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THE WORKING POOR

A Macro Perspective

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In the last decade I have had the opportunity to listen to and participate in policy discourses on the macroeconomics of development in Africa, particularly in Tanzania and Mozambique. Almost invariably, these policy discourses tended to focus on the growth- poverty nexus. What struck me, however, is that, notwithstanding this focus on poverty, these debates remain largely silent on the question of labour and its condition of employment in the context of economic growth. In other words, poverty is discussed without much reference to the prevailing organization of production and the dynamics of unemployment – open or disguised.

Instead, the dominant approach makes a sharp distinction between the 'poor' and the 'non-poor' and then formulates the problem of development as pulling the poor above the poverty line under the impulse of economic growth. The standard argument is that the adoption of a core package of macroeconomic policies will induce economic growth, which, in turn, will lead to poverty reduction. This core package, often referred to as the 'fundamentals', concerns the promotion of low inflation, trade openness, market liberalization, sound financial policies and good governance. In an influential article on development policy, Dollar and Kraay (2004: 57) argued that: 'our evidence does strongly suggest that economic growth and the policies and institutions that support it on average benefit the poorest in society as much as anyone else'. In other words, according to these authors, the evidence suggests that some sort of trickle-down mechanism, left largely unspecified, is invariably at work. Other contributions tend to be more nuanced by bringing changes in the personal distribution of income – or, as is often the case, of household expenditures – into the picture. The 'evidence' in these approaches mainly consists of cross-country regressions. These regressions then become a substitute for theory. As Lindauer and Pritchett (2002: p. 18) put it: 'one would think that the development community does not need any big ideas since they have the results of growth regressions'.

At the practical level of policy making, the premise that growth reduces poverty has become a veritable mantra in the international development industry, particularly (but not exclusively) in Africa, where it constitutes one of the cornerstones of poverty reduction strategies. More specifically, it is argues that, if GDP *per capita* grows significantly and if inequality as measured by the GINI coefficient (usually derived from successive household budget surveys) does not worsen significantly, it follows that the incidence of (absolute) poverty must fall. One consequence of this is that a lot of time, expense and effort are invested in monitoring the relation between economic growth (as measured by GDP growth) and the incidence of poverty, corrected for changes in inequality. Every five years or so, depending on the frequency with which consumer budget surveys are carried out, domestic policy makers and analysts together with donor agencies eagerly await to see whether and by how much the incidence of poverty fell as a result of per capita GDP growth in the preceding period. When this does not happen – as appears to be the case in Tanzania and Mozambique – a paradox is said to exist.

To be honest, I have grown tired of listening to these debates. Their purpose often seems to have more to do with ticking off boxes in the monitoring of the poverty reduction strategies to justify the continued flows of foreign aid than with coming to grips with what is actually happening within these economies and how economic policy might be able to influence outcomes. Monitoring appears to have taken precedence over analysis and, not surprisingly, since the stakes are high, this often involves quite heated arguments, particularly when such a paradox is said to exists. This, in turn, gives rise to a further plethora of commissioned studies and policy discussions, which invariably focus on the data or on the methods used in monitoring the growth-poverty reduction nexus.

What needs to be challenged, however, is the premise itself: the notion that the adoption of the fundamentals – the core of macro policies that underscore poverty reduction strategies – together with an appeal to an abstract market mechanism will bring about pro-poor growth. In this respect, the US economy has often been taken – explicitly or implicitly – as an exemplar of a model of unfettered “free market” capitalist development, the underlying propositions of which are held to be generally valid. In development policy discourses, particularly since the 1980s, this model and exemplar have blended together in ways that have induced prescriptive policy making in which such propositions have come to assume the status of generally accepted axioms of development (Wuyts, 2011: p. 439). This then justifies making a heroic jump from the growth in GDP per capita to the reduction in incidence of poverty without any specification of the mechanisms that supposedly link them together.

However, a recent study of the boom period of the US economy from 2000 to 2007, just prior to the financial crisis, reached the startling conclusion that “the economy did well, except for the people in it” (Mishel *et. al.*, 2009: p. 47). This should help to remind us that the growth-poverty reduction nexus cannot be taken as an axiom, not even within the confines of a single country, let alone for the purpose of cross-country comparisons. Instead, as this study shows, how well working people fare depends not only on productivity growth, but also on the extent to which it translates into growth in labour earnings and on whether or not this goes hand in hand with employment growth. How these elements combine under the impulse of economic policy can be very different across different countries, even with similar growth rates, and at different historical conjunctures, even in a single country.

Once we accept, however, that market economies do not fly on automatic pilot towards the greater good for all, the question of how economic policy shapes “Who will benefit?” and “What production processes will be fostered?” inevitably comes to the fore (Minsky, 1986: p. 8). This – I would argue – are the real questions that need to be addressed. But this requires that we shift the emphasis back to analysis rather than to monitoring. Indeed, it cannot be assumed that trickle down will automatically happen as a result of growth. Instead, to find out whether or not growth benefits the poor it is necessary to bring production, accumulation and the condition of labour back into the picture, thus making the underlying mechanisms visible.

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That growth can go at the expense of the poor is not just a theoretical possibility. Nor is it a new idea. The pioneers of development economics were perfectly well aware of the practical implications of this possibility. Kalecki, in particular, showed that economic growth could go at the expense of poor if it went hand in hand with inflation in the prices of necessities. Looking at the experiences of Mozambique and Tanzania, particularly in last 10 to 15 years, tells me that it still is a real danger. Listening to policy debates in Africa today, however, it strikes me that Kalecki's ideas have largely been forgotten or discarded. Yet, judging by recent experiences, the problem he raised in the past has not gone away today. Instead, it has resurged with increasing vigour, particularly in the last 10 years. It makes sense, therefore, to revisit the ideas of Kalecki, not to dwell in the past, but to look at the future.

Kalecki's concern was not with inflation in general, but with one particular type of inflation: namely, the a persistent rise in the price of necessities as a result of economic growth. Hence, it is not just the rate of inflation that matters, but also the *type* of inflation. The point is that different types of inflation are characterized by different ways in which relative price movements of broad categories of commodities behave (see also Warren, 1977: 2).[1] Consequently, lumping often diverging relative price movements together in a single index of inflation can be misleading and may lead to the problem of what Myrdal called 'misplaced aggregation' (Warren, 1977: p.2; see also G. Myrdal, 1968, Vol. 3, Appendix 3).

This point is often overlooked. Indeed, in neoclassical economics, a sharp distinction is made between the determination of relative prices – the realm of microeconomics – and the determination of the general price level – the realm of macroeconomics. Inflation – a macro outcome – is thus seen as a monetary phenomenon that does not affect the determination of relative prices and outputs produced, consumed or invested. Hence, in neoclassical economics it does not make sense to talk about different types of inflation.

In contrast, as Minsky (1986: p.283) explained, Kalecki saw prices in an accumulating economy as "the carriers of profits and vehicles by which a surplus

1 See also Badhuri (2006) and Rakshit (2009a /b).

is forced". The prices of basic necessities in particular depend on the rate of accumulation in an economy since incomes earned in the production of investment goods or of exports to finance imports of investment goods combine with incomes earned in the production of consumer goods to finance the demand for consumer goods, produced domestically or imported. Stepping up the rate of growth in an economy – Kalecki argued – as a result of a higher rate of investment will raise the effective demand for consumer goods, which, if output of consumer goods cannot respond, will provoke inflation in the price of necessities. Growth-induced relative price changes through the inflation of the price of necessities – food staples, in particular – can thus lead to the erosion of real incomes of the poor.

A corollary of this argument is that the growth in *per capita* GDP cannot always be equated with the growth in the average standard of living.[2] Indeed, the GDP of a country measures the aggregate value added of its domestic production, which comprises the production of consumer goods, investment goods and exports (after netting out imports). To measure economic growth over time, GDP is calculated as constant prices. Consequently, the appropriate deflator here is the *implicit GDP deflator*, which depicts the general rate of inflation of aggregate domestic output (= gross value added). To measure real changes in standards of living, however, it is the prices of consumer goods that matter. In this case, therefore, the appropriate deflator is the consumer price index (CPI). The point of Kalecki's argument is that these two different price indices do not necessarily go hand in hand over time. More specifically, it is possible for consumer prices to rise faster (or slower) than the general rise in prices of domestic output. If this is the case, the growth in the average standard of living will be less (or more) than the growth in GDP per capita.

In the case of Mozambique, for example, during the period 2002 to 2010, GDP grew at 7.4% *per annum* and population growth was ± 2.4% *per annum*, which means that GDP *per capita* grew approximately at 5% *per annum*. The inflation rate for the implicit GDP deflator was 7.5% *per annum* as against 9.8% for the consumer price index, a difference of 2%. The potential growth in the average standard of living, therefore, should be corrected for this differential between inflation rates: hence, the average standard of living grew at most with approximately 3% (= 5% - 2%) *per annum*. Tanzania's experience was somewhat different. From 2002 to mid-2007, the average rate of inflation of the GDP deflator actual exceeded that of the CPI (6.6% against 5.3% *per annum*), but from mid-2007 onwards the GDP deflator lagged behind the CPI inflation rate (8.6% against 9.6% *per annum*). In other words, in Tanzania, the gap between both price indices opened from the mid-2007 onwards and, hence, the growth in the average standard of living lagged behind GDP growth in this latter period.

2 See also Wuyts, 2011: pp.441-444.

Kalecki's main concern, however, was with the danger of the inflation of food prices. He had several reasons for focusing on food prices in particular. First, food consumption takes the largest share of household expenditures. In Tanzania, for example, in 2007, mean food consumption per capita as a share of mean per capita consumption was 59%. This share differed between urban and rural areas: in urban areas this share was 46%; in rural areas, it was 64%. As is to be expected, the share of not-purchased food in total food consumption was much higher in the rural areas than in urban areas, but, contrary to what is commonly assumed, it is not the case that the rural population mainly relies on food produced for own consumption. In fact, the share of not-purchased food in total food consumption in rural areas was about 44%.[3]

Second, mean per capita consumption levels do not tell the whole story. Indeed, consumption patterns differ markedly between households depending on whether they are poorer or richer because, in accordance with Engel's law, the proportion of income spent on food declines as income increases. The implication is that food price inflation hits the poor much harder than the rich (Kalecki, 1963). A corollary of this point is that, when looking at inequality in income and consumption, what matters are changes in the *real* distribution of incomes, and not just in its *monetary* distribution.

The third reason for Kalecki's specific focus on food inflation is his point that macroeconomic adjustment mechanisms differ markedly between agriculture and non-agriculture. His argument goes as follows. The growth in income propelled by investment brings in its wake the growth in the demand for consumer goods – necessities in particular. Whether this leads to inflationary pressures on their prices depends on the ability of the supply of necessities (i.e. domestic production or importation) to respond to growing demand. If supply responds, prices will remain relatively unaffected. Furthermore, if supply responds through the expansion of domestic production, growth will be further stimulated as a result of multiplier effects in the economy. If, however, supply is unable to respond, prices will increase with negative consequences on real incomes.

Now, Kalecki (1954; 1963) argued that in a developing economy both processes are likely to be at work. More specifically, in agriculture, short-run market equilibrium is primarily achieved through price adjustments, which bring demand in line with the available supply (which mainly depends on the previous harvest). In other words, a bumper harvest will lead to falling prices; conversely, when the harvest is low (for example, due to adverse weather conditions), prices will rise to match demand with diminished supply. In contrast, in industry (and

3 Caution needs to be taken with this calculation since the value of not-purchased food is obviously arrived at using an imputed price to estimate the value of its consumption.

services), quantity adjustments tend to dominate the scene with prices determined as a mark-up over variable costs. Capacity utilization, therefore, rises or falls depending on the level of effective demand. Finally, if the rise in the price of food pushes wages up in the non-agricultural sectors, prices of non-agricultural goods will also rise as a result of this cost-push effect.

But Kalecki's argument was not just about the short-run. He was in fact also deeply pessimistic about the capacity of agriculture - and of the production of staple crops in particular – to respond to the growth in demand within a longer-term perspective. His argument was not Malthusian in nature, but rather based on his belief that the institutional arrangements of agriculture production and exchange in developing economies limited their potential growth in productivity and output. These institutional factors were the prevalence of feudal landownership and the domination of peasants by merchants and moneylenders. The problem of financing development – Kalecki argued – consisted of securing adequate growth in agriculture through the removal of these institutional obstacles (1963: p. 51).

Kalecki's argument has important consequences for economic policy. First, as the Indian economist Rakshit (2009a: p. 39) pointed out, it implies that: "the behaviour of the general price level may not constitute a good indicator for policy formulation". More specifically, in the analysis of adjustment mechanisms it is the output gaps between demand and supply in the two sectors (agriculture and non-agriculture) *separately*, and not the total output gap, that matters for framing policies (*ibid*). The reason is that, as explained earlier, economic adjustment mechanisms operate differently across both sectors: in agriculture, prices clear the market, while in industry (and services) quantities (i.e. changes in capacity utilization) do.

Second, the differential nature of these adjustment mechanisms in agriculture and non-agriculture entails "the possibility of the simultaneous operation of demand and supply constraints, the first in the non-agricultural sector and the second in the primary sector" (*ibid*: p. 38). Moreover, these constraints may interact. For example, price inflation in agriculture – food, in particular – can lead to decreased capacity utilization coupled with cost-push inflation in non-agriculture because the demand for food is relatively price and income inelastic (*ibid*).

Consequently, there is no reason to belief that prices of food and of non-food consumer goods move hand in hand and, hence, it is useful to look at their separate behaviour over time. In Mozambique, for example, over the period 2002 to 2010, the average rate of inflation of food prices was 11.3% *per annum* as against 7.6% for non-food consumer goods, a discrepancy of 3.7%. The rate of inflation in the GDP deflator was similar to that of the non-food consumer goods.

Moreover, during this period, in Mozambique, domestic production of food has been highly variable with low levels of overall growth in output, thus rendering the country more dependent on imports. From 2002 to 2008, food production expanded by 2.2% *per annum* (which is less than population growth) and productivity (measured by yield) fell by -2.7% *per annum*.[4] In recent years, world prices of foodstuff have been rising rapidly, which brought increased import prices of food in its wake.

Yet, at the same time, Mozambique has witnessed impressive rates of growth. But what matters for poverty reduction, however, is not just the rate of growth, but also the type of economy it constructs in the process, which – in the case of Mozambique – appears to be quite unbalanced in favour of export production propelled by mega projects. The lesson appears to be that, while export production is undoubtedly important, what matters is the expansion of production of necessities for the internal market, especially food. Last year, notwithstanding a history of high growth rates, Mozambique witnessed serious urban riots as a result of food (and fuel) price increases.

Tanzania witnessed a similar trajectory, particularly from the mid-2007 onwards, with a rate of inflation of food items of 12.1% as compared with 5.5% for non-food items and 8.6% for the GDP deflator.

Kalecki's point, therefore, is still highly relevant today: growth-induced inflation in the relative price of food cannot be ignored as an important dimension of the link between economic growth and poverty reduction.

However, a caveat is necessary here. Indeed, it can be argued that the adverse consequences of a rise in the relative price of food mainly concern urban areas, but that rural producers will benefit from the rising prices of foodstuff. Consequently, since the incidence of poverty is higher in the rural areas than in urban areas, the rise in the food of foodstuff will reduce overall inequalities as well as lower the incidence of poverty overall, given that the majority of the population lives in rural areas.

This is an important point. Rising food prices will benefit rural producers. The question is, however, whether it does so evenly across the rural population? In fact, as I pointed out earlier, in Tanzania, more than half of the food consumed in rural areas is purchased within markets and, hence, not just produced for own consumption. A study on Malawi by Yamada Sachi (2008: pp. 21-22), for example, showed that approximately 90 per cent of rural households in Malawi are maize producers, but most of these rural households were not self-sufficient in their staple food: for 2004/5, the median of self-sufficiency was 7 months, sug-

4 Source: Poverty and Well-being in Mozambique: Third National Poverty Assessment, October 2010.

gesting that 5 months before the next harvest, half of the surveyed households were without their own maize stock. Note, however, that low maize production does not necessarily make rural households food insecure since income from off-farm sources and cash crops plays significant role to determine food security of a rural household. Moreover, not only are a large proportion of the peasantry deficit producers of food, but they often sell food at lower prices immediately after harvest time to pay of debts or to finance necessary expenditures and subsequently end up buying food at higher prices later in the season. In other words, as Kalecki pointed out, the benefits of price rises do not always go to direct producers, but may end up as profits of traders and money lenders. Finally, what matters also is the extent to which the rural labour force depends on wage labour and, hence, on wages to secure its standards of living, including to pay for food. If the rise in the price of food leads to a rise in rural real wages, rural wage labourers will benefit; if, however, it only boasts monetary incomes of surplus producers and of traders, they will not. In conclusion, therefore, whether or not a rise in the price of food will benefit the majority of people in rural communities depends on existing inequalities of rural incomes and assets and on the prevailing nature of employment relations in the rural economy. Unfortunately, little or no research is done on this question in Tanzania or in Mozambique.

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Let me pause here for a moment. What I have done up to now is to restate Kalecki's point that economic growth should not go at the expense of inflation of prices of necessities – food in particular – since it will harm the poor disproportionally. Kalecki's argument had to do with how economic growth could impact adversely on the standards of living of working people, particularly the poor. What I intend to do next is to take this argument a step further. I argue, furthermore, that growth-induced inflation in the relative price of necessities – and of food in particular – in a developing economy does not only affect the standards of living of the poor, but it also affects their condition of employment and its rate of expansion. In other words, the rise in the relative price of necessities does not only affect how the poor live, but also how they work.

From the 1980s onwards, which saw the implementation of structural adjustment policies in Africa, employment more or less ceased to be an explicit policy objective. At first, retrenchment of labour took precedence in the drive to cut public expenditures and to reduce the size of public enterprises. Later on, when social issues re-emerged on the agenda, it was poverty, not employment, that became the focus of policy. Employment, if it cropped up at all, was largely relegated to a matter of social policy, not economic policy. Most recently, however, employment has again come back on the policy agenda in Africa.

Given my own Keynesian roots, I welcome this recent change in direction. Indeed, I would argue that, perhaps paradoxically, a shift in policy emphasis away from poverty towards employment might go a long way to effectively reduce poverty in Africa. But this does not mean that employment growth alone does the trick. What matters is that employment growth goes hand in hand not only with productivity growth but also with the growth in labour earnings. Otherwise, the growth in employment will merely lead to the growth in the numbers of the working poor. This is the issue to which I shall turn now.

To start with, a brief digression on the concept of employment is necessary. The reason is that in Africa many argue that wage employment has become the exception and self-employment the rule, particularly as a result of the growth in the informal sector. The growth in employment, therefore, is said to consist mainly of the growth in self-employment. Not surprisingly, policy attention has turned to how to stimulate this growth in self-employment through formal titling of property to allow for access to credit, through micro-credit schemes and through providing training in entrepreneurship, particularly for the young. The self-employed are thus depicted as an amorphous mass of undifferentiated small-scale entrepreneurs pulling themselves up by their own bootstraps. A major proponent of this is Hernando de Soto who remarked that: “Marx would probably be shocked to find out how in developing countries much of the teeming mass does not consist of oppressed legal proletarians but of oppressed extra-legal small *entrepreneurs*” (as quoted in Rizzo, 2011: 1180). The crux of the matter, then, is that there is a lot of talk about agency and empowerment exercised in the face of an oppressive state but seldom about class. Consequently, as Rizzo argued recently, “the significance of class in understanding how informality works is explicitly downplayed” (2011: p. 1180).

I argue that class matters and, more specifically, that this way of depicting ‘self-employment’ detracts attention away from the pervasiveness of labour markets in Africa within the informal sector, both in urban and rural production, including in agriculture. Specifically, my argument is that much of what is defined as self-employment is in fact wage labour. Indeed, under conditions of low productivity in the context of the uncertain environment of informality the character of wage labour, and the variety of forms in which it occurs, does not correspond to the conventional or ‘formal’ definition of wage labour.

This point can perhaps best be illustrated analytically with the aid of de Quincey’s famous remark about Ricardo’s view of profits as ‘the leavings of wages’. If the wage rate is predetermined (= agreed in advance), it follows that the profit per worker will be equal to the difference between the value-added produced per worker and the wage rate. If the price of the output is less than expected or, alternatively, if (real) labour productivity is less than expected, profits will also be below expectations since the wage rate is fixed beforehand. The employer, therefore, bears the risk that average labour productivity (expressed in value terms) turns out to be lower than expected, given the level of the wage rate. The wage labourer, in contrast, bears the risk of unemployment if the enterprise fails to live up to this expectation. This is the conventional view of wage labour in which the wage rate is fixed *a priori* and, hence, profits are the residual or, as de Quincey put it, the leavings of wages.

But, clearly, this kind of wage system is not particularly attractive to the capitalist entrepreneur when labour productivity is low, volatile or unpredictable, which are precisely the conditions that prevail widely within the informal economies in developing countries. Formal wage contracting, therefore, is unlikely to be widespread under such conditions. But it does not follow from this that all activities are therefore based on self-employment and, hence, that the capital / labour relation ceases to exist or does so only marginally. On the contrary, under these conditions, wage labour exists in different forms. To understand how informality works, therefore, it helps to turn de Quincey's phrase on its head: what prevails is not that 'profits are the leaving of wages', but on the contrary that 'wages are the leavings of profits'. The implication is that capital confronts labour not as the risk-taking entrepreneur but as a rentier, leaving labour to manage the risks inherent in low and volatile productivity, a condition that is not conducive to the growth in productivity.

A recent publication by Rizzo (2011), for example, showed that the minibus driver and conductor in Dar Es Salaam do not generally own the vehicle they drive, nor are they paid a fixed wage. Instead, each day they pay a 'rent' to the owner, which is fixed beforehand, independently from the number of passengers actually transported. Their labour earnings, therefore, are the leavings of profits, earned at the margin. These workers are perceived (and perceive themselves) as self-employed – members of Hernando de Soto's teeming mass of small entrepreneurs – yet they do not own the means of production they employ, they can get sacked at any time, and most of the income they earn is paid out to the owner of the bus, leaving them with the residual. They are entrepreneurs only in the sense that they have become managers of two sets of risks under adverse conditions of extreme competition: the daily insecurity that results from an uncertain income, on the one hand, and the ever-present chance of job loss, on the other.

Note that I am not arguing that petty commodity production does not exist within the informal sector. My argument, however, is that labour markets play a far more important role within informal production than is made out to be and, hence, consequently, that it is important to distinguish between productivity per worker (=value added per worker) and labour earnings per worker (= the wage). The two are not equal to each other nor do they necessarily move similarly over time. Unfortunately, research on actual labour arrangements is rarely done in countries like Tanzania or Mozambique today. Hardly any official data exist that can give insights in the varied nature of the employment relation in informal production, the prevailing conditions of pay in relation to productivity, and the nature of the dynamics of unemployment – open or hidden. Much could be done in terms of research if only a fraction of the amounts of money that are routinely spent on commissioning streams of reports on poverty monitoring were diverted to get insight to these issues. But this is unlikely to happen given that the myth of generalized self-employment is so firmly entrenched in policy thinking today.

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Let me now continue with the premise that employment growth should not go hand in hand with the growth in numbers of the working poor. In this respect, it is useful to start with a point made by Alice Amsden (1997: p. 125) about the trade-off between lowering real wages and raising productivity. Amsden was discussing the challenges that newly industrialising countries like Korea and Taiwan faced in developing a textile industry when confronted with the competition of the then well-established Japanese textile industry (where, notwithstanding higher wages, unit labour cost was lower because labour productivity was considerably higher). She drew a distinction between two feasible alternative strategies: lowering real wages (a policy pursued under structural adjustment) or raising productivity by investment in fixed capital and what she called 'subsidized learning', which she identified as the East Asia model.

For convenience, Amsden assumed that labour is the only input since her argument focused on labour intensive production. Analytically, then, her argument is based on the premise – which she takes to be a definition – that unit labour cost equals the ratio of the real wage to labour productivity (also expressed in real terms):

Unit labour cost = real wage / labour productivity

This definition, however, is incorrect (Wuyts, 2001: pp. 419-424). Indeed, unit labour cost equals the share of nominal wage in nominal output produced by the worker, which does not equal the ratio of the real wage to labour productivity because these two latter measures do not have the same deflator. The *real* wage is a measure of standard of living and is obtained by deflating the nominal wage by the index of prices of wage goods (= consumer price index of basic necessities). In contrast, real productivity is the nominal output per worker deflated by the price of the output. A relative price term is, therefore, omitted from this definition.

What Amsden overlooks is the distinction between the two sides of wages: wages as a source of income and wages as a cost of production. To the worker what matters most is the standard of living that his or her wage can afford. A rise in the real wage implies an increase in the standard of living a worker can afford; a fall in the real wage decreases the standard of living. Given the nominal wage, therefore, the real wage depends on the prices of necessities. To the employer, in contrast, wages are a cost of production paid out of the value added produced. The relevant measure here is the product wage which is obtained by deflating the nominal wage by the price of output. It represents the quantity of output that a worker could buy with his or her own wage. Given the level of labour productivity, an increase in the product wage squeezes profits; conversely, a fall in the product wage leads to an increase in profits.

Consequently, the correct definition of unit labour cost is that it equals the ratio of the product wage (and not the real wage) to labour productivity:

Unit labour cost = product wage / labour productivity

Or, alternatively,

Unit labour cost = (real wage / labour productivity) x (consumer price index / output price)

Amsden did not take account of this relative price term when using the real wage instead.[5] But this term cannot be ignored because the real wage and the product wage do not necessarily move in unison. Indeed, if the prices of necessities, food in particular, rise faster than the output price, it follows that, for the same nominal wage, the evolution of real wages will diverge from that of the product wage as a result of the inflation differential between both sets of prices (Wuyts, 2001).

Amsden ignores this possibility completely and thus overlooks that inflation in the price of necessities relative to other prices can erode the viability of the growth of labour intensive production. This point is nothing new. In fact, it goes back to Marx who never failed to distinguish clearly between the value of labour power as a commodity, on the one hand, and the value produced by labour power in the process of production, on the other. The point made here is just a variation on this theme.

Consider, for example, what happens if the price of foodstuff rises much faster than other prices in the economy, as was the case in Tanzania and Mozambique in recent years. If nominal wages adjust upwards to keep the real wage constant, the product wage will rise and, hence, unit wage cost will rise as well. If this leads to a squeeze on profits, particularly in labour intensive production, employment may fall or its growth will be stunted. Alternatively, if the nominal wage does not adjust to the rising cost of wage goods, the product wage and unit wage costs remain the same, but the real wage will fall. Adjustment takes

5 More recently, J.A. Ocampo, C. Rada and L. Taylor (2009: pp. 130-136) employ the same definition of unit labour cost as Amsden did and, hence, make the same error.

place at the expense of falling real wages, which may thus lead to an increase in the incidence of poverty. What often actually happens is a combination of both these processes at work, with real wages (partly) protected in the formal sector (restraining its potential for employment expansion) while falling in the informal sector, which then becomes a dumping ground for the working poor.

Mozambique provides an interesting example in view of the recent austerity measures imposed by the government in a context where food and fuel prices were rising steeply. In response to a national debate about wage negotiations and social protection, the government of Mozambique announced that it would introduce a scheme of providing a basic basket of food products at lower prices to protect the purchasing power of families earning below 75 USD (2.500 Meticais) per month. The national director for studies and policy analysis of the ministry of planning and development explained that the option of the basic basket of consumer goods was better than wage increases because such increases fuel inflation. In essence, the national director was seeking to partially insulate formal sector low-income workers against the erosion of real wages. This provoked strong criticism on grounds that the incidence of poverty was much higher among informal sector workers. Subsequent promises to include all workers in scheme quickly led to its demise. At first, the introduction of the scheme was delayed and, subsequently, it was formally abandoned, all within less than 4 months.

Note that, in this case, cash transfers do not provide a solution to the problem of a rapidly rising cost of living. In recent years, it has become of fashion, particularly within the donor community, to see cash transfers as a solution to poverty. Hanlon, Barrientos and Hulme, for example, argue that the shift towards cash transfers would yield a more effective way to deal with the plight of the poor, particularly since they can be 'hugely empowering and productive' (2010, p. 175). I do not deny the importance of cash transfers as a means to combat poverty, but to do so they should have a major effect in terms of boasting the effective demand for consumer necessities. However, if the key constraint emanates from the inability of production of necessities – food, in particular – to respond to the expansion in the demand for necessities, the need for cash transfers is a reflection of a deeper problem and using them to combat poverty may amplify this problem rather than resolve it. As Gosh (2011: p. 855) recently argued, "the approach ignores the possibility that the cash transfer itself may be undermined by the wider processes that are not dealt with". 6

6 More specifically, the problem is that policy discourses on cash transfers tend to focus on the micro- or meso-level with occasional reference to fiscal issues (which often concern the use of donor moneys). As Jayati Ghosh argued:

> "This means that macroeconomic processes are entirely ignored, such a patterns of trade and economic activity that determine levels of employment and its distribution and even the viability of particular activities, or fiscal policies that determine the

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In conclusion, in this valedictory address my aim has been to bring some old ideas back into modern debates. Perhaps this just reflects my own age – a kind of nostalgia for old-style political economy. But I think that some of these ideas – suitably adapted to modern contexts – continue to be relevant, particularly in the light of the damage rising food (and fuel) prices are doing in Africa today.

In my view, the present practice of monitoring how growth relates to the reduction in poverty incidence tells us little about how macro mechanisms actually influence how working people, including the poor, live and work today. My argument has been that it pays to put the macro interrelations between productivity, labour earnings and employment back at the centre of the stage in order to get to grips with the dynamics of poverty and inequality in developing economies.

extend to which essential services like sanitation, health and education will be provided, or investment policies that determine the kind of physical infrastructure available and therefore the backwardness of a particular region, or financial policies that create boom and bust volatility in various markets. It also means that no link is even hinted at between the enrichment of some and the impoverishment of others, as if the rich and the poor somehow inhabit different social worlds with no interdependence at all, and that the rich do not rely upon the labour of the poor." (2011: 854)

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