The Right to Employment: Extending the Core Labour Standards and Trade Debate

By

Sean Turnell

sturnell@efs.mq.edu.au

Abstract

Full employment is a necessary prerequisite before the gains from international trade can be specified. Yet the assumption of full employment is seldom acknowledged by economists when advancing policy advice, and nor is it made clear in the policy infrastructure of such bodies as the WTO. The purpose of this paper is to examine the importance of the assumption of full employment to the case for free trade. Arguing that the right to employment is a human right, the paper concludes that it is also a precondition for the successful creation of a rule-based trading order, and the economic basis for global stability and prosperity.

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I. Introduction

There is a fundamental distortion at the heart of 'globalisation'. A label that refers, primarily, to the greatly enhanced international mobility of goods, services and capital, coupled with accommodating advances in information technology, globalisation has yet to encompass any enhanced mobility of labour. Indeed, to the extent that industrial countries have severely restricted immigration relative to earlier periods, globalisation has coincided with the greatly reduced power of labour over market entry and exit. This is a problem. If, as its critics allege, the process of globalisation has created an international market in labour regulation that is open to arbitrage and a competitive 'race to the bottom', then labour is unable to maximise its preferences in the way orthodox economics says it can in a free market.

Consistent with such arguments a number of governments, and various non-government organisations, have sought to incorporate into trade agreements certain 'core' labour standards. In 1998 the International Labour Organisation (ILO) codified these in its 'Declaration on Fundamental Principles and Rights at Work'. The four principles established in the declaration were;

a) freedom of association and the effective recognition of the right to collective bargaining;
b) the elimination of all forms of forced and compulsory labour;
c) the effective elimination of child labour; and
d) the elimination of discrimination in respect of employment and occupation.[1]

The ILO's Fundamental Principles were elaborated from a number of United Nations conventions, but their authority was primarily derived from Article 23 of the Universal Declaration of Human Rights (UDHR). The transformation of these principles into 'core labour standards' for insertion into trade agreements is opposed by many economists, who argue that such a move simply represents a new form of protectionism hiding behind humanitarian concern. This author has argued elsewhere (Turnell 2001) that such an assessment is incorrect, especially to the extent that it has been concerned with the interests of developing countries. The adoption of core labour standards offers the possibility for the greater accumulation of human capital, increases the supply of labour by allowing greater participation, and is likely to increase foreign investment in developing countries through the promise of greater economic and social stability. For organisations such as the World Trade Organisation (WTO), the adoption of core labour standards is likely to bring greater legitimacy, helping to ensure their survival as the pillars that support the emerging liberal trading order.

Article 23 of the UDHR represents the attempt to establish basic human rights in the context of the labour market. There is another aspect to Article 23, however, that has been largely ignored, even by those who otherwise support the adoption of core labour

[1] The Declaration was adopted at the 86th Session of the General Conference of the ILO in June 1998.

standards. This aspect, in some ways the most fundamental, and critical in helping to ensure all the others, is the right to employment itself.

The purpose of this paper is to argue that this *right to employment* is not only an established human right, but is a critically important assumption in the theoretical apparatus that allows economists to argue the case for free trade. To this end, it is also a phenomenon that must be of prime concern to organisations such as the WTO, the institution charged with interpreting the abstract vision of economists into a practical blueprint for world trade.

The argument presented in the paper proceeds as follows: Section II examines the evolution of the right to employment as a human right, and the institutional arrangements it has shaped. Section III, which comprises the core theoretical component of the paper, argues the case that full employment is a necessary prerequisite before the gains from trade can be unambiguously specified. Section IV examines what practical form a commitment to full employment might take in the context of the WTO and argues that, in the Trade Policy Review Mechanism, a likely vehicle already exists to this end. Section V concludes the paper.

II. The Right to Employment

Article 23 of the UDHR, which opens with the proclamation that ‘everyone has the right to work’, was adopted by the General Assembly of the United Nations in 1948. At the dawn of the Keynesian hegemony in macroeconomic theory, it came at a time when national governments for the first time (to simplify the story only slightly) took on something akin to a general responsibility for employment. It followed a period just after the Second World War when a succession of governments issued various official statements to this effect. The first of these, the British Government’s 1944 ‘White Paper on Employment Policy’, declared that the ‘maintenance of a high and stable level of employment’ was now one the government’s ‘primary aims and responsibilities’.[2] This was closely followed by a Canadian White Paper in 1945 that declared ‘unequivocally’ that ‘a high and stable level of employment’ was ‘a major Government policy’.[3] Later that same year the Australian Government issued its own White Paper that not only accepted the government's responsibility for sustaining 'full employment', but also prescribed a particularly rigorous Keynesian approach in bringing it about.[4] In 1946 the US Congress passed the ‘Employment Act’. Though qualified to a greater extent than some of the other documents, it nevertheless acknowledged that ‘creating and maintaining…useful employment opportunities’ was to be ‘the continuing policy and *responsibility* of the Federal Government’ (emphasis added).[5]

[2] United Kingdom Parliament (1944).
[3] Canadian White Paper cited in Garrety (1978), p.230.
[4] Australia, Parliament (1945).
[5] Employment Act cited in Garrety (1978), p.231.

The international aspect of full employment, and especially its necessity if the gains from free trade were to be realised, was recognised by Keynes and a number of writers before and during this period.[6] It was also given a practical aspect in the *early* drafts of proposals to create the institutions that would shape the international economic architecture of the post-war world – the International Monetary Fund and the World Bank.

In institutional terms, however, the idea that full employment was the key to free trade was pursued with particular vigour by Australia. Australian delegations to the great international conferences concerned with post-war reconstruction even sought an international agreement on full employment - that would bind countries 'to do all in their power to maintain employment within their own territories, and thereby expand demand for internationally-traded goods'. The Australians envisaged a new international institution that would be

> able to exercise a strong influence on the policies of other international organisations and of member countries. Nations might consider giving the organisation...the duty of issuing reports upon the employment policies being pursued by members and of making recommendations.[7]

The Australian campaign made little headway until a series of conferences in 1946-47 convened to establish what would be the prototype of the WTO, the *International* Trade Organisation (ITO). Australia, by now joined in its advocacy by the United Kingdom, succeeded in establishing Article 3 of the ITO's constitution that committed members of the ITO to the recognition that 'rising effective demand...is a *condition* for the expansion of international trade and...for the realization of the purposes of the organization' (emphasis added).[8] The ITO would also contain within it a general economic review section along the lines outlined by the Australians above. In the end, however, the Australian efforts came to nought. The failure of the US Congress to ratify the ITO Charter in 1950 meant that it never came into being.

Since 1948 the observance of the right to employment in Article 23 of the UDHR has been observed mostly in the breach. The importance of the right to employment as both a human right and as a precondition for liberal free trade continues to be highlighted by a small army of writers, however, mostly from outside the mainstream of orthodox economics.[9] They emphasise that employment is a fundamental component of an individuals life: It provides the means for survival and the wherewithal through which preferences can be actualised. It is the way that individuals carve out a role in society. It is the essential component in the construction of a person's identity, social status and

[6] See, for example, Robinson (1937), Shumacher (1943) and Kalecki (1946).

[7] 'Suggested Draft of a Charter for an International Trade Organisation of the United Nations', National Archives of Australia, A1976/34/1, Box 1.

[8] The draft 'Charter of the International Trade Organisation of the United Nations' is cited from Australia, Parliament (1946).

[9] Some of the most prominent of these include Kaldor (1950 and 1984), Robinson (1973), Harcourt (1994), Milberg (1994), Prasch (1996), Shaikh (1996), Davidson (1997) and Kregel (1998).

physical and mental well-being (Burnett 1994, pp.284-295). Employment has come to represent, in short, the way in which people lay claim to an equal right of respect from others. A human right in itself, the right to employment helps ensure all of the others too.

III. The Economic Case for the Inclusion of the Right to Employment in Trade Agreements

The case for including a right to employment in trade agreements is not limited to broadly defined human rights. It is also soundly based in standard economic theory. It is for this reason that this author is of the view that the maintenance of full employment of member countries should be of concern to the WTO, the institution at the centre of efforts to create a liberal global trading order.

The reason why it is argued that countries gain from trade, and the intellectual underpinnings of the WTO's efforts to promote freer trade, is dependent upon the Ricardo-Mill theory of comparative advantage. Though it has been modified many times since its first formulation in the nineteenth century, the essential 'truth' of this model is regarded as an article of faith amongst many economists, the belief in which remains something of litmus test for entry into the profession. [10] The 1969 Nobel Laureate, Paul Samuelson, once famously argued that it was the 'one proposition in all of the social sciences which is both true and non-trivial', a quote that the WTO is happy to brandish on its website.[11] Meanwhile, a poll of economists undertaken by Ruffin and Gregory (1990) found that 97 percent of economists were convinced of the general merits of the free trade argument.[12]

The theory of comparative advantage is based upon the idea that gains from trade follow from allowing a country to specialise in production. If a country is relatively more efficient at making wine than cloth (to use the famous example first employed by Ricardo), it makes sense for it to put more resources into wine, and to export some of the wine to pay for imports of cloth. This is true even if that country is the world's *most* efficient cloth producer, since the country will have more of both cloth and wine than it would without trade. A country does not have to be the most efficient at anything to gain from trade. The gains follow from specialising in those activities which, at prevailing world prices, the country is *relatively* more efficient at, even though it may not have an absolute advantage in any of them. Because it is relative advantage that matters, no country can have a comparative advantage in producing nothing at all.

[10] As Prasch (1996, p.37) notes, the appointment of Laura Tyson to the US Council of Economic Advisors in 1993 was opposed by many economists on the basis that she had once said that 'she did not *believe* in free trade' (emphasis in original).
[11] The original quote, which came in response to a challenge from the mathematician, Stanislaw Ulam, can be found in Samuelson (1969).
[12] In his history of Neoclassical trade theory, Gomes (1990, p.vii) declares that 'economists are at their best when they speak out on international trade. On such matters, not only do they speak with the almost unanimous backing of professional opinion, but what they do convey tends to command universal respect…among the wider lay audience'!

The list of assumptions that must be satisfied if the theory of comparative advantage can be used to demonstrate these gains from trade, however, is a long one. It includes perfect competition in goods and factor markets, constant returns to scale in production, identical tastes and technologies, no externalities, free and costless factor mobility *within* countries (but none between them), fixed labour resources and technologies, trade equilibrium between countries, and *full employment of the factors of production*. It ignores levels of economic development, technological change and accumulation. Indeed, it ignores dynamics generally. As Joan Robinson observed (1973, p.14), these 'characteristics of the model exclude discussion of any question which is interesting in reality'.

It follows then, that there can be many ways in which the assumptions that underlay the theory of comparative advantage can be critiqued. The assumption of concern to this paper, however, and the only one that is the subject of its analysis, is that of full employment.[13] The paper examines the implications of the removal of this assumption by first examining the effects upon a static notion of comparative advantage and, secondly, via the effects upon standard notions of balance of payments adjustment.

Comparative Advantage

The theory of comparative advantage was formulated in order to examine the social costs of alternate modes of production in two *fully employed* economies, in order to demonstrate the case for free trade.

For the theory of comparative advantage, however, the full employment *assumption* is not a trivial one. Full employment is a requirement before the gains from trade can be unambiguously specified. Where unemployment exists, an economy is operating at below full capacity and extra production can take place at *zero* opportunity cost. In such a situation, prices no longer reflect relative scarcities within an economy. Trade between such an economy and another may not produce gains, since the 'actual trade-off or underlying rate of exchange between the production of various goods is theoretically undefined' (Prasch 1996, p.42). This is not generally recognised by economists, who typically analyse trade on the basis that each country is operating on its production possibilities frontier.

Far from being a general proposition that is generally 'true and non trivial', the theory of comparative advantage at its simplest is only applicable in very narrow circumstances. Kaldor (1984[1994], p. 62) put it succinctly thus:

> The whole classical and neo-classical conception that the opportunity to trade with abroad will necessarily benefit a country by re-allocating resources in such a way that each unit of labour will directly or indirectly make a greater contribution to national output that it did before, is a false one.

[13] For a description of some of the critiques of the other assumptions, see Milberg (1997), pp.310-312.

Adjustment Mechanisms

Closely related to the comparative advantage story is the adjustment mechanism that, in the standard model, ensures that each country achieves balanced trade. The arguments are well known, but the standard model usually tells a story along the lines that there are two countries, one of which suffers from an absolute cost disadvantage relative to the other (it may have lower productivity, higher costs, and so on). Under the standard assumptions above, and with a flexible exchange rate, the country with the cost disadvantage will see its balance of payments move towards deficit. This outward movement of funds will cause a depreciation in its exchange rate. This lowers the price (in foreign currency terms) of its exports, while simultaneously increasing the price (in domestic currency terms) of its imports. Through the depreciation of the exchange rate, the competitiveness of both the higher cost country's exports, and its import-competing industries, are improved. The process thus outlined will continue – until the imbalance between exports and imports is removed. The exchange rate has performed its equilibrating function, trade is balanced, and the opening up of this higher cost country to trade has not resulted in unemployment.

Though the mechanism is different, this smooth and costless adjustment process also occurs in the standard model if, instead of flexible rates, a fixed exchange rate regime was assumed. In this case, the initial balance of payments deficit that emerges when the higher cost country opens to trade results, not in a depreciation, but in an actual outflow of funds. Under the standard assumptions (including the propositions of the Quantity Theory of Money but also, and crucially, that of full employment), this outflow of funds will reduce the general price level in the deficit country. With the nominal exchange rate fixed, but with a falling general price level, the *real* exchange rate of the deficit country falls.[14] Just as in the case of the flexible exchange rate story, this depreciation of the real exchange rate improves the competitiveness of the deficit country's exports and its import competing industries. The trade balance improves, and must keep improving, until equilibrium between exports and imports is restored.

As with the static comparative advantage case above, however, this story of smooth and costless adjustment to equilibrium is flawed once the assumption of full employment is removed. With unemployment allowed to exist in the model, the effect of the initial trade imbalance of the higher cost country is not to bring about price changes, but changes in income (employment) and/or real interest rates. Relative prices no longer reflect relative scarcities or opportunity costs (only relevant at full employment) and there is no longer an automatic mechanism that can *costlessly* restore trade balance. The theory of comparative advantage breaks down and it even becomes possible, contra to the orthodox story, for a country to indeed produce nothing at all. Joan Robinson (1973, p.17) summed up the situation thus:

> The comforting doctrine that a country 'cannot be undersold all round' was derived from the postulate of universal full employment. The argument consists merely in assuming

[14] Of course, this story ignores Keynes's insight in Chapter 19 of *The General Theory* - that falls in prices may not be accompanied by falls in money wages. In this situation real wages, and hence the real exchange rate, will not fall.

> what it hopes to prove…There is no mechanism to make trade balance; it is merely assumed that the value of exports is equal to the value of imports.

The lack of smooth adjustment is not the end of it, however, for the removal of the full employment assumption provides for the propagation of aggregate demand failure generally. Take, for example, under a fixed exchange rate regime, the situation in which there is a fall in income and employment in a particular country. This will tend to reduce its imports relative to its exports and, all other things being equal, will generate a surplus in its balance of payments. By contrast in the rest of the world, and clearly the magnitudes will depend on the size of the 'depressed' country, balance of payments deficits will emerge.

Now, with the full employment assumption in place, this was not a problem. Through the automatic adjustment mechanism of changes to the real exchange rate, the rest of the world is protected from the failure of demand in the depressed country. The composition of overall production (in all economies) might change, but the volumes of income and employment will not.

But with the removal of the full employment assumption, this automatic mechanism no longer applies. The process of 'deflation' in the rest of the world results not in a fall of the general price level, but in changes to income and employment – directly in export sectors, and subsequently to economies generally through multiplied contractions in investment and domestic spending. Any movement towards balance of payments adjustment in this process occurs only through the induced falls in imports that are a function of the falls in income. The trouble is that this process is itself cumulative – since reductions in imports will be occurring everywhere, compromising further the ability of other countries to maintain full employment and resulting in a reduction in the volume of international trade.

The situation is no better under a flexible exchange rate regime. Here the balance of payments deficits that threaten to emerge are meant to be rectified through changes in nominal exchange rates. Now for any one country this should restore trade balance under the traditional assumptions. But in *this* scenario, in which all but the depressed country's exchange rates are depreciating, who is buying the (now cheaper) exports? It cannot be the initially 'non-depressed' countries, since *between* each of these relative prices are unchanged. The source of demand for the increased exports of the rest of the world required to restore the balance of trade must come from the depressed country. But this is a country at less than full employment, and whose exchange rate has increased relative to the rest of the world. Bearing upon its actions in this context then will not only be the effects of changes to relative prices, but the negative effects of all of this upon its *income*. What is missing from the orthodox story with the assumption of full employment removed, under this scenario, is an inability to account for this combination of price and *income* effects. All would depend upon the relative price and *income* elasticities of the exports of both the depressed economy and the rest of the world. Thomas Balogh, writing in 1944, noted that:

> The effects on the demand for any one country's produce of a fall in price are highly conjectural. They will depend on the reactions of competitors in other countries and also on the state of expectations in each of the countries which...are inter-connected. *All countries may well sink and rise together without their international balance, in distinction to the volume of total trade, altering in a significant manner* (Balogh 1944, p.139, emphasis added).

A variant of all of the above emerges in the 'real world' when countries seek to use trade – export led growth – as an *alternative* to maintaining domestic full employment through domestic measures. Hostility to budget deficits and a predilection for notions of 'sound finance' (often exacerbated by highly mobile financial capital) has meant that such a policy has often been resorted to and, somewhat bizarrely, has often been applauded by economists.[15] As Keynes noted in 1936, a favourable trade balance will indeed work just as well as domestic public investment as a device for stimulating demand and employment. It has, however, the very considerable downside that it is 'liable to involve an equal disadvantage to some other country', and the pursuit of such a policy by nations generally 'injures all alike' (Keynes 1936, pp.338-339).

IV. Monitoring Full Employment via the WTO

Establishing the merits of full employment via the theoretical case for free trade, or on the basis of its consistency in human rights, is a problem altogether different from creating the international machinery that, in practice, can help ensure its achievement. Unlike the 'core' labour standards examined earlier in this paper, the right to employment is not such that it can be policed via the traditional methods through which countries breaching trade rules are sanctioned. The right to employment remains enshrined in all sorts of treaties yet, as Burgess and Mitchell (1998) note, it is unlikely that 'it will (beyond platitudes) be accorded the status of an internationally enforceable obligation'.

There exists within the WTO, however, a mechanism through which full employment, and other labour causes, could realistically be brought into international consideration.

The 'Trade Policy Review Mechanism' (TPRM) was established in 1988 as a result of the Uruguay Round of the General Agreement on Tariffs and Trade (GATT). Subsequently and permanently established as a key component of the WTO, the objective of the TPRM is to review member countries' 'trade policies and practices and their impact on the functioning of the multilateral trading system'.[16] The reviews are carried out by the WTO Secretariat, whose report is subsequently sent to the WTO General Council (which consists of the full membership of the WTO). In this way, the WTO asserts, the TPRM is essentially peer-group assessment. Though all WTO members are

[15] To wit, the now somewhat muted praise regularly handed out to Japan and the Asian 'tigers'. An interesting counter to this adulation, before being a critic was fashionable, can be found in Kriesler and Halevi (1995).
[16] Details of the TPRM can be found at the WTO's website, <www.wto.org>.

subject to review under the TPRM, the regularity of review is determined by their share of world trade. The top four members are subject to review every two years, the next 16 are reviewed every four years, while the remainder are reviewed every six years.[17] The TPRM does not hand out 'punishments', and nor can it be used for the enforcement of specific obligations or to settle disputes.

Mehmet *et al* (1999, p.202) argue, in the context of *core* labour standards and trade, that the TPRM provides 'a constructive and non-confrontational way' through which institutional links can be established between social issues and trade. They maintain that the integration of labour market policies into the review process could highlight the way such policies impact upon trade patterns and, in so doing, could expose disguised protectionist devices and unfair practices. Introducing labour issues into the TPRM could help avoid the 'aggressive unilateralism' of some nations in pursuing social goals and could provide a vehicle through which the linkages between social issues and trade could be further explored. Above all, they argue, introducing labour issues into the TPRM could expose emerging problems in international economic relations, before they are allowed to escalate into trade disputes.

Incorporating an examination of aggregate employment levels in the TPRM process is at least as defensible as using it as a device to take up the issue of core standards. The growing disparities between the relative performances of the major trading countries on employment, and the enormous current account imbalances that have opened up as a result, pose a grave threat over the long-term survivability of the emerging liberal trading order. While there has been much talk in recent years about macroeconomic policy co-ordination, little of substance has been achieved.[18] Tinkering around the edges of policy co-ordination via exchange rate interventions, regulatory convergence and reforms of the world payments system fails to address the central problem – which, as Grieve-Smith observed (1995, p.290), 'is not so much to get everyone marching in step, as to ensure that we are all at least going in the same direction'.

The purpose of the WTO, in the words of the Final Act of the Uruguay Round that established it, is to contribute to 'the expansion of trade, sustainable growth and development, and the timely correction of external imbalances'. Thus far the WTO has directed its efforts towards the elimination of tariffs and other discriminatory barriers to trade. This is all well and good, but it is blind to the main game. Barriers to trade are, under the very narrow assumptions of standard theory outline here, unquestionably inefficient. Their impact upon global welfare, however, is dwarfed by a much greater inefficiency – an inefficiency that arises from daily condemning millions of people to

[17] The WTO may allow a longer period between reviews for members adjudged 'least-developed'. Since the European Community (EC) is classified as a single member of the WTO, the current top four is the EC, the United States, Japan and Canada.

[18] There have been numerous attempts at policy cooperation over the past two decades, most concerned with manipulating exchange rates in the attempt to redress the problems associated with the large and persistent trade imbalances between the United States and Japan. The usual outcome of such attempts (such as the Plaza and Louvre Accords of 1985 and 1987) has been some short-term movement in exchange rates, with the larger issue remaining unresolved. For more on the problems and prospects and problems of policy co-ordination generally, see Bryant (1995).

enforced idleness. There appears to be a complacency at the heart of our global economic institutions to unemployment. It is a complacency that is eroding their legitimacy. Tackling the question of a right to employment via the TPRM process is not yet the answer to the most chronic problem of the global macroeconomy. It is, however, a beginning in that at least provides a forum in which the right question can be asked.

V. Conclusion

The right to employment is an established human right and its manifestation is a requirement for the gains from trade. As such, it is appropriate that the WTO monitors and, where necessary, encourages, policies designed to promote full employment amongst its member countries. Including what will inevitably be seen as a 'social clause' into the charter of the WTO will be controversial but, in the Trade Policy Review Mechanism, the means exists such that it could be done with the minimum of offence to orthodox sensibilities. By creating a forum in which the most intractable international economic tensions can be explored without prejudice, it might even go some way to making a more favourable world for the creation of a liberal trading order from which all, rather than merely a few, can benefit.

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