Financial Crisis and Global Imbalances: its Labor Market Origins and the aftermath

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Abstract

The economic crisis which started in the financial sector in 2007 is still impacting US and European economies today, causing decreases in output and employment levels. The crisis is the biggest since the Great Depression of 1929 and several arguments regarding the financial collapse have already been put forward (Obstfeld and Rogoff, 2009; Skidelsky, 2009; Whelan, 2010; Semmler et. al, 2010; Caballero et al., 2008). The objective of this paper is to show that the crisis is rooted in the uneven income distribution and inequality caused by the current financial led model of growth. The process of financialization which took place in the 1980s in the US and then in the EU, was coupled with labor flexibility, wage moderation and profit soar. The flexibility agenda of the labor market and the end of wage increases, along with the contraction of indirect wage (i.e. public social expenditure) diminished workers' purchasing power. This was partly compensated with increasing borrowing opportunities and the boom of credit consumption, which helped workers to maintain some unstable consumption capacity. However, in the long term such an unstable consumption derived from precarious job creation, job instability, and poor wages weakens the aggregate demand. Hence, labor market issues such as flexibility, uneven income distribution and poor wages, and financial crisis are two sides of the same coin. Both have a direct impact on the real economic crisis and the current global imbalances.

Key words: Financial crisis, saving glut, global economy, labor market, wage, productivity

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