

## CHAPTER 31

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# LATIN AMERICAN LABOR REFORMS: EVALUATING RISK AND SECURITY

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## 31.1 INTRODUCTION

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This chapter addresses procedural and substantive changes to Latin American employment law in the late 20th and early 21st centuries. It covers eighteen Latin American market economies between 1985 and 2009 and pays particularly careful attention to reforms undertaken in the 2000s in light of their variegated—and somewhat anomalous—predecessors. While Latin American policymakers responded to the debt crisis by liberalizing their trade regimes, credit markets, and capital accounts in the 1980s and 1990s, they were reluctant to deregulate their labor markets—and in a number of well-known cases actually adopted *new* regulations designed to protect workers or appease their political representatives (Lora and Panizza 2003: 127; Pagés 2004: 67; Singh et al. 2005: 17–18). The existing literature therefore holds that the relationship between international competition and labor market reform is mediated by domestic politics, in general, and by the partisan loyalties of governing parties, in particular (Madrid 2003; Murillo and Schrank 2005; Cook 2007). In fact, Murillo (2005) concludes that traditionally populist or labor-backed parties and politicians who courted big business with promises of “pro-market” trade, investment, and commercial policies in the late 20th century simultaneously mollified their core constituents in the labor movement by *re-dedicating* themselves to labor market regulation.

Are her findings relevant today? Do partisan loyalties continue to influence the region’s labor and employment laws? And, if so, how? We begin to address these questions by documenting and accounting for the principal reforms to the laws and practices that were designed to protect Latin American workers from the risks incurred

by unemployment in the late 20th and early 21st centuries. We begin by assessing recent reforms to: (i) laws that are designed to reduce the *likelihood* of job loss by limiting the employer's authority to dismiss his or her workers (i.e. "external flexibility"); and (ii) laws that are designed to influence the *compensation* workers receive in case of job loss by creating or reinforcing either (a) unemployment insurance programs or (b) severance payments.<sup>1</sup> We proceed to address the question of enforcement by examining the evolution of resources devoted to labor inspection across the region. And we conclude by discussing the theoretical implications of our findings.

## 31.2 HISTORICAL ANALYSIS

The canonical western European literature on labor market regulation assumes the existence of income replacement schemes that pool the risk of unemployment across workers. Neither the Iberian countries (Bonoli 2003) nor their New World offspring (Schrank 2009a) adopted risk pooling, however, and the Western European literature is therefore broadly inapplicable to Latin America. Instead, Latin American labor codes obliged employers to compensate their former employees with experience-rated severance payments—and thereby limited risk pooling to the level of the enterprise.<sup>2</sup> The implications are decidedly important. While severance payments are designed to mitigate the cost of job loss, and thereby provide an alternative to social insurance in theory, they tend to raise the cost of hiring and firing for individual employers and have ambiguous results in practice—especially with regard to coverage of informal workers.

Experts have recently advised Latin American policymakers to abandon their "labor market-based" (Bonoli 2003: 1008) systems of social protection for a northern European alternative. They are particularly enthusiastic about the Danish "flexicurity" model (Haagh 2006; Tokman 2007a; Cohen and Sabel 2009) which allegedly reconciles efficiency with social protection by combining a low level of employment protection (i.e. flexibility) with a high level of unemployment insurance (i.e. security). But they nonetheless worry that flexicurity presupposes levels of taxation, formalization, and social dialogue that are at best unusual—and at worst unavailable—in Latin America (Tokman 2007a: 102; CEPAL 2008: 54–5).

<sup>1</sup> We ignore labor reforms that do not directly modify the cost of hiring, employing, or firing a worker, or the benefits workers receive in case of unemployment. This restriction implies that we do not analyze reforms affecting collective bargaining, union rights, or labor inspection. Certainly, these reforms can affect working conditions, e.g. via collective agreements. However, whether they produce more or less flexibility/security depends on several factors such as the degree of union democracy and labor's political alignments. We also ignore social policies that provide non-contributory benefits to unemployed workers such as *Progresas/Oportunidades* in Mexico, or *Jefes de Hogar* in Argentina.

<sup>2</sup> A number of scholars have attributed the limited redistribution of the risk of unemployment to the weakness of Latin American states and their inability to provide more comprehensive social insurance schemes. See e.g. Mares (2005) and Schrank (2009a).

Are Latin American policymakers defending labor market-based systems of social protection, moving toward flexicurity, or pursuing alternative strategies? We address these questions by defining three different indicators of the character of labor market regulation in the region: external flexibility; unemployment insurance; and personal compensation for the risk of job loss.

- Our indicator of “external flexibility” assesses the extent to which the regulation of the individual employment contract—and severance payments in particular—increases the cost of hiring and firing. A decrease in the value of severance payments (or limits on their use) is assumed to increase external flexibility and vice versa.
- Our indicator of “unemployment insurance” assesses the extent to which the government pools the cost of income replacement by means of taxation that redistributes income across work categories (or even the general budget) and thereby mitigates the cost of job loss without increasing the cost of hiring and firing. The initiation or augmentation of a social insurance scheme constitutes an increase in unemployment insurance and vice versa.
- Our indicator of “personal compensation” is a composite variable that increases when individual compensation for the risk of job loss increases either due to increased severance payments or expanded unemployment insurance. The indicator therefore recognizes that both schemes provide employed workers compensation for the risk of job loss, and in so doing affect their propensity to invest in skills that may affect the productivity of their firms.

We will eventually create and deploy ordinal variables that code increases in each indicator as “1,” decreases as “-1,” and stasis as “0.” But first we will discuss the historical underpinnings of the three indicators and their evolution in the region over time.

### 31.3.1 External flexibility

Latin American labor codes are notoriously complicated pieces of legislation. According to Heckman and Pagés (2003: 10), the region’s “labor codes determine the types of contracts, the lengths of trial periods, and the conditions of part-time work” available. They tend to give full-time, indefinite contracts pride of place over part-time, temporary contracts. They frequently stipulate when and how an employer can dismiss his or her workers. And they almost invariably mandate the payment of severance upon the dismissal of workers on standard contracts. In short, Latin American labor codes have traditionally substituted a labor-market based system of social protection for northern European-style social insurance.

#### 31.3.1.1 *Normative changes 1985–1999*

By the time Heckman and Pagés had published their analysis of Latin American labor and employment law, however, the region’s labor codes had been subject to a number

of different reform campaigns. Labor market reform was part of a larger reform agenda that included trade, price, and capital account liberalization, deregulation, privatization, and similar reforms designed to foster market competition and the exploitation of globalization. While the international financial institutions and their local supporters portrayed labor market regulation as a threat to the region's competitive advantage, and therefore joined forces in support of deregulation in the 1980s and 1990s, they were ultimately disappointed by reforms that fell short of their expectations in terms of pace, scope, and content (Weller 2001; Heckman and Pagés 2003)—and at times actually increased, rather than decreased, the scope of worker protection (Pagés 2004: 67). The first wave of labor market reform nevertheless provides a necessary introduction to the wave that would follow in the post-2000 period, and we therefore describe it briefly in Table 31.1 by country, year of the reform, and outcome, i.e. whether the reform increased or decreased external flexibility for hiring and firing.<sup>3</sup>

Labor market reforms have frequently been invoked to demonstrate the continued importance of partisan politics in late 20th-century Latin America. After all, the aforementioned reforms occurred during the halcyon days of the Washington Consensus (1985–99), when the external constraints imposed by the debt crisis of the 1980s were apparently at their peak, and were nonetheless limited in scope, inconsistent in direction, and better predicted by the ideologies of their political architects than by the presence or intensity of external constraints (Murillo 2005).

### 31.3.1.2 *Normative changes since 2000*

Did the same logic hold in the first decade of the new millennium? The incentives to adopt pro-market reforms have, if anything, declined since the turn of the century, when the net transfer of resources from Latin America to the rest of the world once again turned negative in 1999 and 2000 and the bloom wore off the free market rose more generally. While Latin American policymakers were by no means invulnerable to the influence of international markets and creditors in the first decade of the 21st century, they were in all likelihood more autonomous—and more likely to impose limits on external flexibility—than they were in the free market 1990s, and we therefore expect our review of normative changes to Latin American labor regulation in the new millennium to expose policy reversals and the revival of labor market-based systems of social protection.

In short, Latin American labor reforms have been inconsistent in nature. The region's policymakers not only increased but at times decreased external flexibility in both the late 20th and the early 21st centuries. While policymakers apparently had a slight preference for flexibility in the former period, they exhibited a modest tendency toward policy reversal in the latter. The big story, however, is that cross-country variation in labor market reform is greater within than between periods—a finding that would appear to distinguish labor market reform from reform in other issue areas.

<sup>3</sup> See Vega Ruiz (2005) for a more extensive analysis of the first wave of labor market reform.

**Table 31.1 Reforms to procedures affecting external flexibility, 1985–1999**

Country	Year	External flexibility	Effect
Argentina	1991	Reduction in severance pay. CDD (part-time contracts and apprenticeship contracts) for new activities and youth; duration up to 5 years with union agreement through collective bargaining.	↑
	1995	CDD for small and medium companies.	↑
	1998	Cancelled CDD, limited apprenticeships, and reduced probationary period.	↓
Brazil	1988	Increased severance payments.	↓
	1998	CDD 2 years; no warning period for dismissal.	↑
Chile	1990	Employers must show cause to dismiss employees or pay higher severance.	↓
Colombia	1990	CDD 3 years + conditions to end CDI. Reduction in severance payment.	↑
Dom. Rep.	1992	Increased compensation for dismissal.	↓
Ecuador	1991	CDD 1 year minimum except for occasional employment. But increased severance.	↑
El Salvador	1994	Increased severance pay; eliminated women's right to return to same job after pregnancy; allowed hiring of 12-year-olds if it did not affect school or health.	↓
Guatemala	1992	Abolished the reinstatement of workers fired without just cause.	↑
Nicaragua	1990a	Dismissal only under a list of just causes.	↓
	1990b	New firing procedures reversing prior reform.	↑
	1996	Increased severance pay; allowed collective dismissal for economic reasons; and allowed reinstatement or higher severance for unjust individual dismissal—mixed but overall reduction in flexibility (Heckman and Pages 2003; Gamboa et al. 2007).	↓
Panama	1986	Increased duration of the probationary period (2 weeks to 3 months) with lower dismissal cost.	↑
	1995	CDD 2 years, collective dismissal for reduction in economic activity.	↑
Peru	1986	Reduction in probationary period (3 years to 3 months).	↓
	1991	Apprenticeships allowed until 25 years of age; CDD up to 5 years for up to 10% of payroll; dismissal without reason; mass layoffs with economic and technological objectives.	↑
	1994	Allowed subcontracting for up to 30% of company employees.	↑
	1996	Increased severance payment.	↓
Venezuela	1990	Limited firing and increased compensation for dismissal.	↓
	1997	Reduced severance payments and established private accounts for capitalization of severance payments.	↑

**Table 31.2 Reforms to procedures affecting external flexibility, 2000–2010**

Country	Year	External flexibility	Effect
Argentina	2000	Increased length of the probationary period.	↑
	2002	Eliminated "unjustified firing"; transitional increase of severance payment to two times their value.	↓
	2004	Extended the transitory increase in severance payments as long as unemployment is above 10%.	↓
	2004	Reduced length of probationary period; increased minimum severance payment.	↓
Bolivia	2006	Established the right of workers to continue working rather than accept dismissal in case of "unjustified firing."	↓
	2009	Granted severance payment to all employees with more than 90 days tenure.	↓
Chile	2002	Increase severance payments.	↓
Colombia	2002	Reduced severance payments; eased use of apprenticeship contracts.	↑
Ecuador	2000	No severance payment in new category of work by the hour ( <i>Trole 1</i> ).	↑
	2000	Reduced severance payments and introduced temporary contacts ( <i>Trole 2</i> ).	↑
	2000	Declared <i>Trole 2</i> unconstitutional.	↓
	2008	Eliminated <i>Trole 1</i> and eliminated subcontracting.	↓
Panama	2002	Established lower cost of dismissal if firms hired young workers.	↑
Paraguay	2002	Established lower cost of dismissal if firms hired young workers.	↑

### 31.3.1.3 Unemployment insurance

The aforementioned reforms addressed external flexibility. Advocates of flexibility maintained that reforms would foster the growth of formal-sector employment by lowering the cost of job creation, unleashing comparative advantage, and undercutting the basis of informality. While their primary goal was to minimize the likelihood or *risk* of unemployment, they simultaneously altered the size and availability of severance payments and thereby influenced the perceived *cost* of job loss as well. We therefore compliment our analysis of external flexibility by examining normative changes that influence income security: first, by examining policies that provide an alternative to labor market-based systems of social protection by pooling risks in the form of unemployment insurance; and second, by exploring the combined effects of reforms that affect external flexibility and the level or availability of unemployment insurance to see whether the flexicurity model—or something like it—has taken hold in Latin America. That is, by focusing on the compensation for unemployment risk that workers receive from different sources, we can assess the impact of such compensation on workers' incentives.

### 31.3.1.4 Normative changes 1985–2000

Only seven Latin American countries have established unemployment insurance as a form of social insurance to pool the risk of unemployment across different types of workers: Argentina, Brazil, Chile, Colombia, Ecuador, Uruguay, and Venezuela. In all seven countries, these systems are characterized by:

- Low reciprocity rates. Because benefits are largely limited to workers who were employed in the formal sector, only 5–15% of the unemployed population in the aforementioned seven countries actually receive benefits (Jaramillo and Saavedra 2005).
- Low benefit replacement rates. Benefits are usually between 40% and 60% of a worker's former wage, and in some cases (i.e. pre-reform Chile and Colombia) they are lower than that level (IDB 2000).
- Poor monitoring. Benefits often go to persons who are currently employed or not actively seeking work (Vroman and Brusentsev 2005).

How did these systems evolve in the late 20th century? Did unemployment insurance compensate workers for diminished employment protection in liberalizing countries? Or did it follow a different logic?

In Brazil, the *Decreto-ley* No. 2283 (1986) introduced unemployment insurance in addition to advanced notice procedures, access to the *Fundo de Garantia de Tempo de Serviço* (FGTS), and a 40% (of the worker's individual account) fine for unfair dismissal. A major reform took place in 1990, when a large development fund called the *Fundo do Amparo ao Trabalhador* (FAT) was created. The program was placed on a more secure financial basis, underwent broader administrative and operational changes, and expanded eligibility to a wider range of workers (Mazza 1999). The unemployment compensation program offers partial coverage for up to four months of unemployment—extended to five months after 1996 (Amadeo, Gill, and Neri 2000).

In 1991, unemployment insurance was introduced in Argentina. To qualify for benefits, a worker must have contributed social security payments for at least twelve months during the three years prior to the termination of employment and must be legally unemployed, i.e. as a result of being fired without just cause or the expiration of an employment contract. The term of insurance ranges from four to twelve months, depending on the length of the contribution period, and the benefit depends on the duration of unemployment and on the monthly salary during the prior period of employment (Hopenhayn and Nicolini 1997).

In 1989, Venezuela enacted an unemployment insurance system similar to the one described in Argentina (Decree No. 449). But according to the IDB (2004) it was never implemented. The system was reformed in 1999, but again it was never implemented.

In short, Latin America has recently played host to a series of tentative experiments with the creation of European-style systems of social insurance that pool the risk of unemployment across—rather than within—firms. While the new insurance schemes differ markedly from the labor market-based systems of social protection that emerged in the postwar

period, they cover a relatively small percentage of the workforce in a minority of the region's polities, and therefore fail to constitute a decisive break with the past. In fact, Latin American policymakers may have unintentionally bolstered support for the pre-existing personal insurance systems based on severance payments by implementing unemployment insurance in a timid manner in the late 20th century. If reasonable levels of unemployment insurance had instead been made available to the bulk of the Latin American workforce, European-style social protection would in all likelihood have been a more attractive alternative to the segmented welfare states that continue to dominate the region.

### 31.3.1.5 *Normative changes since 2000*

Latin American policymakers allegedly adopted their original (and timid) unemployment insurance (UI) schemes in an effort to compensate for the decrease in personal security engendered by the growth of external flexibility in the 1980s and 1990s. We might therefore expect either (i) the retrenchment of UI and the revival of severance payments or (ii) the expansion of UI in conjunction with other types of social provision (e.g. social security, conditional cash transfers) in the aftermath of the free market revolution, and we are therefore agnostic with regard to the direction of UI reform in the new millennium.

We ultimately observe little reform to unemployment insurance since 2000. Only Chile and Colombia have made meaningful reforms in this area. Chilean Law 19,728 (2001) creates a new UI system. It was implemented in October 2002 and created a mixed program with two types of funding mechanisms: an individual savings account for each worker, and a contingency fund called the "Solidarity Fund." Contributing workers are entitled to one monthly payment for every twelve months of contributions to the fund, and the amount of the payment is a function of the accumulated funds. If the accumulated savings in the individual account are insufficient, however, the worker has the right to receive a subsidy from the Solidarity Fund (IDB 2004).

The previous system was non-contributory with low benefits (between \$12 and \$25 per month) for twelve months (Acevedo, Eskenazi, and Pagés 2006). By way of contrast, the new program is financed by the government, employers, and employees; and the government has agreed to spend the equivalent of its expenditure on the previous unemployment subsidy on the Solidarity Fund. The employer pays 0.8% of each employee's monthly wage into this fund as well as 1.6% of wages into an individual account set up for each employee (similar to a pension account). The worker contributes 0.6% of his or her monthly wage to his or her individual account (Sehnbruch 2004), and a single private firm administers all of the individual accounts. Contributions are compulsory for all permanent jobs that started after 2002, and voluntary for holders of previous jobs. Workers with temporary jobs do not participate in the system.

Law No. 789 (2002) creates *auxilios al desempleo* (unemployment aid) in Colombia. This program gives unemployed workers 25% of the minimum wage for six months. The program is primarily financed by formal workers' contributions, and part of the funding is used to provide transitory assistance to informal workers (Gaviria and del Mar Palau 2006). This program is considered "timid" (Reyes Posada 2007), and the government is currently attempting a major change.

### 31.3.2 Reforms in Latin America and “flexicurity”

We have already established that Latin America took rather modest steps toward the provision of unemployment insurance between 1985 and 2009, and that all but two of the experiments with UI were established in the 1990s. We are agnostic, however, on the rationale for UI provision. Were Latin American policymakers trying to establish a variant of the flexicurity model by increasing external flexibility and UI more or less simultaneously? Or were different motivations in action? We begin to address the question by adopting a composite indicator that tracks reductions in the *cost* of job loss attributable to either (i) the establishment of unemployment insurance systems that pool risks across firms or (ii) the reinforcement of traditional severance payment schemes that pool risks within firms. Reforms that augment the benefits workers receive upon dismissal—whether by means of UI or severance payments—are categorized as increasing “personal compensation.” While reforms that increase external flexibility and personal security simultaneously are compatible with flexicurity in theory, reforms that increase external flexibility and decrease personal security underscore Louise Haagh’s sense that “security and flexibility are considered bed-fellows in Europe and trade-offs in emergent economies” (Haagh 2006: 389).

Our composite indicator of “personal security” is more than simply the inverse of our indicator of external flexibility for two reasons. First, not all reforms that increase external flexibility have a negative effect on “personal security.” Regulatory changes that affect the ease of hiring and firing but leave severance payments untouched (e.g. the reform that imposed limits on unfair dismissal in Nicaragua in 1990) constitute the primary exceptions. Second, “personal compensation” is influenced by the extent and level of benefits derived from *either* unemployment insurance *or* severance payments. Although reforms that reduce severance payments but establish unemployment insurance payments have mixed effects, we have coded them as reductions in “personal compensation,” because severance payments provided larger benefits and covered a broader section of the workforce than unemployment insurance in all of the cases we examined. In fact, we have not found a single country that has successfully compensated for the decline in severance payments by increasing the scale and scope of unemployment insurance, thereby reflecting a movement in the direction of flexicurity. Although the reforms in Argentina in 1991 and in Colombia in 2002 reduced severance payments and increased unemployment insurance, in neither case was the UI able to compensate for the decline in severance.

## 31.4 PATTERNS OF LABOR REFORM

The following figures summarize the general patterns of reform associated with the three indicators between 1985 and 2009. We lack confidence in cross-national comparisons of interval measures, and the analysis is therefore based on the direction of the reforms alone (i.e. whether they increase or decrease external flexibility, unemployment insurance, and personal compensation). Figures 31.1(a) and (b) describe the number of

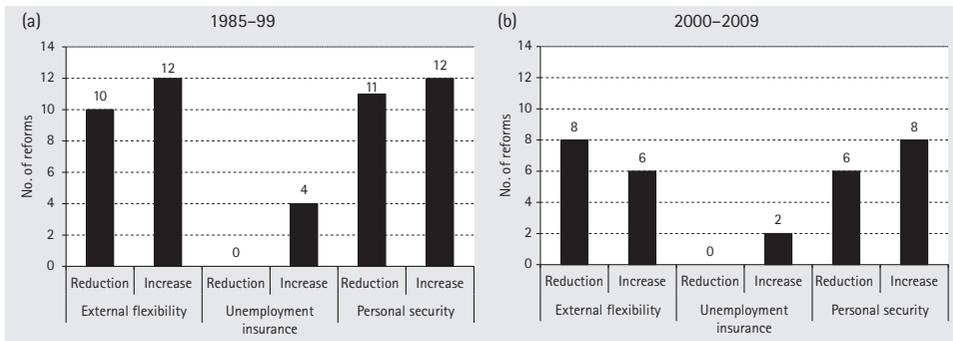


FIGURE 31.1 Number of reforms: Latin America, 1985–2009

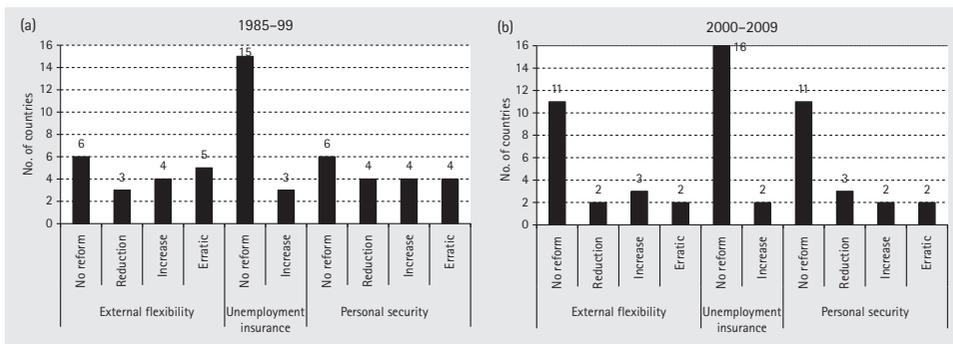


FIGURE 31.2 Number of Countries implementing reforms: Latin America, 1985–2009

reforms implemented in Latin America that affected external flexibility, UI, and personal compensation in each of two sub-periods (1985–99 and 2000–2009). The size of the column reflects the number of reforms. For example, the first column in Figure 31.1(a) is equal to 10, meaning that ten reforms reducing external flexibility were implemented in Latin America between 1985 and 1999.

While the total number of reforms was slightly smaller in the second sub-period, the second sub-period was also shorter, and the overall probability of reform therefore remained more or less unchanged over time. Nor do we observe a large change in the direction of reforms. We observe more reforms aimed at reducing external flexibility in the 2000s while the opposite occurred in the 1980s and 1990s, but the differences are again quite small and therefore difficult to interpret. Most reforms affect external flexibility (employment law), and very few affect unemployment insurance in either subperiod.

Figures 31.2(a) and 31.2(b) compare both periods using the country as a unit of analysis. Some interesting facts emerge. First, we observe that while most countries in the region implemented reforms affecting external flexibility between 1985 and 1999 (12 out of 18 countries), only 7 countries implemented reforms in this area in the 2000s. The difference between Figures 31.1(b) and 31.2(b) is due to the fact that a few countries,

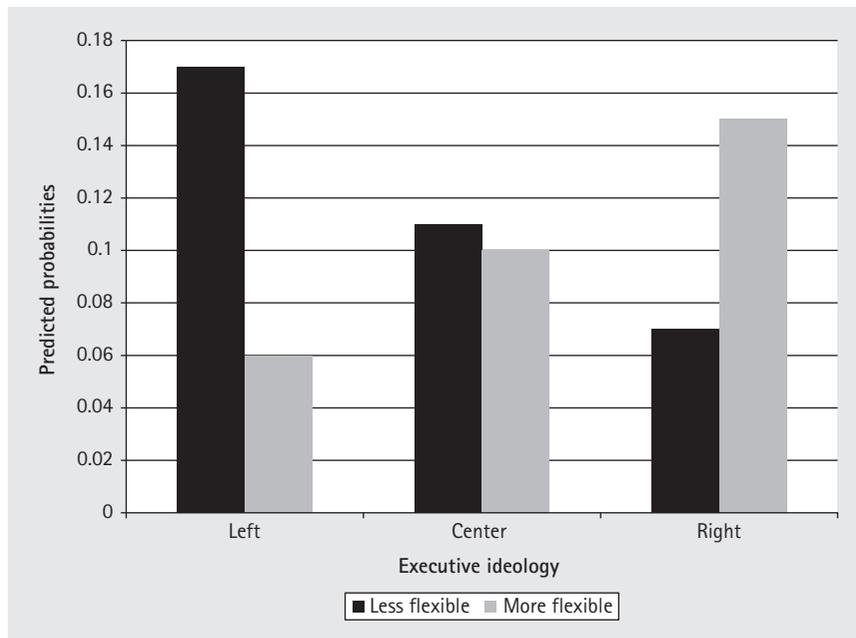
namely Argentina, Bolivia, and Ecuador, implemented several reforms in the 2000s and were thus responsible for a disproportionate share of the reform in the former figure. Second, it is worth noting that several countries implemented offsetting reforms during both periods. This “erratic” behavior is observed in Argentina (both periods), Brazil (1985–99), Ecuador (2000–2008), Nicaragua (1985–99), Peru (1985–99), and Venezuela (1985–99).

An analysis of the whole period (1985–2009) shows that most countries (14 out of 18) introduced at least one reform affecting either external flexibility or unemployment insurance. Only Costa Rica, Honduras, Mexico, and Uruguay failed to introduce any reforms at all. The following patterns emerge from this analysis:

- There are clearly more reforms to employment law than to unemployment insurance (i.e. only seven countries have insurance, while every country provides employment protection). Reforms adopted in the 1980s and 1990s were slightly more likely to increase external flexibility, while reforms adopted during 2000–2009 were slightly more likely to reduce flexibility. However, since 2002 all employment law reforms have been aimed at reducing external flexibility.
- Several countries that adopted pro-flexibility reforms in the 1990s did not reverse those laws (e.g. Brazil, Colombia, Guatemala, and Panama); however, Ecuador and Peru recently introduced employment protection reforms.
- Chile, Colombia, and Panama present a very consistent behavior over time. Chile introduced several reforms that bolstered employment protection, while the other two countries consistently moved towards greater external flexibility. By contrast, Argentina, Ecuador, Peru, and Venezuela exhibit very erratic behavior.
- Argentina (1991) and Colombia (2002) are the only countries to increase external flexibility and UI simultaneously. But it is hard to argue that they are getting closer to the Danish model given the limited coverage of their UI systems. Nor are they alone. Very few Latin American countries provide unemployment insurance, and those that have established UI limit benefits to about 10% of the unemployed population. Considering the extent of coverage in northern European countries, it is worth underscoring the fact that no country in Latin America is even close to embracing the flexicurity model.

### 31.4.1 Political and economic determinants of labor reforms

What accounts for the pattern of labor law reform in Latin America between 1985 and 2009? While the literature on economic reform underscores the role of external financial pressures, and would therefore have predicted divergence between the late 20th and the early 21st centuries, we find only small differences between the two sub-periods. More generally, we find that variation across countries—and even contradictory patterns within countries—trump longitudinal variation between periods in



**FIGURE 31.3** External flexibility by executive ideology

*Notes:* The unit of analysis is a presidential administration. The sample includes the 108 administrations found in Latin America since 1985; however, administrations that failed to pursue reform (i.e., “no net change”) are excluded from the figure. Codings by authors. Ordered logistic regression coefficient = .48; robust standard error = .27;  $z = 1.81$  ( $p = .071$ ); full results available from authors on request.

size and importance. In order to explain these patterns, we follow the prior work of Murillo (2005), who finds that the partisan ideology of the executive is a decidedly more powerful predictor of reform than economic variables like openness to trade and inflation.

### 31.4.2 The politics of employment protection

We initially extend Murillo’s findings by examining the relationship between executive ideology and patterns of employment law reform across the 108 presidential administrations found in Latin America since 1985. We expect that right-of-center governments are more likely to liberalize their labor markets and left-of-center governments are more likely to augment employment protection. The administrations that constitute our units of analysis are therefore coded on: (i) an ordinal scale from “left” (–1) to “right” (1), with “center” in between (based on an updated version of Coppedge’s codings); and (ii) a similar scale from “less flexible” (–1), if their labor markets were less (externally) flexible when they came to a close than when they began, to “more flexible” (1), if their labor markets were more (externally) flexible when they came to a close than when they began,

with “no net change” (o) in between (based on our own analysis of data described in section 31.3). We then analyzed the impact of government ideology on the predicted probability of reform in either direction, derived from an ordered logistic regression of the reform scale on the executive ideology scale. Figure 31.3 provides a graphical representation of our findings.

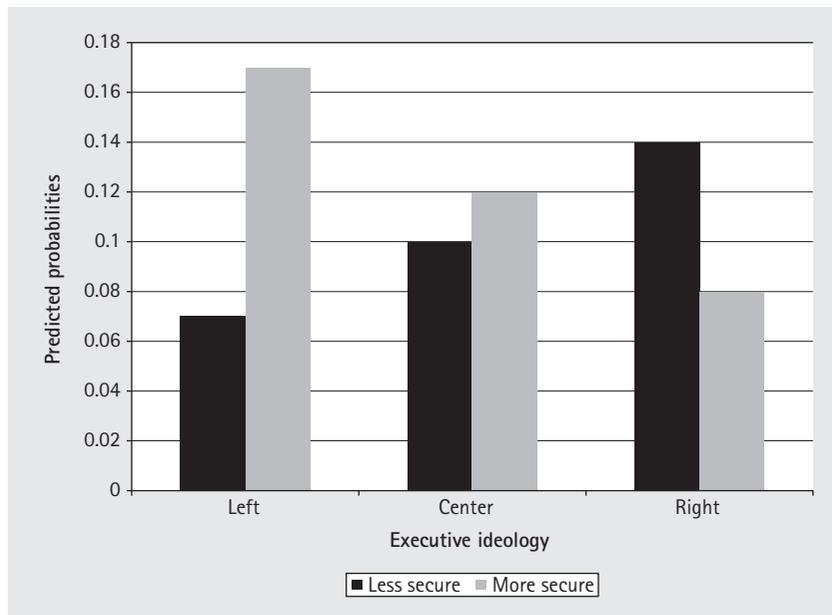
The results indicate that partisan ideology is indeed a powerful predictor of reform. Right of center governments are substantially more likely to liberalize, and less likely to regulate, their labor markets than their left-of-center counterparts. Non-reform is the modal category and is left off the figure.

Furthermore, the results become, if anything, more powerful when we limit our analysis to the post-1999 period—perhaps due in part to the decline of external pressures, improvement in the region’s terms of trade, and the corresponding growth of policy autonomy (Murillo, Oliveros, and Vaishnav 2008). Only eight administrations made net changes to external flexibility in the current decade: flexibility was augmented by the right-leaning governments of Noboa in Ecuador, Moscoso in Panama, González Macchi in Paraguay, and Uribe in Colombia; and flexibility was limited by the left-leaning administrations of Nestor Kirchner in Argentina, Morales in Bolivia, Lagos in Chile, and Correa in Ecuador. Thus, executive ideology all but perfectly predicts the direction of reform in the post-1999 period.

### 31.4.3 The politics of unemployment insurance

The politics of unemployment insurance are much harder to discern. Only five countries—Argentina, Brazil, Chile, Colombia, and Venezuela—have undertaken reforms in this issue area since 1985, and most were at best restricted in nature. While Argentina and Brazil implemented their unemployment insurance schemes in response to the macroeconomic shocks on the 1980s, they did so in decidedly different political environments. In Argentina, a modest unemployment insurance scheme was part of the price the Menem administration paid for organized labor’s acquiescence to other painful reforms (Mazza 1999: 15) including increases in external flexibility. In Brazil, by way of contrast, workers defended their traditional prerogatives—including employment protection—while playing an active part in the formulation of a new unemployment insurance scheme in the mid-1980s (Sarney 1986: 112). Similarly, the labor-backed Lagos administration implemented an unemployment insurance scheme without compromising employment protection in Chile in 2001 (Sandbrook et al. 2007: 252; see also Weyland 1997: 46–7 on organized labor’s support for unemployment insurance). And the right-of-center Uribe administration implemented unemployment insurance while liberalizing labor markets in Colombia. Consequently, the institution of unemployment insurance was accompanied by growing personal security in Brazil and Chile and declining personal security in Argentina and Colombia.

A no less important question concerns the relative absence or poverty of unemployment insurance in most of Latin America. Why is the region allergic to



**FIGURE 31.4** Personal security by executive ideology

*Notes:* The unit of analysis is a presidential administration. The sample includes the 108 administrations found in Latin America since 1985; however, administrations that failed to pursue reform (i.e., “no net change”) are excluded from the figure. Codings by authors. Ordered logistic regression coefficient =  $-.41$ ; robust standard error =  $.27$ ;  $z = 1.59$  ( $p = .11$ ); full results available from authors on request.

European-style social insurance? A substantial body of literature traces the answer to the region’s inability to raise the revenue needed to fund more ambitious UI systems (Schrank 2009a) and the concomitant consolidation of a vicious circle of segmentation and informality. Latin American governments have therefore addressed their social spending less to UI than to conditional cash transfers targeted at the unemployed and underemployed. By targeting the unemployed and the underemployed in the informal sector, these programs may further increase the incentive to sustain the status quo in terms of labor regulation.

### 31.4.4 The politics of personal compensation

What, then, accounts for variation in personal security? While our indicator of personal security is a composite variable, it is by no means random in nature. On the contrary, we would expect executive ideology to influence personal security as well as flexibility, and we therefore code our 108 presidential administrations on an ordered scale that tracks whether workers were “less secure” ( $-1$ ) at the end of the administration, “more secure” ( $1$ ) at the end of the administration, or experienced “no net change” ( $0$ ) in security over the course of the administration, and regress the resultant indicator

on executive ideology. Predicted probabilities derived from the ordered logistic regression are found in Figure 31.4.

While the results fail to achieve conventional levels of statistical significance, and are best interpreted as convenient exercises in data reduction in any event, they are broadly compatible with our hypotheses. Right-of-center governments are more likely to undercut personal security. Left-of-center governments are more likely to bolster personal security. And the modal category is no net change (and is left off the figure). Furthermore, executive ideology provides a perfect prediction of shifts in personal security in the post-1999 period.

## 31.5 ENFORCEMENT AND LABOR INSPECTION

Labor laws are unlikely to affect wages, working conditions, and personal security if they are not enforced. For example, the introduction of severance payments would have little effect on workers' security if employers ignored the law and failed to compensate their former workers upon dismissal. In fact, Bensusán (2007) maintains that regulatory agencies can foster flexibility in the absence of legal reform by reducing the vigor of their enforcement efforts. Cook agrees that non-enforcement of labor law frequently fosters a form of "de facto flexibility" that renders de jure reform unnecessary (2007: 193). And Tokman admits that "haphazard compliance with labor law is commonplace" not only in the so-called informal economy but in "modern activities, particularly in countries where fiscal discipline is poor and inspection capabilities are limited" (2007b: 261). In order to provide a better picture of the worker protection in the region, therefore, it is necessary to analyze the evolution of labor law enforcement over time.

In this section, we address the question of enforcement in two steps: first, by examining trends in enforcement resources and practices; and second, by exploring their political sources. We focus on labor inspectorates rather than labor courts because the former constitute the first line of defense against noncompliance and abuse. That is, we focus on "enforcement" based on the resources for monitoring the application of the law rather than the sanctioning of infractions—in part, because the legal process is usually started after the employment relationship has been ended rather than being remedial.

### 31.5.1 Enforcement trends

We begin with a variant of the International Labour Organization's standard enforcement indicator: the ratio of labor inspectors to the economically active population (EAP) in millions (i.e. the "enforcement ratio"). While the ratio of inspectors to workers "is currently the only internationally comparable indicator available" (ILO 2006: 4), it is not made available on a systematic basis, and we have therefore compiled data and statistics from ministry websites, academic papers, newspapers, country reports produced

by ILO, the US Department of Labor, and the US State Department, and our own survey of country experts in an effort to build the most comprehensive dataset possible.

Table 31.1 includes data on the absolute number of inspectors and the enforcement ratio for four potentially overlapping years: the first and last years for which we have been able to find reliable data; and the years in which the enforcement ratio took on its highest and lowest values respectively. The data suggest the following:

- Between the first and the last observed years, enforcement efforts have expanded in nine countries (Argentina, Chile, Colombia, the Dominican Republic, El Salvador, Guatemala, Panama, Peru, and Uruguay) and declined in eight countries (Bolivia, Brazil, Costa Rica, Ecuador, Honduras, Mexico, Nicaragua, and Paraguay). Data for Venezuela are inconclusive.
- Enforcement expansion has rarely been consistent over time. While Chile and El Salvador appear to have undertaken more or less continuous expansions in the absolute number of inspectors since 1990 and 2002, respectively, most countries have experienced volatility. For instance, the enforcement ratio initially fell and later recovered in Argentina, Colombia, Panama, Peru, and Uruguay and, by way of contrast, initially expanded and then contracted in the Dominican Republic and Guatemala.
- Over the last few years not only El Salvador, Nicaragua, and Panama but a number of the region's largest economies—including Argentina, Colombia, Mexico, and Peru—appear to have undertaken meaningful expansions in their inspectorates. The broad pattern would therefore seem to be one of increasing enforcement.

### 31.5.2 The role of trade agreements

In short, the region's labor inspection agencies have been subject to more change than the laws they are designed to enforce. What accounts for the difference? Regional and bilateral trade agreements (RBTA) are one potential source of longitudinal and cross-sectional variation. After all, the United States has signed RBTAs with eleven Latin American countries since the early 1990s, and all but the North American Free Trade Agreement—which relegates labor standards to a controversial “side agreement” between the US, Canada, and Mexico—treat labor law enforcement as a condition of membership. For example, the US–Chile Free Trade Agreement stipulated that member countries had to enforce their own labor laws (Martin 2005: 203). And similar language was inserted into subsequent agreements with Panama, Peru, Colombia, and the so-called CAFTA countries (Costa Rica, El Salvador, Guatemala, Honduras, Nicaragua, and the Dominican Republic; see Schrank and Piore 2007).

Do RBTAs between Latin American countries and the US foster enforcement efforts among their participants? Unfortunately, the answer is difficult to discern for at least three reasons. First, the causal order of the relationship between the agreements and the enforcement efforts is inverted. While statistical methods assume that causes produce

Table 31.3 Enforcement resources in Latin America, 1985–2009

Country	First observed year			Last observed year			High year			Low year		
	No.	Ratio	Year	No.	Ratio	Year	No.	Ratio	Year	No.	Ratio	Year
Argentina	212	17.27	1988	475	24.77	2007	475	25.32	2006	71	5.03	1994
Bolivia	37	14.74	1990	19	4.18	2008	73	27.54	1992	15	3.72	2004
Brazil	3285	52.62	1990	3021	31.18	2009	3285	52.62	1990	2873	30.93	2006
Chile	80	14.22	1990	357	52.05	2009	357	52.05	2009	80	14.22	1990
Colombia	260	14.28	1998	746	30.99	2008	746	30.99	2008	248	12.38	2001
Costa Rica	61	44.95	1995	90	41.78	2008	117	86.22	1996	90	41.78	2008
Dom. Rep.	70	25.93	1991	203	50.12	2007	212	73.03	1994	70	25.93	1991
Ecuador	74	17.53	1993	61	9.07	2007	74	17.53	1993	61	9.07	2007
El Salvador	40	15.41	2002	159	53.77	2008	159	53.77	2008	40	15.41	2002
Guatemala	98	30.97	1995	238	51.76	2009	292	77.80	2002	98	30.97	1995
Honduras	125	56.82	1997	120	33.98	2008	125	56.82	1997	80	32.57	1999
Mexico	801	23.91	1993	616	13.58	2007	801	23.91	1993	568	13.16	2004
Nicaragua	84	46.98	2001	98	42.26	2009	84	46.98	2001	57	28.02	2005
Panama	80	64.57	1999	185	114.27	2009	185	114.27	2009	78	50.58	2007
Paraguay	38	18.56	1996	41	12.48	2009	103	48.54	1997	41	12.48	2009
Peru	158	14.10	1999	480	33.98	2007	480	33.98	2007	150	12.94	2000
Uruguay	80	59.13	1989	142	76.55	2009	142	76.55	2009	74	52.59	1991
Venezuela	97	7.78	2004	97	7.78	2004	97	7.78	2004	97	7.78	2004

Notes: The enforcement ratio is defined as the ratio of labor inspectors to the economically active population (EAP) in millions.

effects over time, US policymakers ask their trading partners to make the necessary changes to their enforcement efforts pre-emptively—so that enforcement efforts anticipate, rather than follow, the approval of the trade agreements that ostensibly cause the outcome in question. Second, indicators of the *desire* to forge an RBTA are unavailable. While enforcement efforts are perhaps best seen as products not of the trade agreements themselves but of the desire to forge trade agreements with countries like the US that impose conditions on their trading partners, we lack data on the origins of those desires and are therefore unable to trace changes in the level of enforcement to changes in the desire to forge an RBTA over time. And, finally, there are ceiling and floor effects. Nobody would expect an RBTA to foster increased enforcement in a country that is already doing an adequate job of enforcing its labor laws or meeting with US approval. And nobody would expect the absence of an RBTA to foster diminished enforcement in a country that was already lagging behind. As a result, the most compelling explanation for the growth of enforcement in recent years is not readily subject to systematic multivariate analysis.

We therefore pursue an alternative approach by (i) simply comparing the enforcement ratios of RBTA negotiators and non-negotiators and (ii) drawing upon qualitative data to explain any differences in their efforts. Table 31.4 includes descriptive statistics and significance tests and reveals that RBTA negotiators are on average twice as aggressive on the enforcement front as non-negotiators.

The mean differences between negotiators and non-negotiators are broadly significant under either a standard t-test ( $t = 1.92$ ;  $p = .07$ ) or a non-parametric alternative ( $z = 2.31$ ;  $p = .02$ ). The between-group differences in the median values of the enforcement ratio are even higher ( $X^2 = 4.2$  [ $p \{ .04$ ]). And the estimated probability that the enforcement ratio is higher for negotiators than for non-negotiators (derived from the non-parametric Mann-Whitney test) is .83.

The US did not, however, “cherry pick” trading partners with exemplary labor records. On the contrary, many RBTA members have regrettable enforcement histories (e.g. the Dominican Republic, El Salvador, Guatemala, and Colombia), and qualitative data therefore suggest that trade considerations are linked to enforcement efforts in a number of different ways. For example, the Dominican Republic and Guatemala increased their

**Table 31.4 Enforcement resources by RBTA negotiating status**

RBTA status	Mean	Median	Minimum	Maximum	Countries
Negotiator	47.1	42.3	13.58	114.27	Chile, Colombia, Costa Rica, Dominican Republic, EL Salvador, Honduras, Guatemala, Mexico, Nicaragua, Panama, Peru
Non-negotiator	23.7	12.5	4.18	76.55	Argentina, Bolivia, Brazil, Ecuador, Paraguay, Uruguay, Venezuela

*Notes:* The enforcement ratio is defined as the ratio of labor inspectors to the EAP in millions. Significance tests:  $t_{\text{enforcement ratio}} = 1.92$  ( $p = .07$ ); Mann-Whitney's  $U = 64$  ( $z = 2.31$ ;  $p = .02$ ).

enforcement efforts in response to unilateral US pressure in the 1990s and early 2000s, and were thus well positioned to meet US demands when negotiations over CAFTA began a few years later (see e.g. Fuentes 2007; Schrank and Piore 2007; Schrank 2009b). El Salvador and Peru dragged their feet in the earlier epoch and were thus forced to expand their efforts more rapidly in the mid-2000s (Alliance for Labor Rights-Peru 2007: 21; Rogowsky and Chyn 2008: 130). Chile and Costa Rica have for the most part been at the forefront of regional enforcement efforts, and thus had little to worry about when their respective trade negotiations began at more or less the same time. And Colombia and Panama have recently tripled the sizes of their respective inspectorates in an effort to convince the US Congress to ratify their recently negotiated agreements (see e.g. Ministerio de Trabajo and Desarrollo Laboral 2008; Ministerio de la Protección Social 2008).

The point, therefore, is not to posit a simple cause-and-effect relationship between RBTAs and labor law enforcement, but to describe a multi-player game in which an evolving array of US trade conditions alter the incentives of Latin American policymakers over time. Some Latin American governments accepted increasing enforcement as the price to be paid for preferential access to the US market in the 1990s. Others were forced to follow their lead or risk losing market share to their more compliant competitors. And the competition merely intensified when unilateral preferences were replaced by regional and bilateral trade agreements in the 2000s.

The North American Free Trade Agreement not only constitutes the hemisphere's first RTA but provides the exception that proves the rule. After all, NAFTA's negotiators initially overlooked the labor question and wound up relegating the issue of labor standards to a politically controversial and legally ineffective "side agreement." While the negotiators of subsequent trade agreements would learn from their predecessors' mistakes, and would therefore include labor standards in the core of their agreements, their efforts would make little difference in Mexico—which still boasts the lowest enforcement ratio of any RTA member by a fairly substantial margin.

In short, the pattern of labor reforms seems to respond to the ideological incentives of policymakers and their ties to organized labor. By contrast, differences in enforcement—measured as resources dedicated to monitoring those same laws—are more related to the efforts of Latin American countries to gain access to the US market. This is to be expected in a world in which left-leaning political parties in Latin America look for visible legislative victories that will appease their allies in the labor movement and left-leaning politicians in the US look for enforcement commitments that will appease their allies in organized labor as well—and thus condition preferential market access on the enforcement, rather than the character, of Latin American labor law.

## 31.6 CONCLUSION

We find that Latin American countries have not experimented with flexicurity in any meaningful way. After all, the provision of unemployment insurance has been limited to

a relatively small population of formal-sector workers in a small number of countries. And Latin American workers and unions have therefore focused their efforts on the defense of the region's pre-existing model of risk reduction through severance payments and employment protection.

The defense of the traditional model simultaneously constitutes a rational response to the state's inability or unwillingness to provide effective unemployment insurance, and underscores the validity of Mares's account of the politics of social insurance in the context of state weakness (2005). But Latin American informality provides a further obstacle to the emergence of broad-based risk pooling. And the growth of non-contributory cash transfer programs that are designed to deal with unemployment and poverty are likely to further complicate the politics of social provision in the future, especially if their beneficiaries organize to defend their survival rather than to defend or reinforce regulations that address formal employment.

Our analysis is anything but a brief in defense of labor-market based systems of social protection. Employment protection laws and severance payments pool risks at the level of the enterprise rather than the economy, and thereby elevate labor costs, undercut redistribution, and give firms and workers an incentive to enter the informal economy. Informality further enervates the state's ability to mitigate risks and protect workers. And policymakers therefore respond to the growth of poverty, informality, and popular political opposition in accordance with the incentives derived from their partisan preferences, especially since labor reforms in dualistic economies are insufficiently salient to drive national electoral outcomes. The precise balance between liberalization and regulation tends to depend on the ideology of the governing party and the nature of its core constituency, and executive ideology and union influence are therefore more important predictors of labor law reform than "economic" variables like debt and unemployment.

They are by no means the only relevant variables, however, for the failure to develop more thoroughgoing systems of social insurance may well be explained by fiscal constraints. In fact, Victor Tokman worries that the northern European experience is rendered all but inapplicable to Latin America by structural differences including not only pervasive informality in the latter region but an almost chronic inability to generate "sufficient fiscal resources to fund a system of social and labour protection sufficiently broad and generous to provide security for the whole population" (2007b: 102). Latin American governments therefore continue to defend a low-cost welfare state that gives core workers security through statutory labor law and leaves peripheral workers to fend for themselves. In turn, these institutions reinforce the policy preferences of both formal and informal workers who are simultaneously unable to extract redistributive social insurance schemes and unwilling to pool their own resources through a state mechanism that they have little capacity to monitor.

Efforts to gain or consolidate preferential access to the US market may well constitute a shock to the system—if not necessarily a threat to the equilibrium as a whole. While policymakers in North America are inclined to condition their trade agreements and preferences on the nature of labor standards in Latin America, they are understandably reluctant to expose their own labor and employment laws to international scrutiny, and

they have therefore focused their efforts on the enforcement—rather than the overhaul—of existing laws and the protection of the most “universal” of labor rights (e.g. freedom of association). Latin American governments have responded by augmenting their enforcement efforts. The potential consequences for informality, employment, and personal security are by no means obvious.

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