Crisis in a Global Economy. Re-planning the Journey
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THE IMPACT OF THE GLOBAL RECESSION ON DEVELOPING COUNTRIES

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1. Introduction

In a paper entitled 'Global Economic Recession: Effects and Implications for South Africa at a time of political challenges' Padayachee, a research economist from the University of KwaZulu-Natal suggests that, as a region, Africa has suffered from the downturn and cites the International Monetary Fund (IMF) which has placed growth estimates as having been lowered from 5% in 2008 to 1.7% in April 2009 (Padayachee, V. 2010:1). Africa may not be typical of the developing world with which it shares vital socio-economic features. The globalization of the economy has, however, placed together most developing countries such that, in economic terms, it is safe to generalize. I shall, therefore, use mainly Africa as a point of reference to illustrate how the recession has impacted on the developing economies.

At the Africa Group meeting of 20 March 2009, José Manuel Salazar-Xirinachs, Executive Director, Employment sector of the International Labour Organization (ILO), made two principal predictions with regard to the impact of the global recession. The first was that '2009 is a year in which labour markets around the world will be hit hard'. And the second was that '2009 will be the first year since the Millennium Development Goals were launched in which globally poverty will not be reduced but instead will increase' (ILO Global Crisis Observatory 21 May 2009:1). The two predictions have far reaching consequences for the developing world as it is here that individuals and groups are most vulnerable to the vagaries of the economy. A dramatic decline in the labour markets saturates the informal economy adversely as, contrary to conventional economic wisdom, the informal economy cannot act as a cushion to the formal economy in times of a global recession as the data will show in the following sections of this paper. Secondly, adverse effects on the informal economy have dire consequences on poverty and consequently on food security.

Theoretically, all other things being equal, the capacity of states to dispense public goods and services is a function of their economic capabilities. Secondly, political stability within the state is a direct outcome of the capacity to dispense public goods and services. The data in the following pages shows that the recession works against the poor in two ways:

i) The slump in economic activity triggers job losses which in turn impact on the lowly paid in precarious employment; and
ii) The slump in economic activity reduces the fiscal capacity of the state thus impacting on the pro-poor social programmes.

Besides direct economic effects, the recession has serious negative social consequences. As the Executive Director puts it: 'as the recession bites, poverty reduction unravels and the middle classes worldwide are weakened, the risk is that social and political tensions will multiply' (*ibid.*).

In this paper I shall adopt a two-pronged approach to the impact of the recession on developing countries. The first shall comprise an analysis of the impact on macro level factors such as unemployment, reduced commodity prices, reduced trade, foreign aid, etc.; and the second will be on how these factors impact at the household and individual levels. The macro level data is drawn from meetings, workshops and symposia of the ILO in Africa, while micro-level data comes from a study initiated and led by Women in Informal Employment: Globalization and Organization, and conducted in Latin America, Asia and Africa in 2008 – the *Inclusive Cities Project*.

2. Macro-Level Factors

The anatomy of the global recession in developing countries follows a simple logic. Developing countries rely mostly on exporting unprocessed goods, mainly minerals and agricultural produce. Because of reduced financial flows in the developed world, there is a decline in trade leading to reduced demand. This immediately leads to a decline in commodity prices and, in the words of the ILO Global Crisis Observatory, 'reduced liquidity and tightening of credit markets affecting both public and private sectors, reduced flows of remittances, a drop in Foreign Direct Investment (FDI), exchange rate depreciation, and declining flows of Official Development Assistance (ODA)' (*op. cit.* 2). Undoubtedly, it is the developing countries that are at the receiving end in such a situation. What suffers most in this instance are: growth, employment and livelihoods.

2.1. *Growth*

At the Preparatory meeting of experts on the First African Decent Work Symposium held in Addis Ababa on 27-28 February 2009, the meeting noted that: 'the financial and economic crisis has put at risk Africa's growth and development prospects. In its latest update of January 28, 2009, the IMF predicts that, as a direct consequence of the global financial crisis, Africa's growth will drop to a low rate of 3.4 percent in 2009' (ILO: Preparatory Meeting of Experts on the First African Decent Work Symposium 2009:2). This was to be against growth figures of 6.2 and 5.2% in 2007 and 2008 respectively. The consequences of shrinking growth would express in increased unemployment, a reduction in the states' capacities to provide social services and almost no social security safety nets as is the case in almost all Sub-Saharan African states; and forcing precariously placed workers into an already large informal economy.

Africa's economic fate, for instance, is closely interlinked into the global economy through five key sectors:

i) Exports of raw materials from mining and agriculture;
ii) Exporting human resources which results in remittances from the host to the guest countries;
iii) Capital inflows through foreign investment and bank loans;
iv) Earnings from tourism; and
v) Foreign aid.

The recession affected all the above factors in various ways leading to reduced revenues in all respects.

2.2. *Employment*

The meeting highlighted 'cases of company closure, postponed or cancelled investments (mainly in mining, auto finance/banking) and job losses across the continent'. In particular, the meeting noted a loss of 300,000 mining jobs in the Katanga District in the Democratic Republic of the Congo; and 36,500 jobs in the South African auto industry (*ibid.*). The ILO Observatory noted that Zambia had to pay off 3,072 copper miners as a result of the slump (ILO Observatory, *op. cit.*). What exacerbates the impact of job losses in the formal economy is the increase in vulnerable employees (unpaid family workers and own account workers as a share of total employment). The ILO Observatory noted that in Africa the ratio of vulnerable employees had increased by 5 percentage points between 2007 and

2009 pushing the figure up to 81.8 percent. In absolute numbers this represents 28 million persons or an additional 36 million persons earning less than US$1.25 per day. This translates into 67.2 percent classified as the extreme working poor. This has a severe impact on growth, poverty and job creation. The effect of this crisis is that it has reversed the modest gains that Africa made during the growth period up to 2007. As the ILO Observatory states: 'social policy in Africa has not transitioned from a programme-based logic to a truly integrated view of inclusive-growth with social protection and decent work. And in contrast to Latin America, a number of African countries have less fiscal room to maneuver' (*op. cit.* 4).

2.3. *Livelihoods*

There are two ways in which the global recession impacted on the generation of livelihoods in developing countries. The first was a decline in direct investment, and the second was in transfers through tourism and remittances. Activities such as tourism which fall within the small sector suffered as a result of the global recession. For instance, between January and June 2009 the Tanzania Association of Tour Operators reported a drop of between 30 and 50 percent in American and European tourists. In Kenya hotel and bed occupancy declined by between 20 and 30 percent. Another sector that was hit is the NGO sector which relies largely on international donors mostly from Europe and North America. Most NGO work is in the social economy (co-operatives and self-help groups funded from foreign humanitarian aid agencies) and as sources of funding diminished in donor countries, less reached the developing world thus reducing NGO activity. Finally, as the recession hit the developed world most, guest workers were the first to lose jobs and with this, remittances to the home countries fell thus reducing livelihood opportunities.

2.4. *Impact on Policy*

In this instance I shall use the example of South Africa. The most developed economy in Africa is that of South Africa. Despite the level of economic development and an advanced social security system, South Africa did not escape the negative impact of the recession. Padayachee states: 'The country's Gross Domestic Product growth dropped to 1.8 percent in the last quarter of 2008, and then plunged to -6.8 percent in the first quarter of 2009, and to -3.2 percent in the second quarter. So the country fell into a technical recession already at the end of the first quarter of 2009' (Padayachee, V. 2010:4). In addition, '484,000 workers lost their jobs in the third quarter of 2009, the largest number in manufacturing (about 150,000): the total job losses were more than the combined totals of the first two quarters of that year...' (*ibid.*).

Padayachee goes on to draw on policy implications of the recession and selects one of the main pillars of South Africa's post-apartheid restitutive policies – Black Economic Empowerment (BEE) which the country considers as an imperative in the transformation of the economy. BEE deals use money loaned from merchant banks to finance the purchase of shares by blacks from existing companies. As he puts it, 'The lack of finance in the quantum needed for BEE deals creates not only a heavy reliance on the "once empowered", the merchant bankers and others (the real beneficiaries) who just lie below the surface of these deals' (*ibid.* 11). However, what is critical in this instance is that the financial crisis has affected the number and character of deals and thus impacting on the country's social policy, and probably the stability of the social transition. Padayachee contends that a number of companies 'have cut back on dividends' thus 'straining the environment for empowerment deals'. He cites the Financial Mail of April 3, 2009 as saying: 'This creates the danger that the banks that funded the deals will call up the debt, forcing the black investors out of the company'. And continues: 'Industrial conglomerate, Barloworld, offered 10 percent of its shares to black investors at R83.31. But since the recession stock prices decreased by 60 percent and were valued at just R33!' (*ibid.*). The result has been a massive decrease in BEE activity prompting Padayachee to aver that 'South Africa's plan to transfer about 25 percent of the country's wealth to black people by 2017 is increasingly looking like a fantasy' (*op. cit.* 12). In short the South African example demonstrates how the recession could derail government policy thus causing social instability to the political system. In societies already torn by poverty and strife, the consequences could be devastating. But, perhaps policies such as BEE might be limited to resource rich countries and not all African countries have an equity problem where race is the causal variable.

3. Micro-Level Factors

The impact of the recession at the household and personal level is best demonstrated in a study carried out by Women in Informal Employment: Globalization and Organizing (WIEGO) in coordination with the *Inclusive*

Cities Project. The research was carried out in 10 countries in Africa, Latin America, South and South East Asia on informal workers engaged in street vending, waste picking and home-based work. A total of 164 informal workers participated in the study which used both focus groups and individual interviews as a basis of data collection. Results of the survey demonstrate how the recession impacted on individuals, households and groups.

3.1. *Decreased Demand and Consumption*

The study reports that the recession has had a marked impact in low income countries especially on informal workers. Decreased demand resulting from a decline in export trade and direct investment as well as from shrinking commodity prices has caused a slump in both the formal and informal sectors. Inside the poor countries the buying power of local consumers declined thus reducing demand. Retrenched and underemployed workers have had to curb their own consumption. Participants in the study reported a decline in their trade volumes between January and June 2009, with only 10% reporting an increase while 23% maintained that their trade volumes remained the same. The hardest hit was industrial home-based workers producing goods for export (*Inclusive Cities Study* 2009).

3.2. *Price Instability and Rising Costs*

The recession brought about an increase in production costs while stifling the selling price of goods produced. The study reveals an increase in the prices of both raw materials and ready-made goods. As most of these constituted inputs in the informal business, informal sector practitioners had thus to absorb these costs against declining selling prices. In addition, utility costs for gas, electricity and transportation rose. The study cites mat producers in Pakistan who had to sell their goods to dealers in a town 30 kilometres away and exported to Iran. First the cost of reed which the producers used as raw material rose, then a rise in fuel prices precipitated an increase in transportation costs. By the end of six months buyers were looking for local producers in an effort to control costs.

Rising production costs against depressed local demand brought about a vicious cycle. Either producers had to increase the selling price against low sales volumes or increase their production and bank on the economies of scale. Where practitioners dealt in non-durable or perishable goods there were few if no options. In a majority of instances practitioners decreased their selling prices (41%) while almost a third (29%) adjusted their prices upwards while another third (31%) kept their prices the same. With decreased profit margins the only alternative was to increase working hours in order to increase production. This reduced parenting and nurturing tasks thus introducing a negative social dimension to family life.

3.3. *Household Level Impacts*

The recession precipitated a rise in commodity prices including food and transportation costs. It is common cause that in poor households an inordinate portion of the budget is spent on food and transport. Respondents in the survey reported a drop in the quantity and quality of household food. This entailed a reduction in the number of meals taken per day from two to one in a period of six months. Others reported sacrificing 'luxury' items such as meat and milk from their meals and substituting them with relatively cheaper items such as eggs and offal or 'guts'. In some instances adults forewent their meals in favour of their children. Some respondents sacrificed items such as leisure and clothing in favour of basics such as children's education, food and shelter.

Within the household the dynamics changed as unemployment shifted the dependency burden to informal workers, mostly women. Almost one in five respondents reported that someone in the household had lost a job since January 2009. The research quotes the South African Quarterly Labour Force Survey detailing that 85 percent of jobs lost between January and June 2009 were in the domestic and informal sectors (p. 19).

3.4. *Increased Competition within a Shrinking Market*

The *Inclusive Cities Study* dispels the myth that the nature of the informal economy gives it flexibility to cope with shocks and economic downturns. Respondents in the survey reported that more workers had entered their segment of the informal economy. This observation was more pronounced among street vendors where one in four respondents (85%) reported this, and this was followed by waste pickers (49%). The new entrants were mostly women as greater absolute numbers became engaged in the informal economy against a shrinking market (as unemployment increased together with the cost of living, there was less buying power in the economy); increased competition entailed a substantial decline in per capita revenue among informal workers. In total the recession meant diminishing livelihoods in the informal economy.

Informal workers were caught in a vicious cycle. Increased competition led to declining incomes in all the three segments surveyed. Despite the falling incomes very few of the respondents surveyed had attempted alternative or additional employment. In the survey only a quarter of the respondents reported supplementary sources of income. Understandably, informal work is a last resort when individuals cannot find employment in the formal economy. The informal sector has no security and conditions are generally severe. Faced with no alternatives informal workers resorted to further short term survival strategies. Admittedly, the strategies added more risk and uncertainty. Strategies ranged from decreasing stock or production particularly among street vendors trading in perishable goods, to increasing the number of hours or days at work. These were huge sacrifices given that informal workers have very little leisure time.

4. The Response

In this section I shall focus on the South African response for two reasons. The first is that because of its advanced economy in Africa, South Africa has the capacity to respond independently outside of international interventions such as foreign aid and humanitarian grants. The second is that South Africa has developed domestic policies such as the social grant and the Expanded Public Works Programme which enable it to leverage its responses to crises. Also South Africa has an advanced statistical base from which reliable analyses can be performed.

In February 2009 following consultations with the National Economic and Labour Council (NEDLAC), (a social accord between government, labour and business) the government issued a Framework outlining its response to the crisis. The Framework outlined three mechanisms by which government intended to alleviate the effects of the crisis. The first was to minimize job losses, the second was to scale up social welfare programmes and the third was to accelerate access to basic social services such as housing, clean water and sanitation including electrification.

4.1. *Alleviating the Impact of Job Losses*

The Framework urged companies to do everything to avoid job losses and promised tax relief to compliant companies and other measures to rescue companies in distress. The Framework further urged companies to take advantage of the slow down by accelerating staff training programmes thus investing in their people. Finally the Framework stressed government's determination to consolidate the Expanded Public Works Programme as the engine of job creation. Critics of this aspect of the Framework placed emphasis on the problematics of bringing about any job creation within a capitalist labour market framework. Both Jacobs (2009) and Padayachee (2010) maintain that the government is resolute in its commitment to the concept of 'no distribution before growth' as espoused in the Growth Employment and Redistribution policy (GEAR) and propounded in 1996. Critics of the policy have alleged that it resulted in 'jobless growth' between 1996 and 2007 and was, therefore, woefully lacking in its redistributive commitment. In essence, Gear did create skilled jobs while at the same time causing more unskilled jobs to be lost as investors put profits before humanitarian motives. Because of the nature of the model of job creation proposed in the Framework, Jacobs is skeptical of the capacity of the proposals including the Expanded Public Works Programme to create decent jobs. He claims 'when corporations do decide to invest in a few skilled workers this tends to increase unemployment rather than reduce working hours for the sake of sustainable expansion of decent jobs' (*Review of African Political Economy* 2009: 616).

4.2. *Scaling Up Social Welfare Programmes*

South Africa has a well-developed social safety net starting with a universal means tested old age and disability pension, a free health service for pregnant mothers and children under six, an unemployment insurance system and a child support grant for indigent children under sixteen. Jacobs states: 'It is estimated that at least 12 million South Africans (or 25 percent of the population) receive social grants with the number of beneficiaries steadily increasing over the last decade' (*ibid.*). It is also common cause that these grants reach the poorest households and, at times, comprise the sole source of livelihoods. When considering that effective unemployment stands at 32 percent of the economically active age cohort or 5,598,400 in absolute numbers, as a relief measure the social grant is not insignificant. However given the size of the social grant against growing inflation, it is necessary to appraise the plight of the poor within a more complex holistic context. Also, there are competing appraisals of the impact of the social grant in the overall economy. Citing neo-classical labour economists, Jacobs alludes to their claim that 'social welfare grants pegged at high levels discourage the unemployed from seeking work and cultivate dependency on the state' (*ibid.*).

4.3. *Expanding Access to Basic Social Services*

Even much earlier than the onset of the recession South Africa already had a policy of giving rations of free water and electricity to poor households. However, as soon as these households exhaust their free quota, they pay for their consumption, like everybody, on the basis of the charges prescribed by private companies that control the reticulation networks. While in principle government is committed to a policy of universal access to portable water, clean sanitation, housing and electricity, this goal is far from accomplishment. The failure to achieve this has resulted in violent protest action reminiscent of the apartheid days. Part of this cause is the extremely inefficient and corrupt local government system. In the past three years a number of municipalities were declared dysfunctional and some placed under curatorship. This is, therefore, an aspect of the Framework that will need strong political goodwill to accomplish.

4.4. *Other Measures*

Padayachee lists additional measures effected by the South African Reserve Bank to alleviate the financial crisis. These include: 'using moral suasion to get the banks to tighten their lending criteria, while letting credit to flow; further improving banking regulations and supervision, while avoiding the dangers of over regulation; and successively lowering gradually the repo rate (so influencing onward lending rates' (Padayachee, *op. cit.* 13).

5. Conclusion

While the global recession did not change relations between north and south, it definitely postponed the opportunity of the south to reduce their dependency upon the developed countries. The period from the beginning of the millennium to the onset of the recession has been the epoch of unprecedented growth in the third world and notably in Africa where dependency on international aid is high. The World Bank reported that Africa's growth in 2009 would drop by 66% from the 2007 figures, whereas before the recession it was around 6 and 7%. In addition, the healthy growth was 'complemented by the emergence of Africa as a vocal political actor, promoting regional and continental integration, active conflict resolution and in governance, for example, the African Peer Review Mechanism' (ILO Conference on the Social Economy 19-21 October, 2009:3). These are gains that the recession has offset and my take long to recover.

Secondly the recession has hit labour markets hard and particularly the vulnerable groups and informal workers. Significant job losses especially within the unskilled and precariously employed ranks drove large numbers into the informal labour market thus exacerbating conditions within an already fragile sector. The extreme working poor increased significantly as dependency ratios increased with an increase in job losses, household incomes dropped resulting in decreased food intake. Remedial measures only added to the lot of the poor as informal workers resorted to working longer hours and increasing production against decreasing prices. Predictably, women bore the brunt of the recession.

Thirdly, developing economies are characterized by huge disparities between rich and poor. The recession might have deepened these disparities thus widening the social schisms and providing grounds for relative deprivation and the consequent social unrest. Already in South Africa protest action has intensified since the beginning of 2009 and is currently on the increase. The last six months have witnessed marked protest against poor delivery of services in the townships often accompanied by violent confrontation between protesters and the security forces. Where states have even less capacity to offer social services, and less political legitimacy, conditions might even be worse and could easily culminate in uncontrolled chaos. Zimbabwe's example of the outbreak of the cholera epidemic in mid 2009 is a case in point. The danger is that such conditions might easily spread across the region.

Finally, on a positive note, observers suggest that while the recession admittedly had a severe economic impact on the continent; this was limited to resource rich countries in Sub-Saharan Africa. The African Development Bank wrote in January 2010: 'It appears that resource-rich countries in Sub-Saharan Africa suffered the largest setback. In contrast, resource poor, landlocked countries have weathered the global downturn relatively well, and are expected to record the highest rates of growth on the continent in 2009' (African Development Bank January 12, 2009:2).

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