Opening address
at the BIS Conference in Honour of Palle S Andersen

Malcolm D Knight

Good morning, ladies and gentlemen, and a warm welcome to Basel and the BIS. It is a great pleasure for me to open this Conference on "Globalisation and population trends and their implications for labour markets and inflation". As you know, we have organised this conference to honour the late Palle Andersen. Palle was a leading BIS macroeconomist for over two decades, and he made many important contributions to the topics you will be discussing here today. Let me note that here at the BIS we have missed and continue to miss Palle's deep insight and enormous knowledge about the global economy, particularly in this time of heightened financial and macroeconomic uncertainty.

Conference theme

The theme of this conference is the impact of globalisation and population trends, in particular various forms of labour mobility, on labour markets and inflation. Of course, labour has always been mobile, to a greater or lesser degree. But for a long while the macroeconomic impact of labour mobility did not seem to spill over across national borders. Countries where workers were more willing to move in search for jobs tended, other things equal, to have more flexible labour markets and lower structural unemployment. This has been the case, for instance, with the United States in the recent decades. Countries where workers were less ready to move in search of jobs, either because of their own preferences or because of the limitations on mobility resulting from welfare policies or housing markets, tended to have more rigid labour markets and labour costs. For a long time, this has been considered to be *the* major structural weakness of many European economies. In either case, the macroeconomic effects of labour mobility (or immobility) were felt locally, not globally.

Over the past decade and a half, however, we have started to experience more widespread *global* effects of labour mobility. In addition, new forms of factor mobility, such as outsourcing, cross-country commuting and the internet trade have spread. Large-scale migration of workers from rural areas of China into urban manufacturing centres; outsourcing of service tasks from the United States to India; and "commuting" by Polish and Baltic countries' service workers to western Europe are some prominent examples of labour mobility that have started to affect labour markets and prices of goods and services in both industrial countries and emerging market economies.

Major drivers of these changes seem to have been growing integration of the emerging markets such as China, India and central and eastern Europe into the global economy, and technological innovations that have significantly reduced the costs of transportation and telecommunications.

The integration of emerging market economies into global production processes has, by some estimates, effectively doubled the supply of active workers engaged in the global production of tradable goods. Together with other aspects of globalisation, this has arguably influenced labour market policies and wage setting behaviour in advanced industrial countries. At least three channels seem to have played a role in this process.

First, increased international labour mobility has helped to ease supply constraints in industrial country labour markets. This seems to have mitigated upward pressures on wages, especially for low-skilled workers. In western Europe, the average annual ratio of immigrants to population has essentially doubled since the fall of the Iron Curtain in 1989. The effect of cross-border labour mobility on wages within Europe has increased in particular since the EU enlargement in 2004, with countries that opened their domestic markets fully, such as the United Kingdom and Ireland, experiencing the largest inflows and moderating effects on wages.

Second, the relocation of production – actual or anticipated – has curtailed the bargaining power of workers and trade unions in many industrial countries. The rapid growth of trade in material inputs, such as parts and components, has been accompanied by a growing vertical integration of production processes at the global level, enabling the relocation of production from one country to another. While the effect to date has mostly been felt in the manufacturing sector, jobs in the services sectors are becoming more and more contestable internationally.

Third, the opening of markets for goods and, increasingly, services to international competition has intensified competitive pressures on producers in advanced industrial countries. The greater contestability in goods markets has forced firms that were previously dominant in the domestic market to step up their efforts to cut costs, including the costs of labour.

Increased labour mobility could have been a factor triggering the observed decline in the share of GDP that goes to wages. Since the early 1980s, wage shares in the advanced industrial economies have fallen by about 4 percentage points. This downward trend cannot be explained by cyclical factors. Statistical evidence suggests that globalisation and technological progress could have contributed to a structurally lower wage share in advanced industrial countries.

One way they could have done so is by curtailing the bargaining power of workers and, thereby, lowering the remuneration of labour relative to the remuneration of capital. A second possibility is that the global integration of goods and factor markets could have kept down the wages asked by workers in advanced industrial countries by lowering the prices of labour-intensive products increasingly imported from emerging market economies, especially in the last decade or so. Third, and as already noted, greater international labour mobility and the credible threat of relocating production might have helped to ease supply constraints in domestic labour markets.

These developments have started to affect the conduct of monetary policy. One effect, frequently noted at meetings at the BIS over the past few years, has been increased uncertainty about the state of the economy. For instance, when some indicators – activity, employment, capacity utilisation, asset prices – have been pointing to possible signs of overheating, others, such as wage developments, have remained more stable. A further source of uncertainty has been our lack of understanding of wage and price formation and the workings of labour markets in the newly globalising emerging economies.

Another effect has been the uncertainty about possible changes in the inflation process. For instance, the sensitivity of inflation to domestic slack – measured by either the output gap or the unemployment gap – is reported to have declined across a wide range of countries in the past two decades. One interpretation is that Phillips curves have flattened and that unemployment might have to rise more than in the past to reduce inflation. Another possibility is that these estimates might unduly (and spuriously) reflect recent periods of high global growth, which failed to ignite higher inflation in large part because of the big increase in the effective global labour supply. Yet another view is that Phillips curves might have become more difficult to interpret in the recent period, characterised – as it has been – by inflation expectations that have been better anchored at low levels and more credible monetary policies globally.

Overview of sessions

This conference will explore the effects of globalisation and labour market trends in three sessions and a policy panel.

For the first morning session, we will discuss a paper by Steve Nickell from Oxford University on trends and macroeconomic implications of immigration, cross-country commuting and other forms of labour mobility. In the second morning session, Jill Rubery from the University of Manchester will present her research on international migration and outsourcing, as seen through an institutional lens.

During lunchtime, Kazumasa Iwata, Deputy Governor of the Bank of Japan, who was a good friend of Palle Andersen, has kindly accepted our invitation to share his thoughts on the theme of this conference from Japan's perspective.

For the afternoon session we invited Suresh Tendulkar from the Delhi School of Economics to give us an emerging market perspective on these issues. His paper explores whether labour markets in countries such as India, China and other newly integrating economies are different from those in industrial countries and, if so, where the differences may lie.

We will conclude the conference with a policy panel on the implications of globalisation and labour markets for central banks. Governor Frederic Mishkin has kindly offered to chair this panel, which will also include Kazumasa Iwata, Assistant Governor Anders Christensen from the National Bank of Denmark, and Leif Pagrotsky, Vice Chairman of the General Council of Sveriges Riksbank.

Let me note again in concluding that Palle Andersen had a keen interest in all the issues that are on the agenda of this conference throughout his long and productive career. For a number of years he was responsible for developing the OECD's analysis of labour markets, working particularly on wage developments. He continued to do this for the BIS. From the first research papers he published at the BIS in the early 1980s, to the last one completed in early 2005, entitled "On the role of the labour share of income in the dynamics of prices and wages", a leitmotif of Palle Andersen's oeuvre was the implications of globalisation and population trends for labour markets and inflation. This is also the reason why we chose this topic to honour him at this conference.

I believe that you will have a fruitful exchange of views during the conference.