# "Improving Wages" to fight poverty in less-developed countries

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**Europe's 500 – Entrepreneurs for Growth, the european association for growth entrepreneurs (www.eu500.com) is not only concerned with services to their members but also wants to contribute to society with regards to issues of growth.**

As economic growth is the driver to improve living conditions and reduce unemployment, it is therefore top priority on the European political agenda. The association is gathering the European elite of growth entrepreneurs. It develops initiatives to improve growth supported by the ideas and experiences of the entrepreneurs.

The association currently focuses on four main initiatives:

1. Improved financing for innovation and growth.
2. Entrepreneurial education.
3. Paneuropean entrepreneurship.
4. Fair wages in the developing countries.

This article will explain the basic idea, the theory and the concept of the fair wages initiative. Fair wages need multilateral incentives. The industrialized nations (for example the EU) should lower trade barriers for the export from the developing countries linked to an improved social and environmental framework. Such links are not new. The initiative wants to especially prove and emphasize the positive impact of including a regime of gradually growing minimum wages into the international trade policy. Fair wages in the developing countries should drive local demand. At the same time this shall reduce the export of jobs from the high wage to the low wage countries and increase the export of capital goods.

In this context this article looks at three important aspects:

1. Market failure: Why does the liberalized pure market economy not take care of this problem in a reliable and sufficient form?
2. Impact of wages: How does the minimum wage correlate with the major indicators of the welfare and population growth of the countries?
3. Financing of wage increases: How can an increase of minimum wages be financed?

**Aspect 1: Where do markets fail?**

We need to analyse where it is necessary that governments interfere to make markets work better. Everybody acknowledges that the state needs to regulate issues like antitrust, environment, social support, etc. Our hypothesis is that minimum wages need to be regulated and enforced by law, especially if social support is insufficient.

We want to prove that minimum wages can become a key economic steering parameter such as interest rates and monetary policy. Today any company can circumvent our social and ecological system by globalisation which leads to the consequential damages for environment. We also want to prove that rules on minimum wages can have a similar justification for the functioning of the markets as the antitrust laws.

Those special market situations cannot function where the price is not able to create an equilibrium between offer and demand. E.g. the free market cannot find a price for resources that apparently seem to be available in limitless excess (water, air and in the same way unskilled labour), even though those resources need to be protected in the interest of society. If there is a systematic, not absorbable oversupply of unskilled labour (because of the lack of a social support system), the employers have a quasi monopoly negotiating position on salaries. Employers in the poorest hundred countries can therefore fix the wages between 10 and 20 cents per hour and the employee has the choice to accept it or to have no money at all.

The oversupply comes from the fact that also the old, the children, the sick and the mothers are looking for jobs as they are very often not protected by any social system. On the other hand full employment provides jobs to about 40% in a society with division of labour. So there is either a social welfare system or the other up to 60% of the population will fight for non-existing jobs to prevent starvation. This relation between the lack of social support and thereby caused oversupply of job candidates keeps the markets unbalanced and puts employers into the quasi monopoly position. It is a market situation where no price can create the equilibrium. Even if the price would drop to zero, there would not be jobs for everybody. Therefore the price for unskilled labour is so low that it prevents the larger part of the population to participate in the economic exchange system as regular consumers.

The EU is investing huge amounts into development aid and billions of dollars into agricultural subsidies that allow our farmers to compete with the low-wage farmers. So far, most of this aid in agricultural subsidies has been partly counterproductive (in combination with a pseudo-opening of our markets) because they prevent the poor countries from being able to raise their wages, and therefore this creates continuous conflict and debate between the north and the south.

In this project we want to investigate the possibilities of gradually reducing European agricultural subsidies in exchange for higher minimum wages for instance in the agricultural sector of exporting countries without damaging both sides' competitiveness.

**Aspect 2: Impact of wages on social welfare**

We want to demonstrate that all factors of living conditions from population growth to education, illiteracy, health, criminality, etc. clearly correlate with the minimum wages. Therefore, almost all desireable improvements can be achieved at the same time by only improving the one parameter which is the minimum wage.

This hypothesis is supported by a variety of data sources using a computation of data from 52 different nations world-wide in four different income groups (up to \$1000, \$1000-\$3000, \$3000-\$6000, \$6000-\$9000, over \$9000 per year).

Our key findings can be summarized as follows:

- Life expectancy drops from 78 years to 52 years proportionally to the decrease of income. Only an increase from the low income of \$1000 per capita to the average of \$1500 per capita can increase the life expectancy by 26%.
- Infant mortality increases from 6 per 1000 to 125 per 1000 proportionally to the decrease of income. Only an increase of the per capita income from below \$1000 to an average of \$1500 can decrease the infant mortality rate from 125 to 44 per 1000.
- Illiteracy increases from 0.3% to 40% proportionally to the drop of income. Only an increase of the per capita income from below \$1000 to an average of \$1500 can lower illiteracy from 40% to 17% and an increase to the next income category (average per capita income of \$3500) will decrease illiteracy to 6.7%.
- The uncontrolled population growth is one of the world's top concerns. It is a common fear that if the world cannot stop population growth, resources become scarce and peace, stability and environment will be increasingly jeopardized. Only when the per capita income reaches \$350 per month, population growth stops.

These impressive statistics show us that the major problems of mankind can be tackled, if we help the poorest to increase their income. If this target can be reached by trade agreements, a combination of protective rules for the poorest and the free market, then we have the chance to work on one of the most efficient parameters for improvement. Our strategy therefore is focused on income as key parameter to solve the main issues simultaneously: income comes first and education, health, etc. follow.

**Aspect 3: Financing of wage increases**

In low wage countries the percentage of salary in revenues in the industrial sector is mostly in the range between 10 to 20%. If unskilled labour accounts for roughly 50% of the workforce, the proportion of minimum wages in revenues varies between 5 and 10%. Only the unskilled workers

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**The EU could reduce billions of dollars of agricultural subsidies in exchange for increased minimum wages in the low-wage countries**

suffer from the problem of limitless oversupply,the amount of skilled workers is limited and so market equilibriums are established at fairer prices. Therefore the gap between unskilled labour and skilled labour income is mostly huge (factor 5 to 10).

A gradual increase in minimum salaries will increase demand and will therefore increase the occupancy rate of factories so that the labour costs can roughly be compensated by economies of scale. The higher production volumes shall decrease the fix costs per unit. The lower fix cost per unit allows for a higher salary cost per unit leaving the total cost at the same level. The idea of our free market system is to let the workers income participate in the increase of productivity. Only the oversupply and absence of social protection prevent workers in these countries to participate. Salary increase will make the internal demand grow, the markets will need more imports in machinery and the unit prices will not necessarily grow.

So a research project, sponsored by Europe's 500 – Entrepreneurs for Growth and the Schoeller Group and maybe also by the EU Commission, will focus on means to offer incentives to gradually increase income in exchange against improved trade policies and trade agreements. If we don't deal with the most urgent third world problems, nobody doubts that they will also become problems of the first-world.


**Summary**

The "wealth of nations" was one of the main concerns of Adam Smith. Today Adam Smith is quoted when the discussion on removing trade barriers focuses on globalization. Globalization offers an enormous exchange of goods and an increase in wealth in a number of developed countries and the "Fast-Developing-Nations" (Schwellenländer in German). For the poorest countries, however, globalization does not yet really improve the situation for the largest proportion of the population and the living conditions remain poor in spite of the globalization. Extremist groups are even blaming globalization as being the reason for continued poverty. So far it has been a big challenge to show improvement (for example in Latin America). The tensions in connection with globalization and third world poverty leads to political unrest and even favour terrorism in some countries. The purpose of this article is to show the correlation of income per capita (wages) and the most relevant social indicators. The article emphasizes not only what is well known – the poorer the salaries the more terrible are the problems – but it wants to create awareness that an increase in income can be the right strategy to solving many of the most important issues simultaneously. An increase in income for the weakest will allow the free markets and the state to provide more of what is urgently needed. The goal is to develop a strategy to really help them to help themselves by creating incentives and mechanisms that lead to an increase of wages.



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