In 1975, in the midst of a national debate over what should be the primary target of economic policy, Arthur Okun wrote an essay entitled, *Equality and Efficiency*. In it he wrote

The contrast among American families in living standards and in material wealth reflect a system of rewards and penalties that is intended to encourage efforts and channel it into socially productive activity. To the extent that the system succeeds, it generates an efficient economy. But that pursuit of efficiency necessarily creates inequalities. And hence society faces a tradeoff between efficiency and equality.

He goes on to write

The presence of a tradeoff between efficiency and equality does not mean that everything that is good for one is necessarily bad for the other … Nonetheless, there are places where the two goals conflict, and those pose problems.

Okun concludes

If both equality and efficiency are valued, and neither takes absolute priority over the other, then, in places where they conflict, compromise ought to be struck. In such cases, some equality will be sacrificed for the sake of efficiency, and some efficiency for the sake of equality. But any sacrifice of either has to be justified as a necessary means of obtaining more of the other.

In his opening remarks at the IMF’s conference on “Economic Policy and Equity” on June 8, 1998, Stan Fischer, then the First Deputy Managing Director, provided a two part answer to the question, “Why do equity considerations matter to the IMF?” He said

First, as a matter of social justice, all members of society should share in the benefits of economic growth.

Second, there is also an instrumental argument for equity: adjustment programs that are equitable and growth that is equitable are more likely to be sustainable.
Although it was the first oil shock and subsequent recession that primarily motivated his book, Arthur Okun’s comments about the tradeoff between equality and efficiency followed 15 years during which the US economy grew by an average of 4.4 percent (in real terms) each year. And although exports and imports constituted a very small part of the overall economy, the United States was running a current account surplus equal to a little more than 1 percent of GDP.

Likewise, Stan Fischer’s comments came in the midst of one of the longest US economic recoveries in peacetime history. The US economy had already posted 29 consecutive quarters during which real economic growth averaged 3.5 percent. The economy would go on to post an additional 10 quarters during which real economic growth would average 4.4 percent. World GDP had more than doubled in nominal terms, growing on average by almost 3.5 percent annually, in real terms, over the preceding 15 years.

Just a year and a half after Stan Fischer made those comments a WTO ministerial meeting in Seattle was disrupted by riots and it is probably fair to say that subsequent meetings of the World Bank and IMF have not been the same since.

We gather during a period that has been characterized as “no ordinary time.”

- We are approaching the 70th anniversary of the Bretton Woods Conference. Despite the greatest expansion in wealth and technology and significant reductions in poverty probably in human history, there is growing anxiety about economic well-being in many places around the world making it increasingly difficult, if not impossible to pursue further multilateral liberalization in trade and investment.
  
  o Although there is great debate over measurement, it is pretty clear that the distribution of income, at least in most advanced economies, has deteriorated in recent years.
  
  o A comparison of developments in real wages and labor productivity included in the ILO’s recent Global Wage Report provide evidence that equity gains have not necessarily followed efficiency gains in many economies.

- The world economy has not yet fully recovered from a global financial crisis and the worst economic slowdown since the Great Depression.
  
  o Economic growth in the advanced economies averaged less than 1 ½ percent over the last 2 years and the IMF expects it to be a little more 2 percent annually over the next 5 years.
Although it looks like the US economic recovery is finally underway, it is still going to take years for some people to restore their living standards back to what they were before the crisis. Even if it continues to increase by 150,000 per month, the level of US employment will not reach its pre-crisis level until March 2015 and another 6 months later if the increase falls to 125,000, the 30 year average.

The labor force has continued to grow throughout this period, by something like 60,000 to 80,000 people per month, causing the employment-to-population ratio to fall 6 percentage points below the peak it reached in March 2000.

- It has been 20 years since the last successful multilateral trade negotiations and trade policy has been “Balkanization” by the proliferation of bilateral and regional agreements, which may have actually put an end to truly multilateral agreements.

- The shift in the balance of economic power, documented by my colleague Arvind Subramanian, reflects the challenges the United States and Europe face in setting the international economic policymaking agenda, signifying a true end of the Bretton Woods era.

Most of the speakers at the IMF conference in 1998 ignored the important role of economic, political and social institutions in sharing the benefits from economic liberalization and growth with workers and their families and society in general. In fact, some of the speakers at the conference actually railed against them.

These economic, political and social institutions play a crucial role in determining the effect and effectiveness of economic policies.

These institutions include the form of government and the degree to which people have a voice in that government – at the local and national levels, a nation’s education system, the independence of its central bank and the implementation of monetary policy, the progressivity of its tax system and yes, the existence and enforcement of minimum wage laws and other basic labor standards, as well as other labor market policies like an unemployment insurance system.

I believe these institutions are the glue that keep societies together and form the “social contract” that is believed to be at the foundation of democratic societies.

And herein lies the problem:
The people who met at Bretton Woods almost 70 years ago came together in order to address the “collective action” problem of removing high barriers to the flows of goods, services and capital. Their efforts slowly morphed into what we now call the "international economic “system," but this system does not have any of the economic, political and social institutions at the international level to bind the system together.

In fact, some multilateral groups, like the IMF and the WTO, sometimes argue against the need for these institutions and have played little or no constructive role in incorporating them into the system.

And so we got “the Washington consensus” calling for fiscal discipline, the liberalization of trade and finance and the “reorientation” of public expenditures and tax policies all aimed at promoting further economic efficiency, *at any expense*, with virtually no calls for economic, political and social institutions to address equity.

In other words, “international trickle down.”

Instead of taking the lead in addressing equity concerns, following Stan Fischer’s own warning that addressing equity concerns contributes to the sustainability of pursuing efficiency gains, the multilateral organizations, including the IMF and the WTO, have taken a hands-off strategy, hiding behind what they call “subsidiarity” and national sovereignty.

One example is the lack of unemployment insurance programs around the world.

### Unemployment Insurance Programs
**Classified by Country Income Levels**

<table>
<thead>
<tr>
<th>Country Level of Income</th>
<th>Low</th>
<th>Low-Medium</th>
<th>Medium-High</th>
<th>High</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Countries with mandatory UI systems (percent by income group)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>42%</td>
</tr>
<tr>
<td></td>
<td>8%</td>
<td>35%</td>
<td>54%</td>
<td>80%</td>
<td></td>
</tr>
<tr>
<td>Average coverage (percent of labor force by income group)</td>
<td>2.9%</td>
<td>18.1%</td>
<td>38.4%</td>
<td>69.2%</td>
<td>30.6%</td>
</tr>
<tr>
<td>Average recipiency rate (percent of unemployed by income group)</td>
<td>1.3%</td>
<td>3.6%</td>
<td>10.4%</td>
<td>38.8%</td>
<td>12.9%</td>
</tr>
</tbody>
</table>
In fact, 5 of the 19 countries in the G-20 do not have unemployment insurance programs, i.e. India, Indonesia, Mexico, Saudi Arabia and Turkey.

In the United States, presidents have had to ask Congress to establish “emergency UI” programs during each of the last 8 recessions, dating back to the 1950s. So much for the “automatic” stabilizer.

And just last week President Obama insisted that Congress renew the emergency program established in 2008 for the 9th time. How many times do we need to extend “emergency” measures in order to appreciate that there are structural problems with our unemployment insurance system?

Conclusion:

The United States, Europe and China should take the lead in getting all countries – big and small, advanced and emerging, to commit to a timetable for adopting and reforming positive adjustment measures aimed at insuring that efficiency gains derived from economic liberalization are better shared within all societies.

These measures could include, but are not limited to

- Minimum wage and other policies to ensure that wages increases are more closely linked to productivity gains
- Unemployment insurance system
- Active labor market programs to enhance labor market flexibility
- Adoption of core ILO labor standards
- The ILO, OECD and World Bank can provide technical assistance.
- The IMF should provide some of the initial financing, if necessary.
- All international and regional financial institutions should make this commitment a standard part of all their negotiations. Furthermore, developing a timetable for design and implementation of these programs should be a prerequisite for any future lending.
- Ironically, the WTO might provide the institutional infrastructure for negotiations of an International Agreement on Positive Adjustment Measures (IAPAM)

Membership in the international economic system may have its privileges, but it also comes with responsibilities.