for future labor market liberalization, the Kim Young Sam government enacted the unemployment insurance (UI) system in 1993 with the support of both labor and employers. Although the ascending power of labor, the program's electoral appeal, and the contributions and leadership by technocrats and bureaucrats took the credit for the success of UI, the program was designed specifically to help support a more flexible labor market, which both the conservative Kim government and employers expected to obtain in the near future. Employers gave their consent and support to the measure that raised business costs in return for the promise of managerial freedom over hiring and firing (*e.g.*, the use of contract workers, temporary work agencies, and redundancy layoffs).[81] For Korean employers, giving in on unemployment insurance was worth the price of gaining labor market flexibility.

The Kim government indeed delivered on its promise in December 1996 and passed a labor bill that legalized the redundancy layoff, but the law was soon repealed in the face of massive labor protests. The weakening bargaining power of labor vis-à-vis employers in the wake of the financial crisis in 1997-98, however—along with the

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[80] Partisan considerations, though, muted these incentives. The conservative ruling Democratic Justice Party and its candidate Roh Tae Woo appealed mostly to those with conservative leanings, such as rural voters, business elites, and voters from the Kyung-Sang (southeast) and Choong-Chung (central) areas.

[81] It is normally assumed that employers would oppose social and welfare policies that raise operating expenses.

pressures from outside in the form of the IMF rescue package and policy recommendations which also pushed strongly in the direction of labor market liberalization—compelled labor to compromise over these rigid labor laws on employment protections, while receiving in return employer consent to expand unemployment insurance and other compensatory programs, and to legalize various political rights of the unions. Although labor still had enough bargaining power to extract important concessions, it lost what it prized the most—employment protections and job security. Dissatisfied with the compromise, the more radical camp of labor (the Korean Confederation of Trade Unions) later denounced the tripartite agreement and walked away from the bargaining table.

In the end, what we see in Korea is a substitutive relationship or policy complementarity between labor policy on the one hand (*i.e.*, employment protection legislation) and social policy on the other (*i.e.*, unemployment insurance). Korea's advancement towards a welfare state was achieved at the expense of protections on employment, which for at least two decades prior defined Korean industrial relations. Social protection remains a second-best option for labor, making the issue of employment security foremost among the causes of dispute between labor and capital in Korea (see Figure 1 for trends in labor disputes).

This chapter proceeds with a look into the establishment of Korea's labor market institutions under authoritarian regimes, followed by an in-depth investigation of the theoretical expectations outlined above. I examine three episodes of labor-management conflict over protections, chosen according to variance in the three key explanatory variables of democratization, economic openness, and financial crisis (see Table 1 for a summary description of the three cases). The cases are designed to show their causal impact on labor market policies in general and employment protections in particular, and the mechanisms through which they shape policy outcomes. I then conclude by discussing directions for future research.

4.1 Modern foundations of Korea's employment protection: 1945-1980

In Korea's experience with labor market liberalization, the policy status quo played a key role in influencing labor and business views and priorities. Over the course of industrialization, Korea developed a practice of 'lifetime employment' for at least the core male workers in larger firms under legislative protections against dismissal since Korean businesses sought to retain skilled workers and had the financial capacity to absorb labor costs at the time. Moreover, these protections were considered fair compensation for workers who made sacrifices in working long hours for low pay, as well as a necessary condition for regime stability in advancing the goals of national development and industrialization. Korea's authoritarian governments sought to dampen labor unrest through these protections even over business protests. In this section, I endeavor to track the origins of the laws and practices of lifetime employment in Korea during the authoritarian Syngman Rhee (1948-1960) and Park Chung Hee (1961-1979) regimes.

At the time of liberation from Japan in 1945, Korea lacked national capital or a class of business managers or entrepreneurs, which in fact caused over 80 percent of the nation's industry to halt entirely upon the departure of the Japanese managers. In contrast, the General Council of Korean Trade Unions (*Chosun Nodong Chohap* *chunkook Pyonguihwae, or Chun-Pyung*), Korea's first labor union formed by communists and members of left-wing political parties in November 1945, had 246,000 members and an organizational capacity inherited from long years of independence movement and struggles against Japanese capitalists (Park 1979, Kim and Lee 2002).[82] *Chun-Pyung*'s extreme left-wing political orientation and its focus on political, rather than economic, agendas, however, caused right-wing political leaders and the US military administration to form a new moderate labor union in March 1946. *Daehan Nochong (Daehan Dokrip Nodong Choksunghwae)*—the predecessor to the current Federation of Korean Trade Unions (FKTU)—then became the leading national organization with 40,000 members as *Chun-Pyung*'s membership diminished to 2,465 by 1947, following fierce conflicts between the two unions and repression by the authorities that culminated in the outlawing of *Chun-Pyung* and the Communist Party in South Korea in March 1947. In contrast, 683 individual unions with a total membership of 127,618 under the leadership of *Daehan Nochong* registered with the government by 1953 (Park 1979).

In a time when there were only a few, effectively organized interests, Syngman Rhee, who in 1948 became the first President of the Republic of Korea, incorporated the FKTU into his political base (Ogle 1990). Rhee was named the first president of the FKTU in 1947, and after becoming the President of the new Republic, he appointed the chairman of the FKTU, Chun Jin Han, to head the Ministry of Social Affairs. Reflecting

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[82] The laborers' Mutual Relief Association (*Chosun In Nodongja Kongjaehwae*) was formed in 1919, the Korean Federation of Labors and Farmers (*Chosun In Nodongja Nogmin Yonmaeng*) was set up in 1924, and the Korean Communist Party (*Chosun Kongan Dang*) was established in 1925, together forming a workers' wing of the anti-Japanese resistance movement (Park 1979).

the ideals of Western democracy in general and the US in particular, the Republic's first Constitution guaranteed workers' rights, such as the right and duty to work and the protection of working women and children (Article 17), the right to form associations, the right to bargain collectively, and the right to engage in concerted actions (Article 18) (Kim 1981). In his effort to compete with the North Korea's claim of being a 'heaven for laborers' and having better workplace conditions, the Rhee government enacted four basic labor laws in 1953—the Labor Standards Act, the Labor Union Act, the Labor Dispute Adjustment Act, and the Labor Committee Act—which focused on protecting laborers in radical and progressive language. The Korean labor law, imitating Japanese labor law, had a combined structure of a continental law base with labor standards and collective bargaining on the one hand and a practical system of the US labor law on the other that far surpassed its level of industrialization and economic reality (Bleecker 1969, Park 1979, Kim 1981, Porges 1991, Kim and Lee, 2002).[83]

The Labor Standards Act laid the foundation for employment protection by specifying a minimum wage structure and some restrictions on the hiring and firing of workers, in addition to other protective measures such as safety and health guidelines, a forty-eight hour work week, protection of working women and children, a workers' accident compensation system, a retirement benefit plan, and the outlawing of employee discrimination (Articles 51, 56, 58, 61 and 62). These rights were to be further enhanced by the Labor Union Act, which guaranteed the right of workers to self-organization, collective bargaining, favorable working conditions, and welfare (Article 1). The Labor

[83] Park (1979) notes that a number of decrees and regulations promulgated by the Governor-General during 1945-48 remained in force and became the basis for the first labor laws in 1953.

Dispute Adjustment Act guaranteed fair settlements of labor disputes, and the Labor Committee Act established Labor Committees as independent entities to oversee labor disputes and maintain industrial peace by promoting democratization of labor relations (Park 1979, Kim 1981, Porges, 1991)

There was little incentive, however, on the part of the government to uphold these laws.[84] The conservative semi-authoritarian Rhee government had crushed independent workers movement, which minimized domestic pressures to enforce these promises and allowed the government to control use labor unions as a political vehicle. Syngman Rhee's ruling Liberal Party formally affiliated with *Daehan Nochong* in December 1955 without the consent of the Union's Executive Board, and its leadership openly accepted aid from the party and its business supporters. Without the leadership of labor unions, ordinary workers lacked the experience, knowledge, and platform to protect their rights in this high-unemployment—which averaged at least 15 percent throughout the 1950s in a rough estimate (Kim and Sung 2005)—and low-growth period.[85]

The Park Chung Hee government, which came to power through a military coup on May 16, 1961, restored political stability by halting what had unfortunately been chaotic efforts at democracy towards the end of the Rhee government. To restore order and consolidate his power, Park immediately stopped the enforcement of the labor laws through Military Decree No. 6 and abolished the FKTU. He then reorganized the

[84] Additionally, as it is usually the case in developing countries, lack of sufficient enforcement funds, scarcity of fully qualified staff, and the small size of most business establishments make many of the labor laws difficult to enforce (Bleecker 1969).

[85] According to one estimate, the GDP per capita in 1953 was $270, and after a decade it increased only to $350, with an average annual growth rate of 1.7% (Penn World Table).

enterprise labor unions into fifteen industrial labor organizations, forming a new national trade union center (with the same English name, the Federation of Korean Trade Unions) as a government-dominated entity.[86] Park also limited public employees' rights to organization (comprising mostly teachers and civil servants), collective bargaining, and collective action. The Park government amended labor laws in 1961, 1962, and 1963, further restricting labor union activities, prohibiting political participation, outlawing multiple unions, requiring prior government approval over labor disputes, and allowing weak punishment of employers who commit unfair labor practices (Kim and Lee 2002).

To compensate for these repressive measures, however, it extended job protection through provisions regarding severance pay, working hours, and annual paid leave, and maintained the legal prohibition against dismissing redundant workers.[87] For instance, employers having more than 30 employees must establish a 'retirement allowance' (severance pay) system that provides at least 30 days' average wage for each year of continuous service over one year regardless of the reason for separation (Article 28 the Labor Standards Act (LSA)). In terms of restriction on dismissal, Article 27(1) of the Act states, "An employer shall not dismiss, temporarily retire, suspend, transfer, reduce the wages of or take other punitive measures against a worker without justifiable reason." Neither the law nor its Enforcement Decree clarifies what constitutes a justifiable reason, however, making collective dismissal almost impossible to defend.

[86] Its Korean name is *Hankook Nodong Chohap Chong Yonmaeng,* or *No Chong* for short.

[87] Law No. 791 amended the Labor Standards Act on December 4, 1961, establishing or improving the following: the retirement allowance system; the exceptions concerning payment for interrupted work periods; working hours; rest periods; annual paid leaves; extensions of liquidation periods following the death or retirement of a worker; and guarantees of recuperative holidays with pay for female employees before and after childbirth (Kim 1981).

Based on this provision, public corporations, banks, and big businesses in particular did not even consider the possibility of mass layoffs until the financial crisis of 1997-98 (Kim 2001, Kitt 2003).

Additionally, Article 73 of the LSA requires the employer to submit a copy of the reorganization or relocation plan to the relevant government ministry, which has the authority to suspend or alter the plan if it deems such intervention to be necessary to maintain the safety and health of the workers (Park 1979). The government frequently exercised this provision, ordering, for instance, *Namhan Jaeji* Manufacturing and three other companies in April 1974 to alter their reorganization plans (*Dong-a Ilbo*, May 18, 1974).

Even after instituting the *Yushin* ("revitalizing") Constitution of 1972, which prolonged Park's hold on power and forbade the three basic rights of laborers—right to associate, right to collective bargain, and right to collective action—the Park regime supported the policy and practice of stable, 'lifetime' employment for core workers. While the precise origin of this practice and adherence to the law is difficult to ascertain, there are three likely sources—political compensation, ease of compliance, and skill formation—that together explain the persistence of employment protection mechanisms in industrializing Korea.[88] The government had a vested interest in winning

[88] Additionally, it is generally accepted that Confucianism has played a key role in the development of lifetime employment practices in Japan and Korea (Chang and Chang 1994, Miles 2008). Korean employers have shown reluctance to fire even in difficult economic times, and employees have exhibited a sense of loyalty to the company and owner in a manner similar to family relationships. President Park also tried to foster amicable labor relations through company provided benefits (1979). This cultural norm, though hierarchical and paternalistic, has likely provided the philosophical foundation for employment protection in the early post-war period. Confucianism, however, fails to explain the over-time changes in labor laws and practices, as well as an inconsistent application of the rules (*i.e.*, some benefited more than others) given that it is a cultural constant.

compliance for regime stability, and businesses were compelled to comply because of their dependence on government financing. Moreover, businesses had the capacity to comply due to rapid growth, and the larger of them may have even desired stable employment relationships regardless of the government edicts because of their growing need for advanced skills, which was fulfilled through vocational training.

First, labor compliance and peace was deemed crucial to achieving the regime's economic and security goals which they pursued in order to bolster political legitimacy.[89] Several prominent and violent cases of labor protest in the pre-*Yushin* period likely prompted the Park regime to not only tighten its grip on the collective activities of labor, but also to reduce labor grievances through job security and rising wages. In 1970, Chon Tae-Il committed suicide by burning himself during the demonstrations of the Chonggye garment union in protest of labor exploitation, low wages, and violations of the LSA in regards to working conditions and wage delinquency, setting off a string of labor protests that both highlighted the plight of workers and threatened Korea's economic and political stability. In 1971, workers of Hanjin Co. broke into the Korean Air Lines headquarters and set fire to the building; there was a riot in the Hyundai shipbuilding yard, female workers of Dongil Textile Co. went on a long-term strike, and unions of Wonpoong Wool Co., Control Data, and Panda Co. also went on strike for similar reasons.

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[89] I rely on the established assumption that politicians seek office by pursuing the support of the electorate or the selectorate and argue that in Korea, the regime perceived that populace support depended on maintaining a sense of security against the threat of North Korea and continuing the economic growth of the 1960s.

In response, the government forced companies to retain workers, using job security as a form of economic compensation in exchange for the tight control of union activities (Lee W. 2003). Between 1975 and 1979 (the *Yushin* period prior to Park's assassination in 1979), for instance, the issue of dismissal caused less than 5 percent of labor disputes, while the majority concerned wage issues (see Figure 4.1). Given that the unions were a potential source of organization that could bring pressure on the government, the Park regime pursued job creation, employment protection, and skill development as the primary strategy for providing basic welfare for its labor force, appeasing the unions, while seeking to establish legitimacy and popular support.

Second, unlike most of the provisions in the labor laws, employment protection did not impose any financial burden on the employers because of the ever-expanding need for an industrial workforce; a tight labor market resulting from the export boom rendered the invocation of employment protection laws largely unnecessary. The Park government controlled investment, financing, and other key aspects of business decision-making, and organized businesses into large conglomerates in which the firms' incentive geared less toward profit-maximizing and more toward size-maximizing, with their success depending on exports and on maintaining a cooperative relationship with the regime. The laws on employment protection matter only when companies need to restructure and downsize.

Third, the government required on-the-job training to develop vocational skills, which provided the basis for industrial deepening and a continued reliance on export-led industrialization. It implemented the Vocational Training Law No. 1880 of January 16, 1963, which provided the legal basis for formal vocational training, on-the-job training and skill tests of workers aimed at improving their social status and contributing to the development of national economy (Bleecker 1969, Park Y. 1979). It also established the Central Vocational Training Institute in 1968 with the assistance of the UNDP and the ILO (Kim S. 1978). Furthermore, between 1971 and 1973, the government pursued technical cooperation with the German government to establish the Korea-Germany vocational center in Pusan, founded the Chung Su Training Center with aid from the US government, and opened up centers in Chunchon and Taegu with loans from the Asian Development Bank, all equipped with up-to-date training facilities. In 1973, the government announced a policy focusing on technical and mechanical high schools and established public and in-plant vocational training centers, followed by laws in 1974 that required private companies with over 300 workers to assume partial responsibilities for vocational training (Kim and Lee 2002).

It was during this period of the heavy and chemical industrial drive and government-led industrial deepening that the institutions of job security became solidified. Korea’s labor laws provided job security, generous wages, and fringe benefits particularly to male laborers in key industrial sectors to induce investment in technical skills, even as labor’s rights to collective action and bargaining were restricted. In response to the deteriorating economic and security environments of the early 1970s, the regime pursued a heavy and chemical industrialization (HCI) drive, shifting the focus away from labor-intensive light manufacturing. The move was controversial, but the Park regime was able to neutralize the opposition largely by winning the support of the core male industrial manpower through promises of job security, skill development, and generous compensation (see Table 4.2 for wages in manufacturing 1970-1979).

4.2 Democratization, labor power, and institutional changes: 1987-1995

The laws and practices of employment protection established in the pre-democratic period constituted the policy status quo which shaped and conditioned the subsequent political haggling over labor-related laws between labor and business. Under the existing labor market institutions, employers were mainly interested in retaining and developing a skilled workforce at an affordable cost, while workers wanted improvements in wages, working conditions, and collective rights, which for the most part were denied by the conservative authoritarian regimes. With democratization, however, labor’s stature and influence increased as electoral pressures turned them into a powerful voting constituency. Increasing economic openness, on the other hand, began undermining labor’s collective power through competitive pressures.

In this section, I analyze these two shocks—democratization in the late 1980s and economic openness in the early 1990s—that had significant impact on the bargains over labor relations (collective labor rights) laws and the adoption of the unemployment insurance system. The third explanatory factor—the performance of the economy—is considered in conjunction with the two primary factors. The resulting changes in these policies and the new status quo that developed then became the setting from which subsequent negotiations over employment protection and other labor market policies took place.

First, democratization or political liberalization in 1987-88 marked the end of coordinated and government-led industrialization and unleashed pent-up energies and demands from both labor and capital, resulting in improvements in working conditions and collective rights, unprecedented wage increases, and management initiatives on business opportunities. This experience conforms to the prevailing theoretical expectation that democratization expands labor rights and empowers them to defend their entitlements and obtain new ones.

In addition, favorable economic conditions and strong growth during this period—spurred on by the "three lows" of low oil prices, interest rates, and the won—raised business demand for labor as well as labor's political bargaining power. From the labor's perspective, it was now time to demand a greater share of the economic success, and from the business' perspective, it had the capacity to afford, for the time being, the increases in wages and other benefits.

On the other hand, the pursuit of export-oriented strategy—which is a particular form of economic openness—is expected to have the opposite effect. A greater engagement in the global economy through exports generates sensitivity to labor costs on the part of both producers and the government.[90] In the early 1990s, as the Korean government retreated from imposing order in the affairs of industrial relations and businesses were left to compete on their own in the global market with fewer protective barriers and lower financial backing, employers began voicing their concerns over the growth in wages and labor cost. Buffeted also by recessionary pressures in the early

[90] Also, economic openness enhances producer mobility and their relative political leverage through the threat of relocation to lower-cost neighbors or the importation of cheaper labor from abroad.

1990s, employers sought out ways to enhance operational flexibility. All in all, declining product market protections generated pressures against labor market protections, and the granting of the long-denied collective labor rights eliminated the political rationale for compensation in the form of labor market rigidity.

These case studies show that while the theoretical expectations concerning the impact of political and economic changes on labor laws bear out, their very success also had unintended (by labor at least) consequences on their right to employment protection in the subsequent period. The irony is particularly strong with the case of unemployment insurance, as the employer support for the policy was premised on the implicit promise by the Kim Young Sam government that it would help liberalize the laws on mass layoffs down the road.

4.2.1 Democratization and the rise of labor power

The last of the authoritarian rulers, Chun Doo Hwan (1981-1988) continued the policy of repressing labor union activities while promoting the welfare of workers through job-related means. One of the amendments to the labor law in 1980 prohibited the intervention of a third party in the establishment or dissolution of a labor union, joining or leaving a union, or in collective bargaining with the employer. Establishing a labor union required the approval of over 30 workers or over one fifth of the entire work force, and strikes are prohibited outside the concerned workplace to prevent the rallying of public opinion and sympathy (Kim and Lee 2002). These repressive laws prohibiting union activities and the dissatisfaction with wages became the target of labor fury and fueled violent strikes when a democratic opening arrived in the form of the June 29

Declaration in 1987 by the President's hand-chosen successor Roh Tae Woo, following a furious month of student-led demonstrations with mass participation and support. Ushering in a new era of labor insurgency, there were 3,628 cases of labor disputes seeking higher wages and unionization rights during the two months of July and August following the declaration, compared to about 270 cases each in 1985 and 1986 during the entire year (See Figures 4.2, 4.3, and 4.4.) (Lee S. 2003, Chosun Ilbo, August 4, 2008).

The Chun government succumbed to the democratic fervor from both within and without, and amended the Constitution as voted in a national referendum on October 29, 1987, adopting a direct presidential election with a single term limit of 5 years and guaranteeing, among others, the three basic labor rights—right to independent association, collective bargaining, and collective action (Article 33), with public officials and employees of important defense industries being excepted unless provided for by law. Further amendments in various labor-related laws liberalized the rules on the establishment and collective actions (such as strikes) of trade unions, limited government involvement in labor disputes, and established a minimum wage system (which was implemented on January 1, 1988) and shorter working hours (Park 1998).

Democratization and the changing laws and rules of engagement resulted in an explosive growth in the number of labor unions and the establishment of collective bargaining structures at the firm level. Between 1987 and 1989, the number of enterprise unions increased from 2,700 with 1.05 million members to 7,800 with 1.93 million members, and the unionization rate likewise increased from 15.7 percent to 19.8

percent (see Table 4.3).[91] A double-digit wage increase followed—over 15 percent per annum between 1988 and 1992 (and a five-fold increase between 1987 and 1997), led by labor unions organized at large enterprises especially in shipbuilding, automobiles, and electronics, and aided by favorable global economic conditions between 1986 and 1989 in the form of low international interest rates, low oil prices, and a weak US dollar (see Table 4.4 for wage and productivity growth; Figures 4.5 and 4.6 for economic growth). Average working hours per week diminished from 51.1 in 1988 to 47.5 in 1992, marking a noticeable improvement (Lee S. 2003).

Along with the goal of improving working conditions and wages, the labor movement began pursuing an extensive reform of authoritarian-era labor laws and staging demonstrations to oppose the harassment of union leaders (Choi et al. 2001). Around the time of the National Assembly election in April of 1988, which produced a governing minority and opposition majority (*yu-so-ya-dae*), the many newly formed labor unions with anti-FKTU leanings formed a regional, industrial, and national alliances to elevate their political presence and influence, eventually leading to the formation of the National Congress of Trade Unions (NCTU, or *chun-no-hyup,* which is one of the predecessor movements behind the Korean Confederation of Trade Unions, or KCTU) in January 1990. Setting itself up against FKTU as the true democratic and uncorrupted representative of the working class, NCTU tried to expand its organizational reach by taking a strong and confrontational stance in negotiations with employers.

[91] Since then, it came down to around 12 percent in recent years.

Opposition parties in the National Assembly, led by Kim Young Sam and Kim Dae Jung, were sympathetic to the causes of the labor movement, as they themselves had long opposed authoritarian rulers throughout the 1970s and 1980s.[92] A bill to reform the Trade Union Act and Industrial Disputes Adjustment Act[93] that passed the National Assembly vote in March 1989 reflected in large part the wishes of the labor movement—particularly of the conservative FKTU, granting, for instance, the unionization and collective bargaining rights to civil servants of lower rank and continuing to outlaw multiple unions and outside involvement in union matters (Choi et al. 2001).[94] President Roh, however, vetoed the bill, citing the sufficiency of the changes made in 1987 and limitations imposed by Korea's economic reality.[95]

Confirming the theoretical expectation outlined above, political liberalization increased labor's organizational and bargaining power, through which they influenced the reform process in their favor to realize the ideals of the original Constitution and the Labor Standards Act. While their increased power did not translate into the formation of or a direct linkage to a political party, labor obtained enhanced working conditions and higher wages thanks to their newfound collective power. Labor's success, however, sowed the seeds of discontent among employers as they undermined the basic structure of compromise forged in the era of rapid development and state-led industrialization.

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[92] Eventually, the opposition parties led by Kim Young Sam and Kim Jong Pil merged with the governing Democratic Justice Party (*min-jung-dang*) of President Roh Tae Woo on January 22, 1990, bringing the era of opposition majority to an end.

[93] These two Acts that later combined to become the Trade Union and Labour Relations Adjustment Act (TULRAA) in March 1997.

[94] Outlawing multiple unions benefited the already established FKTU and stultified the growth of NCTU, its new competition. While FKTU participated in the discussions, NCTU was excluded from the labor law revising process.

[95] Based on this analysis, a partisanship argument can be made that democracy would have had wider effects under a left-leaning government.

Democratization also improved business' ability to lobby and reduced their reliance on government-sponsored financing, as the authoritarian structure and centralized industrial planning began to dissolve. These changes provided the basis on which business demands for labor market liberalization were built and intensified under the pressures of economic openness.

4.2.2 Economic openness and the adoption of (un)employment insurance

The second case involves the impact of economic openness and slowing growth on the adoption of (un)employment insurance (UI/EI) system[96] in 1993, the efforts which began in 1989 under the Roh Tae Woo government. While the proposal and active support for UI/EI came from labor, first the government (especially the bureaucrats) and later employers also were persuaded to support the initiative, reversing their long-held opposition to the idea of giving money to people who do not work. The crucial turning factor for the government revolved around the core content of the program, *i.e.*, establishing active labor market policies centered on skill development, upgrading of employment structures, job placement, etc., so that the focus would be on the prevention of unemployment, instead of simply assisting the unemployed. For employers, they came to see UI/EI as a necessary expenditure in their quest for labor market flexibility. That employers gave their consent—though cautiously and somewhat reluctantly—was a key factor behind the successful legislation of the UI/EI program. This section documents and analyzes the processes and the politics of UI/EI adoption.

[96] Korean bureaucrats and academics preferred the name *employment* insurance over *unemployment* insurance for its emphasis on promoting employment and not simply assisting the unemployed.

With democratization came the rise in the expertise and importance of labor opinions on labor-related issues. Convinced by policy heads within the organization, the FKTU petitioned the National Assembly on September 25, 1989 for the adoption of unemployment insurance (UI), and recommended it to the Ministry of Labor on the 30th of the same month. It then registered its demands for UI to the ruling Democratic Liberal Party in May and to the opposition Peace Democracy Party (led by Kim Dae Jung) in August of 1990.

Around the same time, the government also began studying the issue formally and actively. In December 1987, the Ministry of Labor issued a report on the Japanese UI system, and the Korea Labor Institute issued a report on UIs in other countries in 1990 for policy formulation purposes. The government looked at this issue more seriously during the planning phase of the 7th Development plan (1990-1991), initially appointing the Korean Development Institute and the Korea Health Society Research Institute to prepare a proposal for the UI legislation. The responsibility then shifted to the Korea Labor Institute, and in March 1991 the Institute submitted a UI proposal to the government and successfully convinced the Economic Planning Board officials of the need for UI. They did this in large part by designing the proposal to focus on schemes that promote job creation, stabilization, and transition out of unemployment through vocational skills training, employment placement efforts, as well as unemployment benefits. To reflect this emphasis, the policy experts chose the name *employment* insurance (EI), as opposed to *unemployment* insurance, to highlight the importance of active labor market policies and downplay the negative feelings associated with giving financial aid to those who do not work.

Given this focus on employment promotion, the Department of Manpower Development and Planning within the Economic Planning Board took over the administrative responsibilities over EI, and with it, bureaucratic support for EI increased significantly (You and Lee, 1996). The Ministry of Economy finalized its decision in August 1991 to adopt EI during the later phase of the 7th Economy and Society Development Plan. EI was also politically popular during the 1992 National Assembly and presidential elections, garnering support from all three major parties. FKTU submitted its recommendations regarding EI to the government in March 1993, and the newly elected Kim Young Sam (YS) government declared its intention to carry out EI as part of "The New Economy Five Year Plan" in 1995.

While the labor camp's championing of EI is understandable, the surprising element in this case is that employers, represented by the Korean Employers Federation (KEF), gave its support to EI, the fourth and last of the major social insurance programs to be adopted for Korea. Employer compromise on this issue was key to enacting EI by the business-friendly and conservative Roh and YS governments. The significance of the employer compromise is seen by the fact that a discussion on EI (or UI, a term that is more generally used in other countries) was going on for a long time, going back to the 1960s. Laws on employment stabilization issued by Park Chung Hee's military junta on December 6, 1961, defined UI as a responsibility of the government, although economic conditions at the time and limits in administrative capacity made UI unpractical for Korea. An unofficial Ministry of Labor report from 1968 recommended unemployment assistance for low-income workers, but this discussion did not gain any traction. Again in 1974 and 1978, internal documents within the Ministry considered unemployment assistance or insurance, but these ideas remained internal and were never discussed outside or with the other ministries of the government (You 2005).

The first official discussion on this topic took place around the time of recession at the end of 1979 through 1982. The ministry of labor officially recommended the adoption of UI to the Economic Planning Board as part of the Fifth Economic and Social development five-year plan. The government decided not to adopt it at the time given the concerns regarding negative side effects, the burden on businesses, the underdevelopment of industry, and strong objections not only from the employers but also from President Chun and other officials. There was hardly any political or economic support for UI, and even labor representatives were unaware or uninterested in pressing for it. It was also during this time that policy experts and government officials began using the name *employment* insurance.

Given the long history of employer objections to EI/UI, it is puzzling why the KEF chose to support the policy in the early 1990s. In its letter to the Ministry of Labor dated June 30, 1993, the KEF acknowledged the need for and its support of EI and made recommendations concerning the scope and other program details. The letter states that designing EI must give priority to maintaining the global competitiveness of the domestic economy, while meeting its stated dual objective of allowing for a more fluid process of employment adjustment and of protecting the unemployed. Concerned about the new law’s impact on small- and medium-sized enterprises, both KEF and the Ministry of Commerce, Industry, and Energy recommended limiting the size of the affected firms to 150 employees or more (similarly to the rules on mandatory job training), transferring a portion of severance payment to unemployment benefits to avoid an overlap, setting the replacement ratio to 50% of average wage, and adopting the experience rating system (KEF Business Report 1994). The KEF again reiterated its cautious support of EI on a letter to the Ministry of Labor dated September 15, 1993, and included additional cost-cutting demands, such as eliminating the provision for disabled and old-age workers (which is already provided for in other relevant labor laws), limiting the vocational ability development program to the retraining of laid-off workers, and eliminating the requirement to accumulate excess funds up to twice a given year's expenditure (Korea Employers Federation 1994).

In contrast, labor demanded that the new law cover firms with ten employees or more and set the replacement ratio to range between 60 to 80 percent depending on the wage level (You 2005). Other demands included setting the minimum coverage period to six months out of twelve months preceding the layoff and the length of benefits payment to range from 90 to 300 days, and leaving intact the existing severance payment obligations.

After much negotiation over these and other details of the program, the Ministry of Labor submitted the EI bill to the National Assembly on October 28, 1993, which passed unanimously on December 1, 1993.[97] The law became effective on July 1, 1995, covering companies with thirty or more employees for the unemployment benefits program (UBP) and with seventy or more employees for the active labor market policies of employment stabilization program (ESP) and vocational ability development

[97] The Employment Insurance Act (1993) Article 1 states that, "The purpose of this Act is, through the enforcement of employment insurance, to prevent unemployment, to promote employment, to develop and improve the vocational ability of workers, to strengthen the nation's vocational guidance and job placement capacity and to stabilize the livelihood of workers and promote their job-seeking activities, by granting necessary benefits when they are out of work, thereby contributing to economic and social development of the nation" (Labor Laws of Korea, 2005).

program (VADP), making 63% of the employed workers eligible for the program (Park, Park and Yoon 2005).[98] Employers are responsible for paying the insurance premium of 0.1% of covered payroll for the employment stabilization program and up to 0.5%, depending on the size of the firm, for the vocational ability development program. For unemployment benefits, employers and employees split the contribution equally, each paying 0.3% of the covered payroll. To be eligible, an employee has to have been covered for at least 12 months out of a minimum 18-month tenure immediately prior to the layoff, and the benefits period ranges between 60 to 210 days depending on the difficulty of re-employment.[99] The new law did not change the existing provisions on severance payments, instead charging the Minister of Labor with the "task of reforming the severance payment scheme in the future" (You 2005).

The turnabout by employers is a significant reason why the conservative and right-leaning YS government was willing to enact EI, a cause championed by the left that raised the cost of labor (by about 1% of the total wage bill) to employers. Political and business leaders in the past resisted and even disdained the idea of giving monetary assistance to those who do not work since they considered such help as breeding moral hazard and laziness. Although rising living standards and income, as well as higher economic, political, and institutional capacity made the execution of EI feasible, what in the end motivated and convinced employers to change their position was its perceived

[98] Excluded from the provision are workers who obtained employment after they were 60 years or older, part-time workers, daily workers, seasonal or temporary workers, civil servants, and private school teachers (Article 8).

[99] These contribution rates are some of the lowest in the world. For instance, as of 2008, France requires a contribution of 2.4% of covered earnings from the insured person and 4% of covered payroll from the employer. In Germany, the insurance person and employer each pay 1.65% of covered earnings. See Social Security Programs Throughout the World (http://www.ssa.gov/policy/docs/progdesc/ssptw/) for information on these and other countries.

necessity in advancing the goals of labor market flexibility. A KEF executive noted this fact as the chief motivation behind the KEF's support of EI in my interview with him[100], and professor Kim Soo-kon of the Korea Labor Education Institute also commented that he was able to convince the leaders of the Federation of Korean Industries (FKI) by pointing out the inevitability of corporate restructuring and how without EI such efforts were bound to fail. He won business consent on the need for EI by arguing that EI is precisely what they needed to make restructuring socio-economically and politically feasible in the future (Ministry of Labor 2005).

Furthermore, analyzing the content of the bill—which includes not only UI but also active labor market policies of the employment stabilization program (ESP) and the vocational ability development program (VADP)—suggests that the lawmakers had in mind the eventual liberalization of employment protection legislations and the support structures that would be needed to transition workers in and out of unemployment. The ESP provides financial subsidies to participating companies for keeping redundant workers on the payroll by resorting to methods such as reducing working hours, work-sharing, participating in vocational training programs, and reassignment; and for hiring covered workers laid off by other firms and a set number of old-age workers; and for facilitating maternity leave and daycare programs. The VADP subsidizes vocational training by employers or employees and the establishment of both public and private vocational training entities (You et al. 2002).

Thus, it can be argued that employers were unlikely to support EI without the motivation and an implicit promise by the government to eventually push for labor

[100] At his KEF office in June 28, 2006.

market liberalization. Although this does not suggest that EI would not have prevailed, the attitude of the YS government and the intensity of the political struggle over the issue could have been strikingly different. In addition to rising labor costs and slower growth in 1992 and 1993[101], employers faced other competitive pressures as the government phased out protective policies from the pre-democratic era. For instance, one of the YS government's new policy priorities was "*Se-gye-wha,*" or globalization, which involved, among others, opening up the domestic market to foreign products in rice, construction, telecommunication, sales, and education.[102] The traditional system of government-controlled finances—over interest rates, policy loans, entry barriers to financial activities, capital account, etc.—was quickly liberalized and opened up to foreign players. Simultaneously, the increased credit ratings of Korean corporations and banks in the international financial markets enabled the private sector to borrow without government guarantees or oversight. Although Korea was an active and important exporter in the global economy since the 1960s, its domestic market was long protected from foreign competition. Korea's transition to an open economy can be said to have begun in earnest during the YS era.

Increased economic openness thus generated competitive pressures on employers who began pressing for policy reforms particularly on the issue of collective layoffs for redundancy (see Table 4.4, which shows that in the 1991-1995 period, wage

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[101] Korea's GDP per capita grew by 4.9% in 1992 and 5.2% in 1993, which by Korea's standard were low. In 1990 and 1991, for instance, its GDP per capita grew by 7.9 %and 8.4%, respectively. See Figure 4.6.

[102] Also important is the fact that, riding the tide of neoliberal ideology and the Washington consensus, the US began to place market-opening pressures for the promotion of its exports and challenge Korea's domestic economic policies or traditional commercial behaviors (Kim 1997). Previously, disputes centered on cheap Korean exports to the US. Now, US pressed for the removal of Korean import and market access restrictions on US exports in financial, agricultural, and cultural sectors.

growth outstripped labor productivity growth by an average of 58 percent annually). Unable to make its demands met, Korean firms began using temporary workers in growing numbers in the mid-1990s prior to the financial crisis, circumventing the restrictive rules on layoffs. With EI in place, however, employers geared up for a major push to liberalize the labor market in the second half of the YS government.

4.3 The IMF crisis, labor market liberalization and the expansion of (un)employment insurance: 1996-1998

In this section, I analyze the case in which the 1997-98 regional financial crisis plunged the entire nation into an economic standstill through conglomerate failures and capital flight, and resulted in an unprecedented negative growth of 8% in GDP and a humbling US$57 billion bailout by the International Monetary Fund (IMF). The theoretical expectation here is that the conditions in the economy are likely to have a strong influence on the strength of labor and thus its ability to maintain protections. When labor markets are tight, the economy is strong, and political liberalization enhances collective rights, labor has more bargaining power vis-à-vis business and is more able and likely to secure benefits with marginal compromises. Immediately after democratization in 1987, rising labor power combined with prosperous economic conditions made it possible for Korean labor to win significant concessions in wages and labor rights.

In contrast, when the economy is in recession, there are pressures to roll back protections and benefits that are deemed excessive—*i.e.*, the status quo of heavy employment protections was seen as untenable. The financial crisis thus created an opportunity for policy change favorable to employers.[103] With rapid deterioration of economic conditions, which weakened labor's bargaining power, labor had no choice but to give up one of its most prized benefits—the prohibition against mass layoffs—and become an unwilling partner in the acts that led to labor market liberalization, the political fight over which began in earnest in early 1996.

By the mid-1990s, the Korean economy in general and employers in particular came under increasing pressure to shore up their competitiveness. Korea's exports stagnated and the trade deficit rose to US$2.3 billion in 1996 following a sharp decline of about 85 percent in the world market price of semiconductors, one of Korea's major export products. Korean products also lost competitiveness vis-à-vis their Japanese competition with a depreciation of the Japanese yen. In this slowing economy, policy makers and business leaders alike began suggesting that enhancing the global competitiveness of domestic firms would not be possible without deregulating labor and other factor markets. Korea's labor market was deemed too rigid due to excessive employment protection provided by the Labor Standards Law and confrontational labor unions. A rigid labor market impedes structural adjustment and raises both socioeconomic dead-weight loss and labor costs for firms.

From the perspectives of labor, the remaining restrictions on union activities were undemocratic, and pressures from the International Labor Organization (ILO) and the Organization for Economic Development and Cooperation (OECD) added to the

[103] The presidential election during the height of the crisis in December 1998, however, resulted in an administration that was favorable to labor.

strength of labor demands.[104] Membership in these organizations had positive impact on labor policies in Korea, both organizations making concerted efforts to pressure Korea to bring its collective labor rights up to date and to ratify the ILO conventions.

Although Kim Young Sam had made a campaign promise as a presidential candidate to reform the three contentious labor laws—the Labor Standards Act, the Trade Union Act, and the Industrial Disputes Adjustment Act, he delayed acting on the issue due to the acute disagreement over the issues between business and labor (Park and Park 2000). But in early 1996, the Minister of Labor Jin Nyum began expressing the need to shore up Korea's legal and cultural backwardness in industrial relations, resulting in the appointment of a committee of interested parties and policy experts to prepare a reform bill addressing the demands from both labor and business regarding the three labor laws (*Seoul Economic Daily*, February 14, 1996; *Korea Economic Daily*, April 16, 1996).

At stake were three collective rights issues championed by labor and three individual employment rights issues championed by employers. Labor had long fought for the elimination of prohibitions on multiple unions, third-party involvement, and political activities by unions (together termed "three prohibitions"). Employers on the other hand had demanded the reform of rules on redundancy layoffs, temporary work agencies, and flexible work hours (together termed "three regulations"), the regulations that constitute the core of employment protection legislation (EPL). By inviting two representatives from the KCTU (still extra-legal at this point because of the prohibition

[104] Korea joined the International Labor Organization (ILO) in 1991 and became a member of the exclusive Organization for Economic Development and Cooperation (OECD) in 1996.

on multiple unions) to participate, the Committee on Labor Relations Reform sought to establish a broad base of support and even signify the arrival of the more radical KCTU as a legitimate partner in labor related negotiations.

Although the opposing parties were able to compromise on several major policy points through the course of the following seven months—such as allowing political activities by unions and expanding the application of the Labor Standards Act to all enterprises, continued and fierce disagreements over other major issues resulted in the governing party in the National Assembly passing the new labor laws in the early morning hours of December 25, 1996 without the opposition party present to vote. The bill failed to legalize multiple unions, eviscerating the KCTU's legal and organizational integrity, while legalizing redundancy layoffs, the most contentious of the proposed changes that is the essence of labor market liberalization.[105]

The traditionally conservative FKTU, the radical KCTU, and the political opposition responded by mounting the largest anti-government demonstration since the 1987 democratization protests, calling for the repeal of the new law in general and the redundancy layoff provision in particular. The government's failure to recognize the KCTU was also condemned by the media and general public, along with what was seen as a complete evisceration of democratic principles in law-making. A nationwide strike followed immediately, lasting for over 30 days and involving 3,206 unions and 3.6 million workers from all ranks and files. The government buckled under pressure, and on January 21, 1997, YS gathered the heads of political parties to discuss revising the contested laws in the National Assembly. After several rounds of negotiation, the

[105] Every major newspaper in Korea reported on the event on December 27, 1996.

National Assembly passed a revised Labor Relations Adjustment Act on March 10, paving the way for the legal recognition of the KCTU and delaying the enforcement of redundancy layoffs for two years. The YS government's underestimation of labor power, as well as its the strategic choice it made in terms of the undemocratic manner in which it passed the law, resulted in a humiliating defeat that undermined the ruling party's popular support and helped usher in the economic turmoil that followed in 1997.

Although labor triumphed over the conservative YS administration's efforts to liberalize the labor market in the early part of 1997, all did not bode well for the future of both business and labor. In January, the Hanbo group began experiencing serious financial difficulty, needing a bailout by the government. Reversing the long tradition of rescuing large firms from financial meltdown, the government decided to let Hanbo fail. Other conglomerates followed suit. Sammi, Jinro, Kia and other *chaebol* groups crumpled under large debt and a liquidity crunch. What followed was the worst economic disaster in Korea's modern history, the East Asian financial crisis of 1997-98.

The fifteenth presidential election took place on December 18, 1997, as the drama of the financial crisis hit its nadir. Just two weeks prior, the YS government announced the IMF rescue package of US$57 billion with stringent conditions on structural reforms. Given that the incumbent and his party was largely blamed for failing to stem the tide of corporate bankruptcies and exodus of foreign capital, it is rather surprising that Kim Dae Jung (DJ) from the main opposition party, the National Congress for New Politics, only narrowly defeated Lee Hoi Chang of the New Korea Party, who joined hands with Cho Soon's Democratic Party to form the Grand National Party (*Hanara*). DJ garnered 40.3 percent of the vote and Lee, 38.7 percent, with only

391,000 votes splitting the winner from the loser. It was the smallest winning margin ever in Korean history. Moreover, DJ owes much of his victory to his strategic alliance with Kim Jong Pil (JP) of the United Liberal Democrats (ULD) who brought with him conservative votes from the *Choong Chung* area (central South Korea). DJ came into power with one major mandate: to reform and rescue the economy from disgrace and disaster.[106]

Given the urgency of the situation, a Tripartite Commission consisting of representatives from the government, business, and labor quickly produced a comprehensive set of policy agreements and compromises by early February 1998. Due to the weakened bargaining power of labor, the Commission was now able to agree on the most contentious of the issues, the enactment of redundancy layoffs and temporary work agencies (dispatch workers) that enhance labor market flexibility. In return, employers agreed to protect the basic and collective labor rights of public employees, teachers, and the unemployed, and to expand social safety nets including Employment Insurance (EI), national pension, and health care. Other agreements included enhancing the transparency of management and corporate restructuring through clarifying the responsibilities of owners and management, and the burden sharing by the political establishment. The National Assembly passed these agreements into law in the same

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[106] DJ's parliamentary base was also weak, being in the minority position with 78 of 299 seats in the NA. Even adding his alliance partner Kim Jong Pil's ULD yielded only 121 seats, compared with GNP's 165 seats. On the other hand, the opposition party had the legislative majority, but its political leverage was weak given the defeat of its presidential candidate and the public perception that as the party of YS, it is responsible for the financial crisis. No one side dominated the politics at the time and there was a close partisan balance both at the political and societal level. DJ needed the support of GNP to enact laws, and both business and labor had voices in politics through GNP and DJ's NCNP, respectively. It was in this political environment of partisan balance that DJ led the national dialogue on restoring confidence and restructuring the economy through bargains and compromises between labor and business.

month, paving the way for the restructuring of much of the economy. In June, five banks were retired, and in July the government announced plans to privatize public corporations. As Hyundai Motor and other firms pursued corporate restructuring, the unemployment rate soared to the upwards of 8 percent, a level not seen since the early days of the Park Chung Hee government.

Although the scope of EI at the onset of the crisis was quite minimal, it nonetheless played an important role in providing the first line of defense for the unemployed and continued to expand as the crisis deepened. At the initiation of EI, the employment stabilization program (ESP) and the vocational ability development program (VADP) were mandatory only for firms with seventy employees or more, and unemployment benefits program (UBP) for thirty employees or more. Speeding up the timeframe set initially for expansion, the government increased the number of applicable firms to those over fifty employees for ESP and VADP and to over ten employees for UBP starting on January 1, 1998. The severity of the crisis prompted the expansion even further, extending the coverage of UBP to firms with ten employees by January 1, then to five by March 1, and finally to all businesses employing at least one worker by October 1, 1998. As of 2005, all businesses employing one or more workers must enroll in EI, except for nonregistered businesses in agriculture, forestry, and fisheries that employ four or less workers, construction firms with project budget of less than twenty million Korean won, and various home-based employment (cleaning, cooking, etc.). The EI system was extended to cover temporary workers employed for at least one month and part-time workers employed for at least eighteen hours per week.

As a result, the number of applicable businesses increased ten-fold between 1997 and 1998 from 47,000 to 400,000 (and to 600,000 in 1999), and the number of the insured increased from 4.28 million in 1997 to 5.27 million in 1998 and 6.05 million in 1999. In 1998, the percentage of the unemployed claiming unemployment benefits rose about six-fold, from 2 percent to 12 percent.[107] The financial crisis became the catalyst in expanding Korea's social safety net for the unemployed, and the policy decision to expand was not questioned by the employer community given the magnitude of the situation and also its usefulness in facilitating restructuring and collective layoffs. Not only was the need for restructuring more immediate, the crisis also afforded them the opportunity to increase labor market flexibility through legal means. For companies that survived the financial crisis—as many failed and were disbanded (*e.g.*, the Daewoo Group)—there came new financial obligations from the EI program (between 0.7% and 1.3% of annual payroll depending on the type of business) but also a higher level of flexibility in their hiring and firing decisions.[108]

Restructuring efforts through redundancy layoffs, however, generated intense protest by both the FKTU and the KCTU. In the more radical KCTU camp, strong disapproval by the member union leaders on the umbrella group's leadership and its

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[107] These and other data indicate the fact that EIS made a modest yet concrete impact on the livelihood of the unemployed during the crisis.

[108] OECD argues in its Survey of Korea (2004) that the revision of the labor law in 1998 to allow collective dismissals for "urgent managerial reasons" has not sufficiently enhanced flexibility in practice, reflecting the attached conditions: most notably, exhausting "all means" to avoid dismissals, discussing proposed dismissals for at least two months with workers, and notifying the government. It notes that although in practice rulings by the Supreme Court have introduced flexibility in certain cases, firms have relied on more expensive methods to reduce employment, such as early retirement packages and incentives for voluntary departures, given the constraints in the law. In addition, it argues, regular workers in unionized companies also receive protection in collective bargaining agreements, impeding flexibility.

decision to agree to the "tripartite grand compromise" eventually caused the KCTU to abandon and denounce the Commission for its bias against labor interests. During this period the focal point of labor contention moved from unionization and wage issues of previous years to job stability, security, and new management strategies centered on labor market flexibility and the retrenchment of company welfare provisions (Figure 4.1). The controversy surrounding EPL—the issues of redundancy dismissal and contract, temporary, and dispatch workers—has become the lightening rods of conflict among business and labor.

4.4 Conclusion

Korea's labor market liberalization resulted from of a political bargain struck between labor and business in the middle of the crisis in February 1998. What underlies this outcome is the surprising policy stance taken by the employers on the unemployment insurance (UI) policy, which the Koreans named the *Employment* Insurance (EI) system. Traditionally, employers are thought to be against social policy commitments; profit-conscious capital prefers to shed expenses whenever possible, supporting deregulatory measures with regards to the labor market. In contrast, the Korean Employers Federation (KEF) supported the adoption as well as later expansion of EI in order to make labor market liberalization more palatable to workers and thus political feasible. Labor, who earlier championed the adoption of EI, initially agreed then later denounced the tripartite agreement, which expanded the coverage of EI and guaranteed various labor rights in exchange for the redundancy layoff provision.

The adoption of EI/UI and its expansion since the economic crisis has increased government spending on labor welfare in Korea. The future of employment laws and related social insurance programs in Korea are being negotiated at present as both sides try to clarify their policy preferences in a fluctuating and competitive product market and organizational environment. The battle over the issues of employment protection and labor welfare, such as the issues of irregular workers and market dualism, will remain a destabilizing force in Korean politics for some time. There is a great need for a better understanding of these and other labor market issues given the significant role they play in the developmental prospects for Korea and other middle-income countries.

Table 4.1: Three cases of labor market policy reform since 1987

	Case 1: 1987-89	**Case 2: 1993**	**Case 3: 1997-1998**
Explanatory parameters	Democratization: labor strength is high	Increased openness and slowing growth: labor strength is moderate	Financial crisis: labor strength is weak
Expectations	Enhanced collective rights & maintenance of existing rights on employment protections	Employment protections/labor market liberalization	Employment protections/labor market liberalization
Actual major outcomes	1. Rights of trade unions advanced. 2. Government interference diminished.	Employment Insurance System (EIS) adopted.	1. Restrictions on trade unions liberalized. 2. Labor market liberalization. 3. EIS expanded.
Changes in laws concerning collective labor rights	1. Eliminated: restrictions on the form of unions (to enterprise unions); requirements for setting up unions; restrictions on union shops (now allowed with a 2/3 member vote); government authority to dismantle unions; securities (equity) and coal industries from the scope of public interest industries. 2. Eliminated the prohibition of unions' political activities. 3. Relaxed the prohibition of third-party involvement. 4. Restrictions on defense industry strikes to public interest industries. 5. Limited the scope of public interest industries.		1. Multiple unions allowed at the national level (delayed for 5 years at the enterprise level). 2. Fulltime pay to fulltime union officials prohibited (delayed for 5 years). 3. Eliminated restrictions unions' political activities and third-party involvement. 4. Union membership of laid-off workers maintained until Central Labor Committee's decision. 5. Allowed the use of replacement workers during strikes. 6. Prohibited payment of wages during a strike. 7. Reduced restrictions on defense industry's strike. 8. Law on workplace committee for civil servants adopted. 9. Special law on teachers union adopted.

Table 4.1: Three cases of labor market policy reform since 1987 (continued)

	Case 1: 1987-89	**Case 2: 1993**	**Case 3: 1997-1998**
Changes in laws concerning individual labor rights (employment protection)			1. Flexible hours adopted (48 hours per week in a given 92 weeks period; 56 hours per week in a given month; and a maximum of 12 hours per day working hours) 2. Collective dismissal allowed for urgent managerial reasons and for mergers and acquisitions (gender discrimination prohibited in target selection; 60 days notice to unions required; priority given to the laid-off when rehiring within 2 years). 3. Mid-tenure payout of the severance payment allowed. 4. Dispatch workers law enacted: allowed in 26 occupations; prohibited if in strike; prohibited unfair treatment in comparison to regular workers.

Source: Sung Hee Lee (2003)

Table 4.2: Wages in manufacturing (Select industries; Earnings per month in Won)

	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979
Food manufacturing	15.7	18.1	19.9	23.5	30.3	40.1	53.3	76.8	102.1	134.4
Growth rate		15%	10%	18%	29%	32%	33%	44%	33%	32%
Wearing apparel, excl. footwear	10	12.1	14.6	15	19.9	25.2	35.8	45.7	60.9	80.5
Growth rate		21%	21%	3%	33%	27%	42%	28%	33%	32%
Industrial chemicals	22.2	26.7	32.4	49.1	58.7	79.1	106.9	132.3	166.6	210.4
Growth rate		20%	21%	52%	20%	35%	35%	24%	26%	26%
Petroleum refineries	30.9	36.6	44.2	61.5	92.3	124.1	179.6	225.1	289	345.6
Growth rate		18%	21%	39%	50%	34%	45%	25%	28%	20%
Iron and steel basic industries	20.9	24.5	29.6	38.7	49	51.3	71.9	103	138.2	167.7
Growth rate		17%	21%	31%	27%	5%	40%	43%	34%	21%
Electrical machinery apparatus, appliances and supplies	15.2	18.7	19	20.2	27.8	37.9	49.8	62.2	79.2	99.9
Growth rate		23%	2%	6%	38%	36%	31%	25%	27%	26%
Total manufacturing	14.3	16.6	18.9	22.3	30.2	38.4	51.7	69.2	92.9	119.5
Growth rate		16%	14%	18%	35%	27%	35%	34%	34%	29%
Consumer prices, gen. indices	7.4	8.4	9.3	9.6	12	15	17.3	19	21.8	25.8
Growth rate		14%	12%	3%	24%	25%	15%	10%	14%	18%
Total manufac. real growth rate		3%	2%	15%	11%	2%	19%	24%	20%	10%

Source: LABORSTA Labour Statistics Database.

Table 4.3: Growth in labor unions in Korea: 1980 - 2004

	Unionization Rate	Number of unions	Number of members
1980	21.0	2,635	948,134
1985	16.9	2,551	1,004,398
1986	16.8	2,675	1,035,890
6/30/1987	15.7	2,742	1,050,201
12/31/1987	18.5	4,103	1,267,457
1988	19.5	6,164	1,707,456
1989	19.8	7,883	1,932,415
1990	18.4	7,698	1,886,884
1991	17.2	7,656	1,803,408
1992	16.4	7,527	1,734,598
1993	15.6	7,147	1,667,373
1994	14.5	7,025	1,659,011
1995	13.8	6,606	1,614,800
1996	13.3	6,424	1,598,558
1997	12.2	5,733	1,484,194
1998	12.6	5,560	1,401,940
1999	11.9	5,637	1,480,666
2000	12.0	5,698	1,526,995
2001	12.0	6,150	1,568,723
2002	11.0	6,506	1,538,499
2003	11.0	6,257	1,549,949
2004	10.6	6,107	1,536,843

Source: Ministry of Labor, Korea

Table 4.4: Average rates of growth per annum in wage and productivity in Korea: 1986 – 2002

	Nominal values		Real values		Non-agriculture GDP		Non-Agriculture employment	CPI
	Wage	Productivity	Wage	Productivity	Nominal	Real		
1986-1990	14.6	12.1	8.8	5.6	18.5	11.6	5.7	5.4
1991-1995	13.7	12.6	7.1	4.5	17	8.6	3.9	6.2
1996-2000	7.2	5.8	3.1	4.5	6.8	5.6	1	4.0
2001-2002	8.6	4.7	5.0	2.4	7.9	5.6	3.1	3.4

Source: Ministry of Labor, National Statistical Office, Bank of Korea, as cited in Jung (2003).

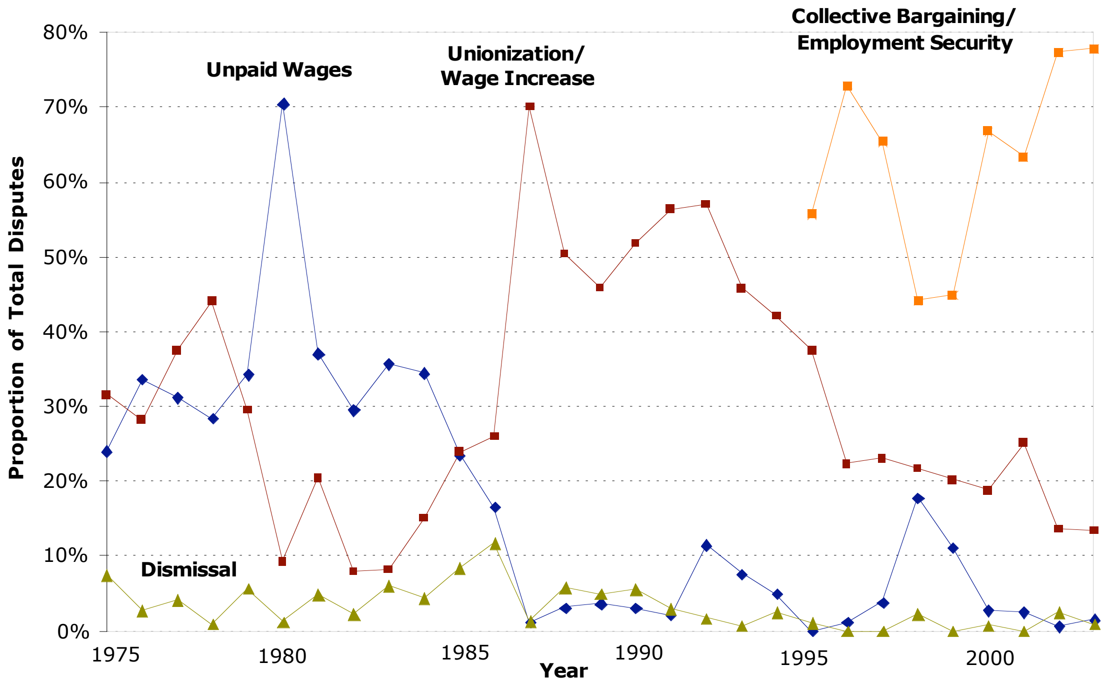

Figure 4.1: Causes of labor disputes in Korea, 1975 – 2004 (Ministry of Labor, Republic of Korea)

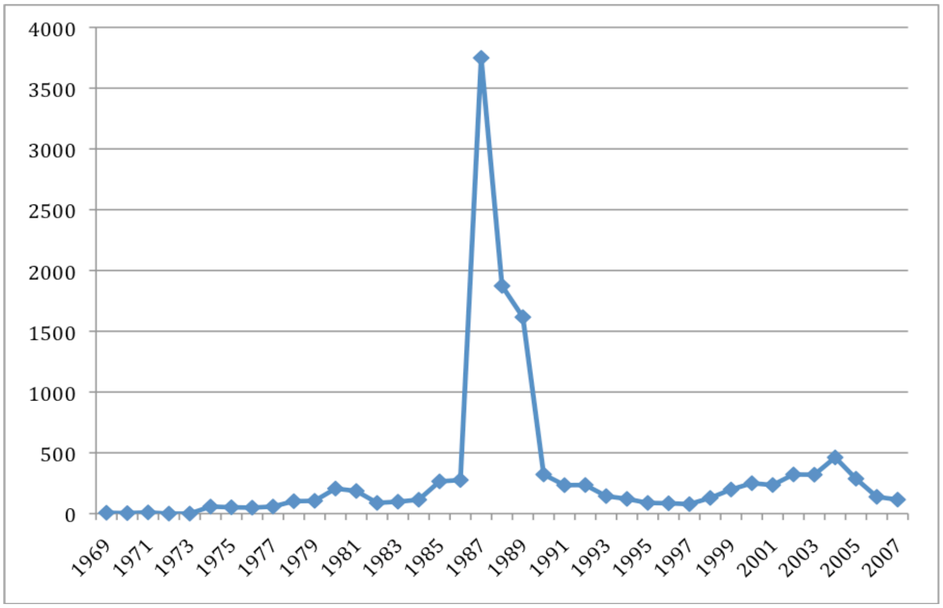

Figure 4.2: Number of strikes and lockouts, Korea, 1969 – 2007 (LABORSTA Labour Statistics Database)

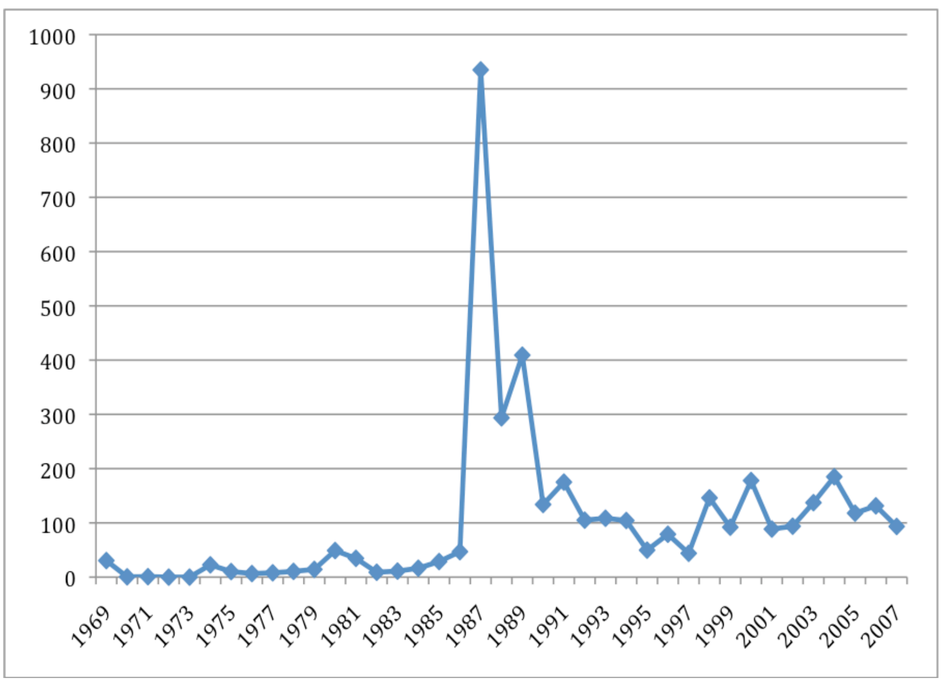

Figure 4.3: Number of workers involved in strikes and lockouts (in thousands), Korea, 1969 – 2007 (LABORSTA Labour Statistics Database)

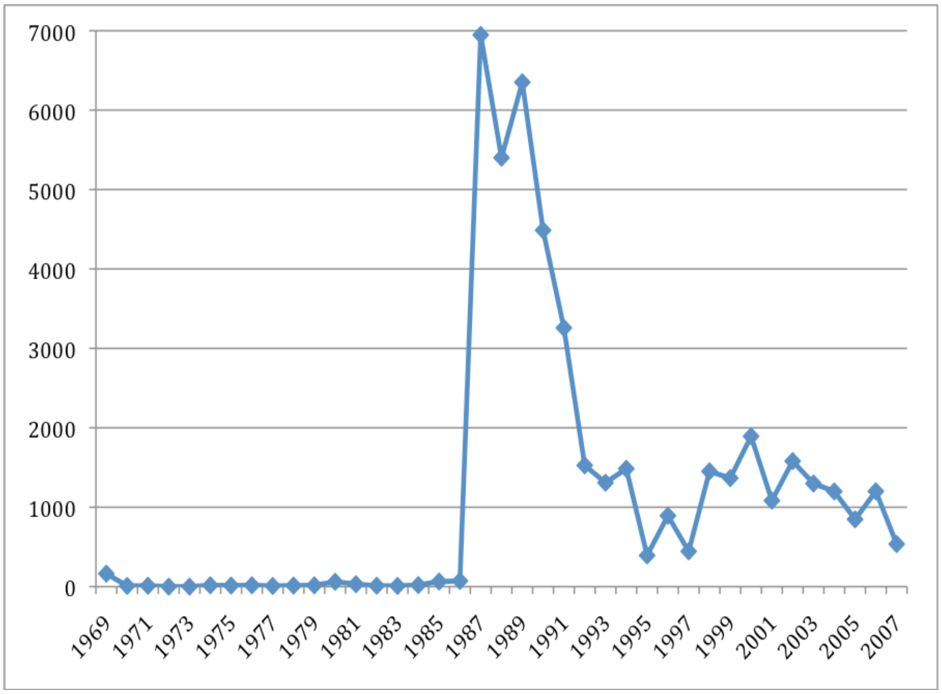

Figure 4.4: Number of days lost to strikes and lockouts (in thousands), Korea, 1969 – 2007 (LABORSTA Labour Statistics Database)

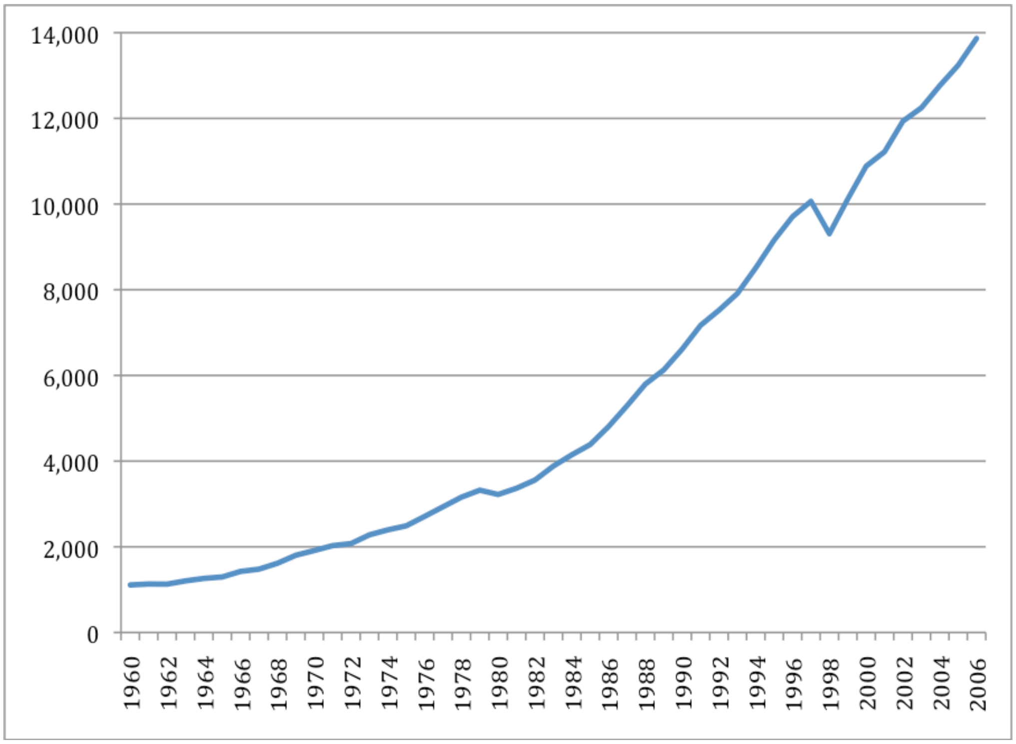

Figure 4.5: Korea's GDP per capita (constant 2000 US$), 1960 – 2006 (WDI)

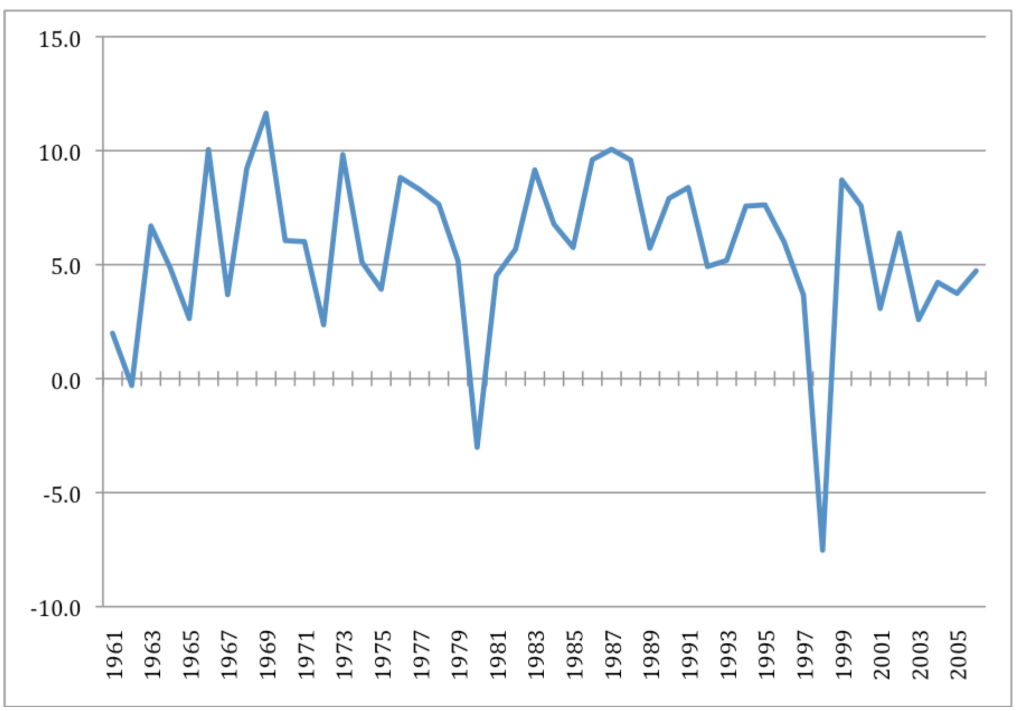

Figure 4.6: Korea's GDP per capita growth (annual %), 1961 – 2006 (WDI)

Chapter 5: Conclusion

This dissertation examines the political economy of labor market institutions in the area of employment protection, which regulates hiring and firing procedures and thus largely determines the overall flexibility (or rigidity) of the labor market and the level of job security for workers. As these rules define the type of contract, length of employment, and the manners in which a worker or a group of workers are let go from their job, both employers and employees as individuals and as collective units invest much political capital to shape and sway the rules in their favor. Employers desire flexibility in hiring and firing, while employees desire restrictions given that these rules directly affect profit (for employers) and income (for workers). Employment protection legislations (EPL) are thus at the center of labor-management disputes in several industrialized countries, especially in Western Europe and Asia.

When are these conflicts likely to arise? Who wins and loses, *i.e.*, what policy outcomes are likely, and why? The theory developed in this dissertation predicts the choice of labor market institutions—employment protection regimes in particular—results from a political bargain between business and labor, a bargain that is conditioned not only by shifts in labor power, but also by the existing set of labor market institutions that shape the preferences of labor and business. Where there is little employment protection, an increase in labor power—brought on most prominently by democratization—prompts workers to bargain for more protection, raising the likelihood that there will be more employment protection. Where workers already enjoy substantial employment protection, however, a decline in labor power—brought on most prominently by economic openness and financial crisis—encourages employers to demand labor market flexibility. In these particular circumstances, employers may reverse their traditional opposition to social policy commitments and compensate labor by offering, among other things, unemployment insurance (UI) to overcome labor opposition to market liberalization.

These conjectures are tested through a quantitative analysis of inter-temporal variance in EPL between 1997 and 2006 on a sample of 84 countries in the world (Chapter 2); in the middle-income countries in East Asia through a comparative case study (Chapter 3); and in the Republic of Korea through an in-depth historical-institutional case study (Chapter 4). Some of the main empirical findings of Chapter 2 include: countries that initiate unemployment insurance (UI) are more likely to reduce overall employment protection, driven by the easing of rules on firing; globalization, measured as changes in trade openness and inward flows of foreign direct investment (FDI), surprisingly does not have any discernable impact on employment protection; contrary to prevailing expectations, economic growth in general and growth in manufacturing in particular are associated with labor market liberalization; and lastly, the higher the initial level of employment protection in 1997, the more likely it is that there will be labor market liberalization in the following ten years.

Narrowing down the focus of analysis to East Asia in Chapter 3, we learn that democratization in Indonesia, prompted by the financial crisis in 1997-98, raised Indonesian labor's political and organizational power, which they used to consolidate and enhance EPL in their favor through the 2003 Manpower Law. It further maintained the new rights against employer pressure to liberalize them in 2006 by staging mass strikes and disrupting business operations. Countries that maintained an authoritarian style of government (*e.g.*, Malaysia and Singapore), on the other hand, did not experience any changes in the type and level of employment protection provided to labor. The Malaysian authorities withstood democratization pressures during the height of the crisis, which in turn allowed the authoritarian (or semi-authoritarian) government to maintain its liberal labor market policies. In terms of globalization, economic openness in trade and finance did not exert any notable pressure on employment protection policies as long as authoritarian regimes stayed in power.

Chapter 4 then examines three episodes of labor-management conflict over protections in the Republic of Korea, chosen according to variance in the three key explanatory variables of democratization, economic openness, and financial crisis. What makes Korea so fascinating in regards to EPL is that it Korea first established restrictive, *labor-friendly* employment protections during its authoritarian, developmental era. Even as the government denied labor's collective rights, it provided job security through stringent rules on collective layoffs and policies that promoted long-term employment relationships. This restrictive and protective status quo labor regime at the time of democratization shaped the politics of labor in subsequent periods in a critical way.

Democratization in 1987, combined with favorable economic conditions, increased labor's bargaining power over employers, which it used to not only maintain the existing protections, but also to improve labor's collective rights, organizational capacity, as well as wages and working conditions. Facing increased competition in the world market and diminishing government support domestically in the 1990s, however, employers began demanding labor market liberalization. In anticipation of and preparation for future labor market liberalization, the conservative Kim Young Sam government enacted the unemployment insurance (UI) system in 1993 with the support of both labor and employers. Then came the financial crisis in 1997-98, which weakened labor's bargaining power vis-à-vis employers. The rapid deterioration of the economy necessitated a renegotiation of the rules on employment protections, forcing labor to accept the legalization of redundancy layoffs, temporary work agencies, and other liberalizing measures, while gaining additional collective rights and expanded social compensation.

These empirical chapters together show the causal importance of economic openness (including regional financial crises), regime change, the policy status quo, and compensatory policies such as unemployment insurance on inter-temporal variation in EPL. The main theoretical contribution made here is in clarifying the conditioning impact of status quo institutions on actor preferences as well as policy alternatives. The traditional assumption that employers are opposed to social policy development (in power resources theory) or that employers support social policy when they desire skill development (in varieties of capitalism) is based on the experiences of advanced industrialized economies. The Korean case shows that employers can also support social policy and welfare state development when they find them to be a necessary prerequisite to gaining greater managerial freedom in hiring and firing. In these situations, we see a decline in labor power resulting in both the advancement of social policy (unemployment insurance in particular) and labor market liberalization. And what makes employers desire greater managerial freedom? One of the main reasons or causal factors is intensified competitive pressures that comes from economic openness and reduced protection in the product market.

On the empirical front, the new data illuminates how EPL has changed between 1997 and 2006 and whether there has been a ‘race to the neoliberal bottom’ in employment protections. The answer is a qualified no, given that countries in Europe, America, the Middle East and North Africa, and Sub-Saharan Africa increased their EPL on average, with only Asia and the former Communist region reducing their EPL. Although countries that accelerated their global economic integration tended to liberalize EPL at the margin, it cannot be said that there has been a global trend of convergence in EPL since the mid-1990s. Lastly, the study shows that the impact of globalization is conditional on the regime type.

There are a few reasons, however, to be cautious about the findings reported in this project. First, as with many statistical analysis, errors in data are a major concern. Especially since the new inter-temporal data is of only two periods, the findings are not only based on this particular time period, but the impact of any potential data error is all the more heightened. To remedy this potential problem and to enhance the scope of analysis, I would like to extend the data on EPL to previous decades, to the 1970s and 1980s. The World Bank’s Doing Business project dates back only to 2003, and OECD’s data on employment protection legislation is limited to its member states and to laws as of the late 1980s. Developing more refined and comparable data on employment protection, labor unions, business associations, and the like, which extend beyond the developed countries would greatly aid a better understanding of the politics of globalization.

Second, other causal mechanisms at work may have not been fully explored as a result of case selection. For instance, the Philippines did not change its EPL even though it democratized in 1986. Thus, the lack of regime change, which accounted for Malaysia and Singapore's stasis in EPL, does not apply to the Philippines. More research is needed to strengthen the findings' generalizability.

One avenue of future research is to explore the link between labor market policies and social insurance or welfare policies beyond unemployment insurance. Loss of a job not only entails a loss of income but also a potential loss of company-based health, pension, and other benefits. Thus, political bargains leading to labor market liberalization may also entail expansions in these other social policy instruments.

Another avenue is to tease out the politics of labor market institutions by looking deeper into the policy preferences of different kinds of employers and producers (large vs. small enterprises, export vs. import industries, etc.) and of labor (formal vs. informal workers, export vs. import industries, etc.). Policy preferences are likely to diverge even within the same class of socio-economic agents, and understanding these differences would enhance the analysis of labor, trade, and investment politics that are at the core of modern economies.

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