Social and Labor Market Policies for Tumultuous Times

Confronting the Global Crisis in Latin America and the Caribbean

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Inter-American Development Bank

Foreword

This report was prepared for the Annual Meeting of the Board of Governors of the Inter-American Development Bank held in Medellín, Colombia, in March, 2009. A complementary report, *Policy Trade-offs for Unprecedented Times: Confronting the Global Crisis in Latin America and the Caribbean,* was also prepared for the same event. Together, these two reports seek to contribute to an understanding of the social and macroeconomic implications of the current global crisis for the Latin American and Caribbean region (henceforth "the region"), and the options and risks faced by policymakers in these two critical and inter-related areas.

This report is devoted to the social impact of the crisis, and focuses on its effects on employment, nutrition, health, education, and poverty. It identifies the mechanisms by which the crisis can affect these critical social dimensions, and discusses possible policy responses given each country's circumstances, fiscal space and administrative capabilities. The report argues that an important but at times overlooked determinant of appropriate responses is the expected length of the crisis, as some measures that may be useful in the context of a short-lived recession may not be so in the context of a longer lasting downturn. In parallel, the report argues that it is essential to consider the impact of any measures on the incentives of households, workers and firms, as some measures may have negative impacts on fundamental determinants of productivity and medium-term growth. The social challenge generated by the crisis is therefore not only to protect the vulnerable population, but to do so in a fiscally sustainable manner and with programs that contribute to, rather than retard, the resumption of growth. No individual country suggestions are made. Instead, the report indicates some general policy principles that can hopefully be of use to policymakers, including the international financial institutions engaged in the region, on the difficult road ahead.

The report was coordinated by Suzanne Duryea, Jacqueline Mazza and Ferdinando Regalia, and synthesizes more detailed studies listed in the references by Veronica Alaimo, Cesar Bouillon, Julian Cristia, Jesus Duarte, Roberto Flores, Ariadna Garcia-Prado, Amanda Glassman, Julia Johannsen, Florencia Lopez-Boo, Frank Niedert, Isabel Nieves, Hugo Ñopo, Consuelo Ricart, Marcos Robles, David Rosas, Eleanor Sohnen, Waldo Tapia and Luis Tejerina. The situations described are not forecasts of social or labor market outcomes by the Inter-American Development Bank; they are illustrations of possible scenarios that exemplify the issues under discussion. The views expressed here do not necessarily coincide with those of the management of the Inter-American Development Bank, its Board of Directors, or its Board of Governors.

Santiago Levy
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1 Introduction

The region of Latin America and the Caribbean (LAC) is no stranger to aggregate economic shocks triggered by financial crises. Although the region has confronted a high frequency of economic crises, recoveries have tended to be rapid. The rebounds from the 1994 crisis, in Mexico, the 1997 Asian crisis, the 1998–99 currency crisis in Brazil, and the 2001 Argentine crisis to name a few, all occurred with a span of a year or two. Notwithstanding the region's experience with dramatic economic downturns, the characteristics of the current global economic crisis may represent for LAC a test which is unparalleled in recent decades. According to IMF estimates the year 2009 will be the first year since the Second World War in which the world economy will contract rather than grow. In 2009 alone, the estimated number of unemployed is projected to reach 17 million, exceeding the estimate of unemployment in the US of 13.4 million.[1] The crisis is already hitting LAC hard through various channels. Credit to governments, firms and households shrank rapidly in the second half of 2008. With the US at the epicenter of the crisis and the contagion spread to Europe and Japan, the collapse of aggregate demand in LAC's major trading partners signals a grave situation. Reflecting this, prices for exports like oil, metals and basic grains have dropped. A dramatic fall in net private financial flows and direct foreign investment is foreseen for 2009 with remittances also declining.

As argued in the parallel report *Policy Trade-offs for Unprecedented Times*, overall LAC pre-crisis conditions were more favorable than before the crisis of the 1980s and 1990s, including better fiscal positions, higher reserves and more flexible exchange rates. Nonetheless, the characteristics of the current crisis (large scale, with epicenter abroad, systemic) make predicting its depth and duration extremely difficult. Indeed, in the last nine months, growth forecasts have repeatedly underestimated the impact

[1] The estimate of 17 million for Latin America comes from (ILO 2009) and the estimate for the US is derived from Federal Reserve Bank estimates.

of the crisis on growth rates. In light of the most recent adjustments in growth projections, the likelihood of a V-shaped recovery for LAC over the course of 1-2 years may not be different than that of a more protracted L-shaped recovery over a 3 to 5 year period. As discussed in *Policy Trade-offs for Unprecedented Times*, under the L-shaped scenario average growth in the region might be close to zero in the next five years (and negative in per-capita terms), indicating that the collateral damage of the global crises could be felt for years to come. The uncertainty regarding LAC recovery scenarios is further complicated by: (i) the potential impact that regulatory changes in the financial systems in OECD countries might have on the long-run cost of credit and risk assessment for LAC economies; (ii) the possible crowding out of LAC countries from international capital markets given large and persistent deficits in the US, Europe and elsewhere; and (iii) the political dynamics in countries around the world that could lead to beggar-thy-neighbor policies, protectionist pressures, competitive devaluations, and so on. What *is* certain is that the world economy will be substantially changed in five years as the vast majority of countries have already or will have aggressively altered their policies in response to the crisis.

Given the uncertainty surrounding the depth and duration of the crisis, LAC faces critical policy challenges. In particular, governments need to assess the inter-temporal trade-off embedded in the measures designed to respond to the crisis. Ensuring that these measures do not hamper but rather enhance the prospect of recovery in output growth may not be a luxury that is out of reach but rather an essential element that cannot be ignored. Within this inter-temporal approach, this report analyzes the role that social and labor market policies can play as part of the response to the current crisis. Of course, social and labor market policies are not implemented in a vacuum. Their viability and effectiveness hinge upon countries being able to respond to this crisis with sound macroeconomic policies that prevent countries from entering financially fragile territory, as discussed in the already mentioned companion report. In turn, strengthening social and labor market policies to protect the most vulnerable within a context of fiscal scarcity could contribute to the sustainability of prudent macroeconomic policies.

If a protracted period of low or negative growth materializes, the countries best poised for a recovery will be those that have responded to the crisis with social and labor market measures that offer a high degree of social protection (e.g., policies that effectively prevent irreversible impacts among the most vulnerable), are fiscally sustainable, and are aligned with, or at least do not undermine, the necessary changes required to adapt to the new environment which will emerge from the crisis. The latter will most likely be characterized by higher competition among emerging economies for scarcer capital and foreign direct investment. This new environment will reward those countries which have adopted social and labor policy measures in response to the current crisis which, while expanding coverage of a bundle of essential social entitlements, are also aligned with the medium to long-term objectives of removing bottlenecks for growth in aggregate labor productivity and output.

The assessment of policy options may be fundamentally changed by incorporating the inter-temporal dimension. First, the ranking of the policy instruments to be deployed may be altered with different forecasts of the length of the crisis. Second, some instruments which may be appropriate for a short-run crisis may be inadequate under the scenario of a longer crisis where deeper measures are necessary. Finally, short-run instruments may be detrimental to or delay more systemic changes which are required under a longer crisis scenario, especially if their "short-term" nature is not credible and they end up perpetuating inefficiencies year after year. For example, new programs are often created in the midst of crisis instead of addressing structural deficiencies in existing policies and programs, and at times are not removed once the crisis is over, creating further distortions—particularly in the labor market—that hinder medium-term growth.

2 Framework

A large body of empirical evidence from previous crises is available to shed light on the potential impacts of an aggregate economic crisis on households, and on the effects of public policies and programs, particularly in health and nutrition, education and labor markets. This report draws from the available literature but also addresses the possibility of a more protracted crisis, specifically exploring the dynamic consistency of the various policy instruments. In three critical areas—health and nutrition, education, and labor markets—we examine (i) instruments that can be recommended regardless of the duration of the crisis, (ii) instruments that should be deployed only if the crisis is relatively short (e.g., less than two years), and (iii) measures that could be taken if the crisis is of longer duration. As we explore the different instruments, the ordering of the measures is not intended to reflect an implicit ranking or recommendation.

For ease of exposition we characterize policy instruments as **short-term measures** or **systemic measures**. The former include programs or policies that can be deployed within the existing framework of social and labor policies. For example, a temporary employment program can be added to the mix of available programs. The latter refer to reforms that are structural, changing the essential nature of social or labor policies such as, for example, replacing the existing system of severance pay with unemployment insurance, substantially reforming a labor intermediation system or modifying the scope and financing of social security. To illustrate the potential inter-temporal tradeoff between short-term vs. systemic measures consider, for example, a medium-income country with a high degree of labor market informality facing a collapse in demand for exports, tourism, and remittances. Under a V-shaped recovery scenario it may be appropriate to temporarily waive employer contributions to social security or temporarily suspend required contributions to pension funds as a means of providing incentives to retain formal workers. Under an L-shaped recovery, however, the long-run viability of these systems would be threatened by the large and persistent reduction in contributions. If the longer term scenario plays out it would make more sense to address structural problems that might affect labor costs and have to do, for example, with the scope of social security and the way it is financed. Moreover, if systemic measures are required, they should be planned and implemented as early as possible, while short run instruments are "credibly" phased out.

Before moving to the analysis of the different social sectors it is important to clarify that while the speed of deployment is a relevant characteristic in the assessment of which social and labor market policy measures a country might want to adopt in response to the crisis, this characteristic is orthogonal to the categorization of a policy as short-term or systemic.

Our framework has three key criteria in terms of policy objectives, (i) to protect the most vulnerable (the chronically poor but also those who are most likely to plunge into poverty), (ii) to prevent irreversible impacts, and (iii) to respond in an inter-temporally consistent manner. The concept of dynamic consistency has already been addressed in terms of the robustness of the policy instrument to the duration of the crisis. It also applies to exit strategies for short-term programs. For example, for reasons of political economy, many of what are initially thought of as "transitory measures" become permanent policies of social assistance. Therefore, the credibility that a short-term measure will be "transitory" hinges on the fact that more systemic interventions can be designed and implemented, that allow the first to be phased out.

Vulnerable Groups: Chronically versus Transitorily Poor

In a crisis the chronic poor are particularly susceptible to adverse impacts given their compromised status before the crisis. Even if the chronically poor experience a smaller shock than other population groups, they may be more vulnerable to irreversible impacts of the crisis because they are closer to critical thresholds such as removing children from school and dropping below an adequate level of nutrition. The deepening of poverty for households already below the threshold is a grave issue since these families are the least likely to have resources to ameliorate the shock. Not only do they have low levels of assets and access to financial markets, but their income sources are also less diversified, their low level of education and skills limit their mobility across sectors and regions, they depend more on public transfers and social services and, therefore, are more exposed to cuts in government spending. Faced with a covariate shock, neighbors and family members cannot finance consumption gaps through personal loans because the others are likely to be affected as well. Poor families may be forced to adjust to the decline in household income by decreasing investments in children's education, health and nutrition. While some losses can be reversed in the long run—starting another business or replacing a sold asset—human capital accumulation is asymmetric in the sense that investments forgone cannot be easily or efficiently recouped at older ages.

The changing of poverty status must also be considered as families cross the threshold over time. The greater churning associated with job destruction during a crisis can generate substantial additional poverty as families previously above the poverty line plunge into poverty. Households are highly vulnerable to falling into poverty even when their average consumption is some distance above the poverty line.[2] Previous crises in LAC and other regions suggest that consumption may fall as much as 10–20% as a result of the crisis. During the Asian financial crisis in the 1990s, poverty rates in Indonesia increased from 15% to 33%; real per capita consumption expenditures fell by 17%, and per capita consumption fell about half as much as real wages. In South Korea poverty rose by 10 percentage points but only by 2 percentage points in Thailand. In Mexico consumption fell by 11% during the 1995 crisis and in Argentina by 6%.[3] Poverty increased by 6 percentage points from 1994–1995 in Mexico and 4 percentage points in Argentina. Although poverty levels fell quite steadily in LAC in the last decade, the current financial crisis could reverse some of these gains.

Transmission Channels

The distinguishing characteristics of LAC in comparison with the rest of the world will affect the transmission of the shock as well as the mix of appropriate responses. These characteristics are (i) high income and asset inequality; (ii) lower productivity growth; (iii) low savings rates; (iv) high levels of labor informality; and (v) poor educational quality. The dramatic lack of formal credit available on world markets has extended to the public and private sectors in LAC including small and medium enterprises (SMEs) and households. The global nature of the recessions entails a sharp decline in demand for the region's exports as well as a decline in foreign direct investment.

Based on previous crises, employment is expected to decline more in small and medium firms than in larger enterprises as SMEs are crowded out of the credit market. This implies the potential for escalating effects as small and medium enterprises generate over two-thirds of employment and represent on average about 30–40% of GDP. As firms shed jobs and close their doors in response to deteriorating business conditions the impact can be observed in the labor market in the form of higher unemployment rates, lower labor force participation and a higher level of informality. With labor income comprising 80% of family income for the average family in LAC, job losses hit hard. An increased fear of job separation among employed workers can translate into a reduction in consumer spending which in turn lowers aggregate demand for goods and services, and translates into higher levels of informality among workers and firms.

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2 See McCulloch, World Development (2003).

3 See Lustig (2000).

Lower commodity prices also reduce government revenues. The contraction of overall fiscal resources traditionally translates into reductions in public expenditures in social sectors. Finally, despite the more consistent nature of remittances flows in comparison with other income sources, the constricting opportunities in OECD countries have already translated into a decline in the absolute volume of remittances, for example, in countries such as Mexico, Haiti, and Honduras.[4]

[4] See MIF (2009).

3 Deploying an Effective Social Safety Net

An effective social safety net provides a minimum level of welfare in light of the diverse risks faced by families, including individual shocks such as health and labor disruptions, and aggregate shocks such as natural disasters or financial crises. If safety nets with a good track record exist (e.g., with efficient mechanisms to target the most vulnerable, enroll, deliver and monitor transfers) which also nurture investment in human capital and promote future potential productivity gains, then they should be supported and expanded during the crisis. If they do not exist, increases in the level and depth of poverty might create an opportunity to promote policy reforms to establish them, although, if the process is started from scratch, it might require at least a year, if not longer.

Over the past decade many countries in the region have put in place programs to address issues of structural poverty, whereas programs to manage risk are more incipient. In terms of addressing structural poverty, LAC has been the cradle of one of the most popular versions of targeted income transfer schemes: conditional cash transfer (CCT) programs which aim at providing income support to households while promoting human capital investments especially for the younger generation. Over the last decade, CCT programs have grown in number and size. However, the almost two dozen CCT programs currently in operation vary in scope and coverage, with only a few national programs (for example in Mexico and Brazil) covering close to all of the poor or extremely poor in their respective countries. CCT programs or CCT-like components are only rarely part of a more holistic social protection system (such as in the case of *Chile Solidario* in Chile).

CCT programs' incomplete coverage of pre-crisis chronically poor in many countries, leaves their expansion as an important option in response to the crisis.[5] However, experience shows that once coverage is expanded, scaling down remains a challenge;

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[5] See Johannsen, Glassman Duryea, Robles, Tejerina (2009) for more details.

as a result, the long-term fiscal implications should be carefully assessed. Public expenditure "switching" strategies might need to be enacted by financing targeted programs through restructuring generalized consumption subsidies of energy or food, or eliminating transfer schemes which involve a high fiscal burden but are often not targeted to the poor.[6] Moreover, expansion of CCT programs might not be entirely feasible in the short term if under-coverage is generated by factors beyond budget limitations including absence of viable payment alternatives or, more importantly, suitable supply conditions. Restricting "conditions/co-responsibilities" to a minimum meaningful set could be pursued while putting in place the right supply-side incentives to improve coverage and quality of essential health, nutrition and education services.

Depending on the country context, adjustments to the design and operation of existing CCT programs could be warranted to mitigate welfare losses of the chronically poor during the crisis. For example, transfers' amount could be maintained in real terms to prevent inflation-related erosion in purchasing power (although in the current low inflation environment this risk seems limited). Transfers could be temporarily increased on an "exceptional" basis to also compensate for estimated reductions in other sources of household income, although downward revisions post-crisis should be credible and enforced. In some cases, the frequency of payments could be increased but the cost implications of such modification should be examined *ex ante* given the potentially higher administrative costs involved in terms of both greater number of transactions and more frequent verification requirements.

Whereas CCT programs have been shown to be effective in addressing issues of structural poverty and in ameliorating the effect of an aggregate shock on existing beneficiaries (such as in the case of Nicaragua and Indonesia), these programs traditionally have not developed administrative and targeting mechanisms that could rapidly and accurately assess the eligibility of the newly poor and promptly remove them from the program rosters when their situation improves. An analysis of CCT eligibility rules and other design features that is perhaps more responsive, for example, to household income volatility could be carried out. However, the primary focus of CCT programs should remain structural poverty.

While an important component of an effective safety net, CCT programs should not be expected to address all vulnerabilities. For addressing the acute needs of the new poor, other instruments such as self-targeted temporary employment programs are better suited to provide income support in response to a crisis of short duration, as discussed in the next section.

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[6] See Lindert and Skoufias (2008) for more details.

4 How the Crisis May Affect Labor Markets

Perhaps the most visible impact of the crisis is in workers losing jobs. Most of those affected would be the "newly poor" with the biggest immediate concern being large pools of unemployed that create ripple effects in other sectors and diminish economic activity. Absorbing large pools of labor temporarily will not be the way out of this crisis for the region. Compared to other regions of the world, Latin America and the Caribbean has not made the systematic changes in the way its labor markets operate—its systems of training, employment generation, human capital formation, labor ands social security regulations—to enable it to exit from this crisis in a stronger competitive position. The global nature of this crisis means that the region may not be able to "muddle through" waiting for export growth or wage declines to diminish the need for more fundamental reforms. As a result, while LAC governments may feel the pressure to initiate programs to stave off key short-term effects, the most critical element will be to simultaneously initiate key systemic labor market policy and program changes to lay the foundation for the region to emerge from the crisis not leagues behind its international competitors and with the foundation of stabilizing policies to react to future crises on a more immediate basis.

More specifically, the labor market transmission channels are expected to be different in this crisis than in past ones. First, in the early stages, unemployment, particularly in the export-dominated sectors (e.g. automobiles, agriculture, mining) and tourism is expected to rise and have a large impact. This can be seen in its early stages now in the mining sectors (e.g., Dominican Republic, Chile), textiles and apparel (e.g., Honduras, El Salvador, Dominican Republic) and auto industry (e.g., Mexico, Argentina). In past crises, unemployment was not as much a factor, with many countries adjusting largely through falling average real wages in the context of sharp inflationary outbursts associated with the crisis; real wage adjustment put greater burdens on the poor as well as brought in new poor. In this crisis, given the current low inflation environment, downward pressures on real wages are likely expected over the medium-term, if the crisis is prolonged and economy-wide. Second, the quality and size of formal sector employment—already suffering in most of the region—would likely decline further. Formal workers would lose health benefits and no longer contribute to pensions and potentially move to the informal sector without such basic coverage. In such an environment, an increase in discouraged workers (those who temporarily quit looking for work) is expected, as has happened in past crises. In the short term, the pressure on the region's pension systems will be focused on a relatively small group of beneficiaries—those closest to retirement age—who want to draw on pension funds which have lost value. The medium term for pension systems is more troubling as fewer contributors and an uncertain financial environment may call into question either the financial viability of some systems, or the likelihood that workers will accumulate sufficient contributions given that they will spend critical years of their working lives in the informal sector. A final factor, distinct from past crises, is labor migration. Previously outmigration to OECD countries and increased remittance flows back to the region were considered important safety valves for deteriorating employment conditions. The opposite trends are occurring in this crisis. There is evidence of a drop-off in the value of remittances in key countries; to date migrants losing work seem to be staying put and looking for other employment,[7] although key countries in the region are starting to note an increase in return migration. The latter is not yet shown in official statistics.

Overall, the medium-term scenario is not a pretty one: increasing levels of already high informality, lower labor force participation, falling real wages, pressures on pension systems and, most importantly, little to no new growth in formal employment. Should the crisis be L-shaped, it will be those countries which initiate key structural changes, both social and labor market-related, that will emerge best from the crisis and positioned for the future. Below policy options are divided into those **short-term measures** designed largely to absorb unemployed workers or workers at risk of losing jobs vs. **systemic measures**—more fundamental changes in programs and policies which also must be considered "immediately" as well to build the foundation for exiting from the crisis. Most of the measures discussed in this report correspond to the area called "active labor market policies". They do not constitute the whole range of policies that affect labor markets and, in particular, the conditions for job creation. Macroeconomic policies and policies to spur small and medium business development—the largest sector of job generation in the region—such as those aiming at preserving access to credit, play a critical role in employment and job creation, but their discussion goes beyond the scope of this report. Nonetheless, this section addresses the issue of human capital development within SME policies.

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7 Regarding migration see Papademetriou and Terrazas (2009).

Short-Term Policy Measures

The most worrisome trend in the short term is growing unemployment and poverty due to layoffs in export-related sectors that have ripple effects in supplier and market-sensitive sectors (e.g., tourism), swelling the rolls of the newly poor and unemployed. In a short duration crisis the labor "problem" is principally a social one—pools of the newly poor and poor with few prospects for reemployment.

If the crisis is short-lived, the policy alternatives countries may want to consider include retaining or absorbing pools of workers in jobs in the short run (1–6 month range, either via short-term training or temporary employment) and protecting key worker benefits. Whether a country sees a need for such instruments depends on the scale of job loss, reemployment prospects, and regional impacts.

Short-Term Measures to Retain or Absorb Workers in Jobs

If countries want to react quickly, institutional capacity really matters in either delivering to workers temporary jobs or short-term training. Both instruments are intended to absorb workers for short periods and have distinct pros and cons.

On the Job Training (OJT)—*to both retain employed workers ("keep the insiders in") and employ the unemployed ("bring the outsiders in")*. Long-term and classroom-based labor training (more than one year, typically for the non-poor) has a very mixed record in getting the structurally unemployed back into the marketplace. Short-term training, however, if it is done in the workplace and related to improving skills for a specific job, has a much stronger record both in getting the unemployed re-employed and upgrading existing worker skills.[8] If the crisis is truly short-term, and there is some employment growth or prospects for keeping key firms operating, OJT can be a method of bridging the unemployment period with skill development in place. Both instruments have been utilized in OECD countries and East Asia during crises. Training for employment retention, however, needs to be particularly well targeted to those jobs in risk of layoff during the crisis but competitive over the medium term. Targeting can be accomplished in a number of ways: to high job loss sectors (e.g., maquila), vulnerable regions (e.g., mining areas), low-work seasons (e.g., low tourism seasons).

If programs are constructed via modifications of existing training programs, they can be fairly straightforward to execute and targeted to lower-income workers by keeping the training salary close to the minimum wage. If no institutional base exists, OJT is harder to implement quickly during a crisis. It is essential that OJT not

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[8] See STPS 1995, Hernandez Laos (2001), IDB/Office of Evaluation (2006).

be confused with public sector-based training models which have demonstrated little to no labor market benefits. LAC has experimented extensively with youth training models which are a mix of OJT with classroom-based skills training [e.g., *Chile Joven*, *Argentina Joven*, *ProJoven* (Peru), *Procajoven* (Panama)]. These models have been largely successful in getting at-risk youth into new employment, but rely on firms who have the potential to hire new employees. For those countries with employment growth prospects, expansion of such models, or adaptation to adults, is another viable short-run measure.

For employed workers, OJT training (from 2–6 months typically) acts, in effect, as a wage subsidy, as the employer receives a training subsidy from the government for the worker's salary (usually 1–2 minimum salaries). OJT is typically a better adaptation to a crisis than a wage subsidy because its temporary nature does not distort salaries or incentives within the firm and can be targeted easily by region, industries, or job level. This is an employment retention strategy, however, only if the crisis is perceived as short-term and that the workers will resume jobs in the firm after the crisis period. If these are jobs that will be lost in the medium-term, then OJT merely has the effect of postponing unemployment, and in this case, acts just as a form of short-term unemployment insurance.

There is even more international and regional experience for OJT as a form of inserting unemployed workers into new jobs. These training subsidies, if based on an existing program base, can be scaled up and targeted to areas of high unemployment.

Table 1: How Much Would On-the-Job Training Cost?

The fiscal implications of enacting on-the-job training as a crisis instrument need not be overwhelming, even for large numbers of trainees. Traineeships, if targeted to lower income levels, are some multiple of either the minimum salary up to two minimum salaries. Using a current regional example, the minimum salary (estimated for six months plus transportation assistance) results in a per beneficiary cost of US$911. This means that 100,000 traineeship subsidies for 6 months—a longer period than typical—could be provided for approximately US$91.1 million. More workers could be served for shorter training periods of 1–3 months. If we use previous cases to estimate potential administrative costs (in the range of 10–15% of subsidy levels), program expenses total in the $US100–104 million range for the outlined program.[9]

[9] IDB Staff calculations using the case of mexico based on published 2009 minimum salary using current exchange rate (December 2008) of 13 pesos to the dollar. If the official 2009 exchange rate of the Mexican government is used (11.2 pesos/US dollar) program costs would rise proportionately. This includes transportation costs of MX$11.

If the crisis persists to the medium term, however, OJT to support increased labor insertion of the unemployed is much less viable, e.g., it will be harder to get employers to agree to employee trainees after the traineeship period if firm viability is in question. If the crisis should extend to the medium-term, this report suggests a form of integrated training-technical assistance and credit (see discussion below) that is more oriented to assisting firm growth and productivity as labor insertion will not be a feasible goal for short-term training.

Beyond the instrument of short-term on-the-job training, there are a host of short-term labor contract adjustments to temporarily lower labor costs which can be initiated by firms without government subsidy or support. These include short work furloughs, unpaid vacations, part-time employment, etc. Such actions can be seen already by firms in countries like Argentina and Chile. The governmental role in such cases is to insure a regulatory environment for such crisis adjustments without undermining the longer term quality of employment.

Temporary Employment and Public Works. With the prospect of unusually high unemployment and few unemployment insurance programs in place to compensate, the most common policy assumption made by policymakers is that they need a temporary employment program. These kind of programs have operated in many countries in the region, East Asia and Eastern Europe. They are used to keep very poor, unemployed workers earning a basic income in their home regions. Temporary employment is thus a labor absorption tool to deal with a severe unemployment crisis, especially one affecting low-skilled poor workers. Temporary employment is a pure short-term instrument—it has no measured significant positive medium- term impact on workers—and in a number of cases participating in a temporary employment job has been found to have negative effects on workers' ability to get jobs post-crisis (e.g., Chile, due to the stigma attached to poor and unskilled work.).

The emphasis of temporary employment is getting the most employment for dollar spent. Labor-intensive works such as building or maintaining rural tertiary roads, street cleaning, re-forestation are typical temporary work projects. A second model that countries often consider is public works investment projects which have labor benefits. In these cases, countries would be putting a higher premium on the value of the public works and less on the number of short-term jobs generated. Public works jobs can include a range of relatively high to low income jobs.

Temporary employment works best as an instrument to employ low-skilled poor workers for short periods (1–3 months typically). Its price tag can rise quickly above its value if administrative costs are not kept in check and the type of employment contracted is not heavily labor-intensive so that the majority of costs go to pay the salaries of workers. The key recommendations from previous policy reviews are: setting wage rates below minimum wage so that only the poorest apply; targeting employment to regions where there are large pools of poor unemployed; and keeping administrative costs low (10% or below of total program costs). Administrative capacity to quickly launch such programs is key. LAC has used more models of temporary employment administered by government agencies; East Asia nations have used a bit more models to contract out temporary employment jobs to private or non-profit firms. If the current crisis should stretch into a longer scenario, however, temporary work programs provide less relief as workers find it difficult to find new work. It is important for Latin American and Caribbean nations to keep the "temporary" in temporary employment and dismantle these programs after the worst part of the unemployment crisis is over. Unfortunately, it has been more typical that such temporary programs start too late to address the worst of the crisis and continue too long.

Extend Worker Benefits through Crisis Months. Few Latin American and Caribbean countries have unemployment insurance (UI) programs to protect workers incomes in the event of unemployment. OECD countries, however, have a series of short-term benefit extensions that can be employed to cushion unemployment. A six month extension of health insurance eligibility (COBRA), for example, is possible in the United States (workers pay a higher share in such cases). Developing countries may also consider crisis aids such as short-term health benefit extensions, social security payment extensions, or catastrophic medical coverage extensions. However various issues should be considered before implementing this type of measures: fiscal implications; targeting and eligibility challenges; their credibility and enforceability as "short-term" measures; and, last but not least, the risks of increasing incentives towards informality for both firms and workers (for example, firms laying off and then re-hiring workers informally since workers' health benefit coverage becomes subsidized by the government).

Systemic Policy Measures

The longer duration scenario is something Latin American and Caribbean labor markets have not faced in past crises—4–5 years with few new formal jobs. Should this be the scenario, "absorption" or palliative measures will postpone unemployment but have no impact on underlying labor market conditions. In a low growth scenario, Latin America and the Caribbean can only achieve more or better jobs principally via three groups of instruments: (i) helping firms (and their workers) be more productive, (ii) changing the fundamentals about how human capital is protected, allocated (fitting the right people into the right job), and formed, and (iii) changing the relative costs and benefits of formal vs. informal employment for firms and workers, taking structural steps to lower labor costs in the formal sector to improve both productivity and growth, while expanding the scope of social security.[10]

Measures to Increase Firm Competitiveness

Labor Training and Human Resource Restructuring. Countries would be well advised to initiate or reform current training systems to incorporate more dynamic and effective models of training that combine training of the workforce with technical assistance to the firm, credit, and human resources management. Simply put, training needs to be part of a human resources strategy of the firm that may include moving into new markets, restructuring work better, and introducing new, more efficient processes. Training in Latin America and the Caribbean is too often divorced from firm needs and conducted in an isolated fashion apart from other human resource and technical changes within a firm. Mexico's former CIMO program (*Calidad Integral y Modernización*) combined the key elements of human resource diagnostics of firms, training related to the human resource modernization plan, and technical assistance to implement firm-level changes (from marketing, to product management, to processing) with positive results.

This instrument cannot start massively; rather, it requires the building of the infrastructure (specialized industry-based promoters who can assist firms) and relationships with firms that can make this work as a motor for advancing firm competitiveness. Mexico's CIMO program was built on using industry associations to house promoters and link them directly with area firms. It then was expanded during crisis times, building on already established relationships with firms. A longer crisis, with changed competitiveness conditions at its end, will make it important for many countries to begin to build firm-based human resource development models that can become an essential element in the "infrastructure" of competitive labor markets in the future. The government role is to provide the incentive structure for this type of pro-competitiveness, integrated human resource strategies; it cannot hope to reach all firms. Over time, larger firms will tend to adopt such models without government incentives (through demonstration effects) and public subsidies can be focused on small and medium firms in emerging sectors.

Measures to Support and Better Allocate Human Capital

Improving Human Capital Formation through Technical Education. Short-term human capital interventions (e.g., training, temporary employment) will do little

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[10] See Levy (2008).

to fundamentally shift the way Latin American and Caribbean countries prepare the workforce for the future. While LAC has made significant progress in education coverage, education quality, technical education and readiness for the workplace lag far behind other developing regions. Developing countries that have proven to be export and technology leaders, e.g., India and other countries in Southeast Asia, have done so by turning around their education systems, particularly at the secondary and university levels, both to better prepare workers and to use such institutions as catalysts for technology advances and innovation. A medium-term investment to improve the region's human capital base should include reform and modernization of technical education, creation of community colleges or technical colleges linked to local industries and services, as discussed in Section 6 of this report.

Restructuring Labor Benefit Systems to Serve Future Crises: Severance Pay and Unemployment Insurance. A longer term crisis may put key labor-derived benefit systems at risk—either in terms of financial solvency or the ability to serve beneficiaries just when the crisis demands it. This particular crisis could pose great challenges to portfolio-based benefit systems given the simultaneous unraveling of key financial institutions and investments. These benefit systems may have large "drawdown" needs while values are dropping, compelling nations to put such benefit systems on sounder financing footing or enact reforms to insure their viability and utility post crisis. Firm closures or slowdowns may cause many firms to renege on or contest employee-provided benefits such as severance and vacation pay or unemployment insurance eligibility. Key benefit systems discussed here are severance payments and unemployment insurance.

Large numbers of firm failures and bankruptcies may force many firms to abandon legal obligations for severance payments or, at a minimum, postpone or deny benefits to workers to ease the burden of the crisis. Such a situation provided Barbados an opportunity to enact an unemployment insurance program which provided a system of more secure payments to workers over time.[11] The current crisis, if continued over the medium term, could provoke similar moments where reform, restructuring, or enactment of new benefit systems could be part of the response.

Very few countries in the region have *unemployment insurance systems* to protect incomes during the crisis. Chile has the largest system, while smaller systems (coverage of 4% of the workforce or less) exist in a handful of countries (e.g., Uruguay, Argentina, Brazil, Barbados, Jamaica). Overall, UI systems in LAC are for much shorter durations and lower levels of income replacement than their OECD counterparts. In past crises, even these small coverage systems were overwhelmed by the demands

[11] See Mazza (1998).

of higher levels of unemployment, and benefit levels were reduced from low levels (via shortened periods of time, increased requirements for eligibility) even while fiscal costs rose.[12] Although an efficient UI system is administratively difficult and fiscally challenging to set up in a crisis (because of high demand for payouts before surpluses can be accumulated), it has been done in the past as high firm bankruptcies may put into crisis the severance payment system. As mentioned, Barbados took advantage of such a crisis to reform its system of severance pay. Since many firms escaped paying generous severance payments in crisis times, there was consensus from both the private sector and unions that a UI system would be a more reliable alternative covering more workers.

Building the Infrastructure to Help Workers Get Jobs. If they work well, labor intermediation systems (e.g., job finding services) help get workers into jobs quicker and more efficiently (like better matches of workers to jobs) than local job hunting on its own. OECD research has amply identified employment/intermediation services as the most cost effective active labor policy investment.[13] Intermediation services maintain active listings and relationships with employers on current jobs, help prepare and direct workers for job search, and help move workers into needed training or other labor support services. In OECD countries, many intermediation services also serve as the gateway for unemployment insurance and other social services.[14]

In a short-term crisis, the job matching function of intermediation services is often less pronounced due to the falloff of new job listings. Over the medium term, however, investments in more modernized intermediation services are important to provide the future platform for a more efficient movement of workers economy-wide, particularly in countries with so much informal, inefficient job search. Modernizations beginning now in the region can include: reforms and service upgrading (e.g., computerization, quality control systems, staff training, mobile services for rural workers, electronic job banks), expanding connections with employers, and focusing instruments on moving workers into higher quality jobs. It is highly recommended to create complementary labor market information systems and capacity to conduct labor market surveys again to better respond to market trends.

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12 See Mazza (1998).
13 See Martin (2009).
14 See Mazza (2003).

Table 2. Potential Responses with Respect to Labor Markets

Short Crisis Scenario	Long Crisis Scenario	Comments
• Retain workers in employment – OJT subsidies • Benefit extensions	• Improve firm competitiveness – Integrated training, credit, technical assistance services – continue credit and support to SME sector – regulatory reform	*Short-term actions lose value if crisis is prolonged, systemic measures for firm competitiveness must to begin immediately whether short or long crisis.*
• Absorb pools of unemployed labor – Temporary employment programs – Public work programs – OJT for unemployed	• Building of training and intermediation infrastructure to improve services	*Short-term measures to be deployed only with large scale unemployment of "new poor"; no positive medium-term labor impact; systemic measures to improve active labor market policies needed immediately regardless of length of the crisis.*
	• Improve human capital formation, technical education, community colleges	*Essential for development of regional labor force and competitiveness.*
	• Restructuring labor benefit systems for improved coverage of workers, sustainable benefits	*Longer crisis may motivate creation of more stable financing of key labor benefits and broader coverage, particularly of the poor.*

5 How the Crisis May Affect Health and Nutrition

Macroeconomic crises can have important detrimental effects on population health outcomes. These effects operate through three main channels: (i) reductions in public spending on health generated by lower revenues leading to reduced availability and quality of services; (ii) reductions in private spending on health instrumented through decreases in out-of-pocket spending and drops in health care utilization and health insurance coverage; and (iii) direct impact of crisis on the most vulnerable individuals, for example through a worsening of early childhood nutrition, which can have permanent effects on children's physical and intellectual health as adults.

Both public and private health spending drops substantially during crisis. Data from the 1980s indicate that public spending per person on health was much lower by the end of the decade than at the start, and health was also found to be given lower priority within public budgets. The crises of the late 1990s suggest that this pattern has continued; in Peru, for example, public health spending dropped 60 percent between 1988 and 2002. During the 1995 Mexican crisis, consumers reduced health spending in a larger proportion compared to the drop in income. These drops in health spending may be accompanied by important health utilization reductions, especially for primary health care by children and by poor households. In Colombia, cuts in non-salary spending items such as the purchase of vaccines resulted in very low vaccination rates during the 1997–1999 period, putting group immunity at risk.

Related to spending cuts, quality of care may also be affected. Although there is little direct evidence, facility data from the 1999–2002 Argentine crisis suggest that cardiovascular mortality during hospitalization and incidence of medical complications may also have been affected by financial crisis.[15]

Given that insurance via social security institutes and group private insurance plans is linked to employment, it is likely that formal sector job losses will be accompanied by

[15] See Garfinkel et al. (2005).

the loss of health insurance coverage unless governments and social security institutes take mitigating actions to assure continuity of coverage. In Argentina in 2002, for example, drops in health insurance coverage associated with job losses led to increased demand for public services, while spiking poverty led to decreasing ability to pay for the most basic medicines.

The most vulnerable individuals suffer the most. Consistent evidence from previous crises points towards increases in infant mortality. Pooled data from 59 developing countries suggests that negative economic shocks, especially large ones, produce substantial increases in infant mortality. In Mexico, mortality rates for the very young and the elderly increased or declined less rapidly in crisis years, as compared with non-crisis years. During the 1995–96 crisis, mortality rates were about 5 to 7 percent higher than in the years just prior to the crisis. Indonesian data also show that the late 1990s financial crisis led to an increase in infant mortality of about 1.4 percentage points. During the 1988 crisis in Peru, infant mortality increased about 2.5 percentage points for children born during the crisis.

Short-Term Policy Measures

Monitor and protect public spending on essential public health programs. To protect health, a minimum requirement during crisis is to maintain essential public health programs, such as immunization, control of communicable disease (TB, HIV/AIDS), control of vector-borne diseases (malaria, Chagas, dengue, NTD), and safe blood supply, among others. Although not public or merit goods, other health promotion activities—such as prevention and control of chronic diseases like hypertension, diabetes and mental illness—are also important to maintain (and scale up) given the current disease burden in the region and the effects of crisis on these outcomes. While all countries have run essential public health programs for decades, the effectiveness of such programs is dependent on the availability of non-salary inputs (like vaccines) that are frequently vulnerable when across-the-board spending cuts occur.

Maintain and improve the quality of preventive nutrition services in primary health care. In terms of nutrition, budgetary allocations and actual expenditures can be increased and protected for those nutrition interventions that effectively prevent rapid weight loss and growth faltering or safeguard the very young from nutritional deterioration in times of crisis. Priority programs are: (i) promotion of exclusive breast-feeding in the first six months of life; (ii) active growth promotion at the community level and in health services, including promotion of minimum monthly weight gain, education on feeding and care behaviors, monthly growth monitoring and promotion services for all children zero to 24 months of age, and referral of children; and

(iii) distribution of micronutrient supplements to pregnant women and children six months to 5 years.

The quality of care in well baby visits should be protected or improved such that growth promotion and education activities are adequately performed, beyond the mechanical taking of anthropometric measures. Serious consideration should be given to the provision of supply-side incentives to points of service that target the poor in order to maintain or improve coverage and quality of nutrition services, especially prenatal and well-baby services. Supply-side subsidies for micronutrients, alongside subsidies for key medications like antibiotics, should also be considered.

Targeted support for micronutrient supplementation. Where rapid appraisals demonstrate pervasive household food insecurity associated with the financial crises, subsidies will be efficient policy responses provided adequate targeting mechanisms are in place and rapid evaluations are conducted to inform quick up-scaling when appropriate for: (i) micronutrient supplement stamps or vouchers (as Guyana, Brazil and Argentina have introduced); (ii) free distribution of micronutrient supplements and (iii) school feeding programs, preferably using fortified staple foods. All of these policy options should include clearly defined scale-down strategies that should be pursued when the situation improves and improvements appear sustainable.

Avoid drops in health care utilization of critical services. Where appraisals demonstrate pervasive drops in health care utilization of critical preventive and disease control services, targeted demand-side subsidies and fee-waiver programs can help households to cover both indirect and direct costs of accessing care.

Expand or adjust CCT programs. Depending on the country, the health and nutrition components of a CCT can be strengthened in response to the crisis. More intensive prevention and disease control efforts are needed during recessions, and CCT programs are ideal instruments to cover the indirect costs related to accessing preventive health care, especially for poor families with small children. The quality and thus effectiveness of the preventive care provided via the public clinics that participate in CCT programs in the region remains an important issue.

Maintaining the preventive nutritional components of CCTs is essential for pregnant women and children under 2 years of age. Compliance with the health and nutrition conditionalities of beneficiary households with children under 5 years should be verified, especially attendance of well-baby visits. If need be, the health conditionality for well-baby visits should be upgraded to monthly visits for all children less than 24 months; for pregnant women five prenatal controls should be expected. Weight gain during pregnancy should be adequately monitored in these controls and infections aggressively treated.

Provide vouchers for key services to the poor. Where public services can not accommodate increased demand, countries may consider the use of targeted vouchers to subsidize the price of health services and products with the goal of improving access and utilization. Vouchers are a variant of a conditional cash transfer, but may imply lower information system requirements and allow for the use of private providers (most CCT programs are limited to public providers). Subsidies go directly to the health care consumer (patient) in the form of a voucher—a certificate or other token—that the consumer redeems when seeking care, usually from a private sector provider.

Establish a targeted fee waiver program. User fees have been in place for decades virtually everywhere, responding mainly to a lack of public funding. While there are advantages to fees, in the context of falling household incomes, fee waivers can be put in place to protect poor households, assure the delivery of specific services and correct for incomplete markets in health insurance. It is important to restrict the benefits included under waivers to those services that create the most health benefits or greatest externalities. However, it should be noted that freeing the most vulnerable from out-of-pocket payments may not suffice to promote access to care, given the indirect costs associated with reaching services, especially for the poorest segment of the population. For this reason, targeted fee waivers or exemptions should be paired with CCT programs where possible. The most common implementation challenges for targeted fee waiver include: promptly compensating providers for forgone revenues to avoid compromising quality of care and targeting exemptions (though, the latter could be simplified if fee waivers are associated with other targeted programs such as CCT programs).

Systemic Policy Measures

The quest for universal health insurance coverage compatible with growth in labor productivity and output. In most countries in the region, insurance and household protection against health shocks are tightly linked to employment status. In the context of the region's segmented health systems, formal sector workers are covered by insurance provided by social security institutes and the rest of the population seeks insurance and care in both the public and private sectors. The reform agenda to delink health system financing from labor market status and to unbundle health insurance and pension benefits has not yet made significant progress. However, the spectrum of a prolonged L-shaped crisis and of the loss of formal sector jobs and health insurance coverage for millions of workers in the region brings renewed urgency to the issue. The pursuit of reforms to achieve universal health insurance coverage while creating incentives to boost formal job creation, labor productivity and output growth is critical today more than ever.

Table 3: Potential Responses with respect to Health and Nutrition

Short Crisis	Long Crisis	Comments
• monitor health indicators	• monitor health indicators	*Critical under both short-term and long-term crisis scenarios.*
• protect public spending on essential public health programs	• protect public spending on essential public health programs	*Critical under both short-term and long-term crisis scenarios.*
• expand or adjust CCT program	• expand or adjust CCT program	*Warranted only if pervasive drops in health care utilization of critical preventive and disease control services are detected.*
• Strengthening school feeding programs with fortified staple food		*Warranted only if household food insecurity is pervasive.*
• targeted fee waiver		*Warranted only if pervasive drops in health care utilization of critical preventive and disease control services are detected.*
• Vouchers for micronutrients		*Warranted only if household food insecurity is pervasive and drops in health care utilization of critical preventive services are detected.*
• Temporary extension of health insurance for formal sector workers		*Caution with: fiscal implications; targeting and eligibility; credibility and enforceability as "short-term" measure; risks of increasing incentives towards informality for both firms and workers.*
	• Benefits and financing reforms to achieve universal health insurance coverage while creating incentives to boost formal job creation, labor productivity and output growth	*Systemic measure. A long crisis scenario increases its urgency.*

6 How the Crisis May Affect Education

In the absence of widespread instruments to smooth shocks, families may be forced to adjust to the decline in household income by increasing the supply of economic activity by children and by decreasing investments in children's education ("income effect"). In LAC where indirect costs of school attendance at public schools can be considerable relative to households' income and especially for the poor, reflecting transportation fees, uniforms, books and parent association fees, some families may be unable to maintain children in school as income falls. At the same time that total household income is falling as a result of the crisis, particularly in households experiencing job separation, labor market opportunities for children are also contracting. This effect, referred to as the "*substitution effect*", implies that the labor supplied by children will fall as a result of the decline in aggregate demand. The relevant question is, therefore, whether the income effect or the substitution effect will dominate in response to the crisis. The body of economic literature addressing this question has generally found that the substitution effect protects school attendance in an aggregate crisis as has been demonstrated in the cases of Argentina, Brazil, and Peru during the crises of the 1980s and 1990s for primary and secondary school-aged children.[16]

Much more worrisome, at least in the short-term, is the potential impact that a decline in public expenditures on education could have on quality of education provided by publically funded institutions, given LAC's rather dismal performance pre-crisis. In Peru during the 1987–90 crisis public expenditures on education fell by nearly 50%.[17] Teacher salaries tend to have the most acyclical tendencies, but other critical inputs linked to education quality such as textbooks tend to be pro-cyclical, with budgets declining at the same time enrollment expands. Although rigorous studies have not addressed the impact of declines in expenditures, teacher inputs, or student time on school quality,

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[16] See Duryea and Arends-Kuenning (2003); Lopez Boo (2008); Schady (2005).

[17] See Schady (2005).

a negative correlation has been observed during economic crises, particularly with the decline in PISA international test scores in Argentina over the period of the economic crisis beginning in 2001. Teachers facing job losses by other family members or falling own real wages may increase their time on income-generating activities outside the classroom. A reduction in hours or efforts in the classroom may deteriorate the quality of services offered to students (real salaries of teachers fell 22% in Mexico in 1982–83; 50% in Peru in 1988–92; 50% in Costa Rica in 1980-82; 33% in Argentina in 2002). Studies in Chile have found that teachers who work excess hours achieve lower results in performance evaluations. A similar phenomenon occurs at the child level. As the time of poor children shifts toward income-generating activities and away from schoolwork, the performance of children in school deteriorates.

Although higher income families are unlikely to face the difficult decision of removing their children from school in response to falling income, some may transfer their children from private institutions to public schools, placing more stress on the public systems in terms of class sizes and related materials. Although rigorous studies of this channel have not been conducted, this pattern has been observed during economic crises in Bogotá, Colombia (2000–2002) and in the Province of Buenos Aires, Argentina (2002).

Short-Term Policy Measures

Monitoring Enrollment. The monitoring of administrative data can serve as an early warning function regarding major shifts in enrollment and attendance. Real-time monitoring systems can be put in place with limited administrative burden.

Protect Core Public Expenditures. This is probably the most critical of the interventions under both a V-shaped or L-shaped crisis scenario. In addition to teachers' salaries, expenditures in areas that have been demonstrated through rigorous studies to improve performance should be protected from budget cuts. These include non-salary expenditures on textbooks, teaching materials and teacher training.

Expand or Adjust Conditional Cash Transfer Program. If school enrollment and attendance are falling in response to the crisis, existing CCT programs can be expanded to cover the chronically extreme poor especially in countries where these programs reach only a fraction the extreme poor as discussed in Section 3.

Temporary Scholarships. Should declines in school enrollment result, well-targeted scholarships can be considered, especially in countries where CCT programs are not available or their scaling-up cannot be pursued in the short-term. Argentina's National Program of Student Scholarships, launched in the last crisis, has been effective at keeping children in school. Indonesia enacted the Scholarships and Grants Program in 1998 to respond to its crisis. Many programs begun in a crisis, however, are not phased out when the economy improves. The distribution of scholarships must follow clear and transparent procedures, as scholarships have a long history of discretionary influence.

Systemic Policy Measures

In a longer recession the fiscal challenges will loom much larger, translating into a high risk of declines in public expenditures on salary and non-salary intermediate inputs which could undermine the quality of the education provided. While parents may be able to cover school-related expenditures in a shorter crisis by decreasing consumption of other goods or borrowing through family or informal channels, a longer crisis brings a moderate risk of children leaving school. In addition, the nutrition impacts previously addressed imply that a smaller percentage of children will be physically ready to enter school, and will therefore delay entry. A longer recession places the school-age population at risk of exiting the crisis with significant human capital deficiencies, putting the competitiveness of the economy at risk.

Improving Human Capital Formation. As previously noted, in LAC significant improvement is needed in the formation of human capital such that the workforce of the future is adequately prepared. A comprehensive body of educational literature finds that of all inputs associated with education systems, the quality of teachers is the most important. Significant reform is required in the national systems that educate teachers as well as in the institutional mechanisms that attract and maintain effective teachers. To advance the productive skills of the generation that will be entering the labor market to a changed world, educational systems in LAC must realign institutional and student incentives toward performance rather than attendance. A medium-term investment to improve the region's human capital base should include simultaneous efforts to: (i) reform and modernization of technical education, create community colleges or technical colleges linked to local industries and services and (ii) better align curriculum at the secondary level with core competencies demanded across labor markets (e.g., communication, critical thinking, problem-solving, and group work).

Table 4. Potential Responses with Respect to Education

Short Crisis	Long Crisis	Comments
• monitor school enrollment	• monitor school enrollment	*Critical both under short-term and long-term crisis scenarios.*
• protect core public expenditures	• protect core public expenditures	*Critical both under short-term and long-term crisis scenarios.*
• expand or adjust CCT program	• expand or adjust CCT program	*Warranted only if enrollment and attendance fall.*
• targeted temporary scholarships		*Warranted only if enrollment and attendance fall and CCT programs are not available or their scale-up is not feasible in the short term.*
	• introduce CCT program	*Systemic measure. A long crisis scenario might increase the need for demand-side interventions.*
	• align curriculum and technical education with core competencies in labor market	*Systemic measure. A long crisis scenario increases its urgency.*
	• align institutional and student incentives toward performance rather than attendance	*Systemic measure. A long crisis scenario increases its urgency.*

7 A Final Word

The uncertainty regarding recovery scenarios in LAC, a direct result of the nature of the current global crisis—large scale, with epicenter abroad and systemic—presents complex and in some sense novel challenges for policymakers in LAC. Given this situation, this report argues that an assessment of the inter-temporal trade-offs embedded in social and labor market policy responses may not be a luxury which at present countries cannot afford, but an essential element that cannot be ignored.

To the extent that the likelihood of a protracted crisis increases, only short-term policy responses that offer a high degree of social protection, are fiscally sustainable and are aligned with, or at least do not undermine, long-term productivity and medium-term growth should be deployed. Moreover, if the likelihood of such a scenario increases, so should the urgency of credibly phasing out short-term measures to leave ground, as soon as possible, to more systemic reforms aimed at simultaneously strengthening social protection and removing distortions that limit growth in output and labor productivity in LAC. Of course, the appropriateness of individual policies will depend on the specific conditions of each country.

Finally, it is clear that the viability and effectiveness of social and labor market policy responses to the crisis hinge upon countries being able to maintain macroeconomic policies that prevent countries from entering financially risky territory, as discussed in the parallel report *Policy Trade-offs for Unprecedented Times*. In turn, strengthening social and labor market policies to protect the most vulnerable could contribute to the sustainability of prudent macroeconomic policies.

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