

Essays on the South African Labour Market



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Foreword

This short text represents a series of nine print media articles that were written over the last 14 months on South African labour market issues. The articles deal variously with labour demand trends in the domestic economy; the nature of poverty in the labour market; the ongoing problem of skilled worker emigration and the much vexed issue of a national income grant.

The decision to put this publication together was borne out of the constant requests that the Unit fielded for non-technical advice and assistance on the South African labour market. It is hoped that this publication, by providing short, focused and non-technical articles, assists in this regard. Given the nature of the topics covered, it is perhaps inevitable that a certain degree of overlap would eventuate. All the same, this should only enhance the value of the publication in engendering interest and debate amongst students, policy makers, unionists and others interested in the South African labour market.

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Some People are more Jobless than Others

Public debate on the institution of a universal income grant was sparked most notably by the Congress of South African Trade Unions's (COSATU) call for a Basic Income Grant (BIG) of R100 to all adults in the society. The notion of an income grant has more recently become part of official government policy thinking, through the newly formed Committee of Inquiry into a Comprehensive Social Security System.

One of the committee's briefs therefore is to investigate the notion of a national income grant scheme for the unemployed. Indeed, the Minister of Welfare has already provided an estimate of R7 billion as the potential cost of such a scheme. If the grant scheme is going to be targeted at the unemployed though, a few important factors need to be considered, relating to the nature of unemployment in the South African economy.

Taking cognisance of employment trends

At the outset, one needs to recognise that South Africa's extraordinary unemployment levels exist within the context of specific employment shifts that have occurred in the economy over the last few decades. These employment shifts indicate massive job losses, particularly in the primary sectors, matched on the other hand by significant increases in the demand for labour in the services sectors, notably in financial and business services.

In terms of skill levels, this sectoral change in employment reveals that the need for highly skilled workers (concentrated in the services sectors) has risen dramatically. For example, over the last 25 years the demand for professionals has risen by about 250%. In contrast, the demand for unskilled workers has plummeted. Hence, the number of farm workers over the last 25 years, fell by 50%, while the demand for basic production workers declined by 4% over the same period.

Importantly, these employment trends are likely not only to continue, but in all probability to intensify over the medium term. This is crucial for our thinking around an income grant, because these trends inform us about who the winners and losers have been, and are likely to be, in the labour market. Simplistically, the winners have been the highly skilled while the losers have been almost without exception, unskilled workers. To caricature this trend - while computer programmers have gained dramatically, mine and farm workers have been the losers from these changing employment patterns.

In terms of the unemployed, this means that those individuals who are not skilled or, put differently, have low levels of education will in all probability not get a job. Furthermore those who are older and not well-educated will most likely never obtain a job in their lifetime. In contrast, young unemployed individuals with some form of education can be trained up and provided with some of the skills that

firms may find useful. It needs to be remembered that in contrasting these two groups, whilst they are both officially unemployed, they present very different employment probabilities.

In this context, the unemployed youth with some level of secondary education may, with the help of a skills development programme for example, find some form of employment. However, the middle-aged unemployed with very low levels of formal education will in all likelihood never find employment in their lifetime. It is our employment trends observed above, that strongly indicate that such an outcome has an extremely high certainty.

Targeting the unemployable

If one dissects the unemployed in this way, the unemployed youth are a *job creation* issue. However, the older unemployed are *not* a job creation problem, as these workers are likely to never find employment again. The latter, in being *unemployable* rather than unemployed, are a *poverty alleviation* issue, and as such it is this group of individuals that the income grant needs to focus on.

It is for those individuals where the labour market is no longer a feasible option as an income source, that the notion of a welfare grant is at its most powerful. In other words, the idea of a social safety net for the poor is most potent when focused on those workers who are so marginalised, that no form of labour market intervention will extricate them from indigence.

It is when trying to use the income grant - a poverty alleviation tool - for a problem that is a labour market challenge (such as the unemployed youth) that the scheme begins to lose its appeal and indeed its effectiveness.

So, what do the basic numbers tell us about such an idea? According to the October Household Survey of 1999, the unemployed number about 5.9 million individuals. Of these close to 90% are African, and 56% are female. Hence, unemployment as we know too well by now, disproportionately affects Africans and women. In addition, the data suggests that about 70% of the unemployed have never held a job before. This fact justifies the importance of looking into the feasibility of an income grant, given the apparent failure of the domestic economy to organically create sufficient job opportunities.

In addition, and very importantly, the figures show that close to 40% of the unemployed have primary schooling or less. This cohort of the unemployed captures a large percentage of mine and farm workers who lost their jobs over the last few decades. These individuals are invariably living in rural areas and between the ages of 35 and 64. It is precisely this group of workers that needs to be targeted for an income grant. No amount of state intervention in the form of skills development, SMME support and the like is going to lift these workers out of indigence and into employment. These individuals form the core of the *unemployable*.

Given the changing employment trends observed above, these workers are never going to find sustainable, long-term employment. What is required to assist these individuals is some form of poverty alleviation expenditure - and no intervention would be more suitable than a direct income transfer. In this way, the income grant would be confined to a particular group amongst the unemployed, and in addition one would be assured that it would be reaching the most marginalised amongst the unemployed.

By the same token an income grant to unemployed youth who, in the main have a matric would be an ineffective and inefficient use of state resources. The data shows that these unemployed youth number approximately 4 million. Hence an income grant targeted at all the unemployed would not only go predominantly to the youth, but would end up assisting that group amongst the unemployed who arguable least require direct state assistance.

These individuals require more focused labour market interventions such as skills development and

SMME promotion programmes. It is these individuals that do still have some probability of obtaining formal employment, and state intervention needs to reflect an attempt at upgrading the supply characteristics of these workers to meet the new labour demand needs of formal sector firms.

Ultimately then, one would hope that the Department of Welfare considers the potential unequal effect of an income grant that is applied unilaterally to all unemployed individuals. Apart from the obvious effects that such a scheme would have on for example the disincentive to find work it is evident that the transfer, in trying to reach all the unemployed with a limited budget, may end up providing very little to the unemployed who need it the most.

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5th November 2000, Sunday Independent

2

Brain Drain hits the Labour Market

At first glance, employment trends over the last few years tells us nothing surprising - that aggregate employment grew at modestly low levels, with the informal sector being a job creator and the formal sector a job shedder. The employment of different race groups however, yields a disturbing trend. While the employment of African, Coloured and Asian workers either remained constant, or increased marginally, White employment declined by some 90 000 jobs.

Given the skills biased nature of employment changes in the South African labour market, and the fact that these overwhelmingly benefit White workers, this is a startling and totally unexpected result. Is this reflecting the fact that White unemployment levels have increased significantly?. This is a conclusion one would be tempted to arrive at on the basis of casual observation.

The data however doesn't support this, given that White unemployment in this period increased by less than 5000 workers. The main reason then for the drop in White employment levels, has to be that fewer are now part of the local labour force. Hence, we find that the White economically active population actually declined by about 85 000 workers - an extremely disturbing trend. The two key reasons, in any labour market, for fewer individuals in the labour force as a whole is that they are either retiring early or emigrating.

In the case of early retirement, this may reflect the spate of Voluntary Severance Packages and other public sector strategies to shed White labour in the early days of internal civil service transformation. It is a process that was probably necessary in order to truly transform the sector in the higher-level occupations. But the other reason for the 90 000 fewer Whites in employment, namely emigration, is a vastly different issue that does raise serious concerns about the economy's ability on the one hand, and need on the other hand, to retain its skilled workforce.

Estimating the brain drain

Informal knowledge and personal experiences tell us that there has been significant emigration of skilled individuals from South Africa to the developed world - a phenomenon colloquially captured as the 'brain drain'. Determining the size of these flows however is notoriously difficult. It is essential that we derive accurate estimates of these emigration flows, in order to determine what constraint this poses in a labour market that already faces severe skill shortages.

One of the key data problems is that Statistics South Africa (which in turn collects its data from the Department of Home Affairs), only measures the extent of self-declared emigration. Needless to say, the numbers represented here are a gross under-estimate of actual skilled worker emigration.

The SSA estimates of emigration tell us for example, that in the period 1994-1997 some 20 000 economically active individuals left South Africa. A more ingenious method of estimating emigration

though, revolves around going to the recipient countries, who often keep better data than the sender country.

A recent study by the South African Network of Skills Abroad (SANSA) based at the University of Cape Town, estimated that between 1994 and 1997, the number of workers going to 5 select developed country economies totalled about 33 000.

Given that these 5 countries capture about 77% of all emigration from South Africa, one can arrive at a guesstimate of total labour force emigration between 1994 and 1997 of 43 000. Dwell on this figure, because its important in the context of our labour market: Recall that White employment in this period fell by about 90 000.

What we are saying then, is that close to half of this employment decline amongst Whites was because these individuals were emigrating. Placed into a context of serious skills shortages at the top-end of the labour market, and of growing wage premia for skilled workers, this is an extremely worrying trend.

It means that the population wherein the country's skills are currently concentrated are also those with a very high propensity to leave the country permanently. What is popularly known as the 'brain drain' then, must be recognised as one of the most serious labour market constraints that this economy currently faces.

It is interesting to note that large declines in labour force participation and employment are reported amongst Whites in the 16-24 and 25-34 age groups. This may typify the nature of the emigration exodus: that of young White graduates who at the beginning of their working life are leaving the country. If this is the trend, and the evidence is provisional rather than confirmed, then the labour market may be losing skilled individuals who are at the beginning of their earnings and productivity life cycle. This age dynamic adds another worrying dimension to the emigration problem.

Ultimately though, the analysis above has uncovered an important, and worrying, development in terms of employment creation. This is that the country's key skills reservoir located, for historical reasons primarily amongst White workers, is being rapidly depleted. The results indicate that this is a function simultaneously of White emigration of alarming proportions, and high levels of early retirement concentrated in the public sector.

Individuals retiring can be reintegrated into the workforce, and indeed many have opted back into the labour market through various forms of short-term employment. Those emigrating however, pose a completely different, and potentially insurmountable problem to the domestic economy.

A framework for policy intervention

In terms of policy intervention to deal with this issue of ongoing and apparently rising emigration, it would seem that a few issues need to be dealt with. These are firstly, that SSA in conjunction with the Department of Home Affairs sets up formal agreements with recipient countries to access all the data required to monitor our annual levels of emigration.

Every year then, we should as a country be able to determine how many individuals emigrated, where they emigrated to, why they did so, what their occupations were and so on. It should not be the job of researchers to intermittently try and piece together emigration figures from secondary sources. This is far too important an issue for government agencies not to get involved in.

Flowing from this basic data requirement would be a series of issues that need to be injected into the current policy debate around emigration.

- Firstly, we need as the above has done very briefly, to link the notion of emigration to the skills shortage in the labour market. It means that not only do we currently need to encourage the development of a wider base of higher skilled workers, but also that we need to focus on the fact that the existing base of skilled individuals are showing a very high propensity to leave the country. The issue of emigration needs to be placed at the heart of the skills development debate.
- A reorientation of the debate would lead to a second issue, that of interrogating the various factors that underlay the decision by individuals to emigrate. Scant evidence is not good enough. An extensive profile of all emigrants is the first step in trying to stem the outflow. To my knowledge, we do not as yet have this detailed profile.
- Finally, there can be no doubt that to match the ongoing outflow of skilled people, we need to act more vigorously in attracting non-South African skilled workers into the country. This is clearly not occurring systematically, and in many cases it could be argued that we are discouraging the entry of skilled foreign labour. The attraction of these individuals from the rest of the continent and indeed other developing countries, is essential if we are going to begin in the short-run to counter the current skills gaps in the economy and the future shortages that will occur through emigration.

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7th September 2000, Business Day

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How to reduce South Africa's Wage Gap

As the Employment Equity Commission (EEC) of the Department of Labour begins to assess the nature and extent of discrimination and inequality in the labour market, it is important to inject a series of numbers and facts early on into this debate. This is to ensure that the EEC makes proclamations and decisions that will be based on empirical evidence that represents the nature and extent of inequity in the labour market.

Wage inequality measures by race and gender

The most obvious markers of wage inequality are race and gender - namely that significant wage differentials exist amongst race groups and between males and females. The evidence shows though that while White workers earn on average 70% more than their African and Coloured counterparts, they only earn about 43% more than Asian employees. This immediately suggests that in terms of race-based differences, it is African and Coloured workers in particular who are low earners in the labour market.

The gender differences indicate that the gap between males and females is not as stark as the racial wage gap. For example, the average female wage is close to 80% of the male wage. This is mainly due to the fact that many Asian and White females are in fact earning more than African and Coloured males. In essence, the racial wage gap is at present more stark than the pure gender-based wage differences. The importance of this basic data is that the EEC in its deliberations, needs to be mindful of carefully and simultaneously dissecting the race and gender components of the South African wage gap.

Wage inequality measures by education

Now of course one of the key drivers of the wage earned, is the level of education an individual attains. The data again supports this notion, as we find that employees with higher levels of education are likely to earn a higher average wage. In particular, those with a tertiary degree earn the highest average wage - which is what one would expect. However, more interestingly is the importance of attaining a matric certificate: those with a matric earn about 70% of the average wage of a degreed person, while those with some secondary schooling can only expect to earn about 35% of the wage of a university graduate.

The lesson here is starkly evident, namely that individuals are severely disadvantaged in the labour market if they fail, at a minimum, to obtain a matric certificate. Again then, the EEC needs to be cognisant of the fact that wage gaps and wage discrimination are strongly influenced by the levels of education and schooling acquired by individuals and employees in the labour market. This could mean, although more evidence is required for this, that the race and gender wage differences observed

are in fact partly because certain race groups (for historical reasons of course) have acquired more education than others. This allows them to attain higher levels of earnings.

With this reasoning, the most important element in an employment equity strategy becomes equalising access to and the quality of all educational provision in the society. A tall order no doubt, but this intervention needs to be seen as a key component of any extensive employment equity strategy.

Perhaps the strongest evidence for the importance of education in determining South Africa's wage gaps is provided when one examines wages by occupation and race. The data firstly shows that in general highly skilled workers earn significantly more than unskilled employees. For example, the average wage of a manager is approximately 93% higher than the average wage of a domestic worker or farm labourer. However the data then delivers an intriguing puzzle: skilled or semi-skilled African workers earn consistently less than their White counterparts at the same skill levels.

For example, an African manager will earn a median monthly wage of R2646, while a White manager will earn over twice as much at R7500 per month. In other words, we have two individuals who are both formally classified as managers, yet their wage differs markedly because of their race. Is this a case of widespread discrimination in the workplace?

To some extent, yes, unofficial discrimination has got to be a part of the story. And this relates to the fact that employers are probably viewing a degree from a historically black university (HBU) as inferior to that from a historically white university (HWU). Thus, although individuals may formally both have degrees, those obtained at an HBU simply yield a lower return than those from a HWU, given employers' inherent biases.

But this is only part of the explanation for the difference in the skilled wages for Africans and Whites. Perhaps a more important reason lies in the fact that the tertiary degree is a heterogeneous product. Simply put, individuals may all go to university or technikon, but will obtain *different* degrees and qualifications. Not all certificates and degrees are the same, and neither can they be expected to fetch the same value in the job market. It is this difference in degrees and post-graduate qualifications between African and White employees, that goes a long way toward explaining the skilled wage gap observed.

So does the data support the evidence of lower skilled African wages relative to White workers? In short, there is clear evidence that skilled White employees are primarily in occupations that fetch the highest price in the job market. Specifically, skilled White workers are predominantly employed as general managers, finance professionals and as engineering technicians. African individuals, on the other hand, are mainly employed in skilled occupations, as primary and secondary school teachers and in the nursing occupations. Of all skilled African workers, 42% are found in these occupations, while over 35% of Whites are found in the three listed occupations.

There can of course be no doubt that both sets of occupations are essential to the labour market and the economy in general. However, the wages these occupations fetch depends crucially on the demand for their services. Hence, employment patterns in South Africa indicate a very high demand for individuals with skills in financial and business services, information technology and science and engineering. There remains an extreme shortage of these skills in the labour market, and thus these workers will be paid a premium if they are hired.

In contrast, the need for individuals with teaching and nursing degrees, with some exceptions like Mathematics and Science teachers, has not increased dramatically and is unlikely to do so. The result of course, is that their wages are consequently lower.

What the above suggests is that the inequality in wages amongst skilled African and White workers can be ascribed essentially to the differing occupations they find themselves in, and then more importantly the different needs the economy places on these skills.

Ultimately, ascribing skilled wage gaps between the race groups as a function solely of unofficial

4

A Closer Look at the Income Grant

The Minister of Welfare and Development, Zola Skweyiya, has recently announced his department's intention to pursue the feasibility of setting up a national income grant scheme. There can be no doubt that such a grant system requires serious consideration, to buttress the current suite of social assistance programs directed at the country's most indigent.

One of the primary reasons for examining the option of a national grant, is that the current system omits significant segments of the populace, most notably the unemployed. It is known for example, that over a third of the unemployed are individuals who, given their skills, levels of literacy and location, are in fact unemployable, rather than unemployed. It is trying to target this prototype individual, that the notion of the welfare grant is at its most powerful.

However, it has to be recognised that such a grant system contains numerous difficulties that could result in its premature failure. This is particularly true given that the current suggestion conceives of a national, universally applicable grant. The difficulties arising from a national scheme, has lead many policy makers, to have deep reservations about the efficacy and workability of the scheme.

Obstacles to a national welfare grant

Operational expenditure costs

The first obstacle to a national welfare grant is that of the additional costs imposed on the scheme by the required operational expenditures. It is not clear whether Minister Skweyiya's estimate of R7 billion in fact included these costs. If not, then the operational expenditure in setting up and maintaining such a scheme would significantly increase the estimate provided by the Minister. Indeed, because such a fiscal transfer scheme does not exist at present, it would entail a massive initial set-up cost, combined with concurrent annual expenditures on maintenance. It is possible however, that the Department's new Welfare Payment and Information Service (WPIS) could reduce these set-up costs.

An additional problem with the price tag of R7 billion is that it does not build in the continued cost of the scheme from one year to the next, and fails to account for fluctuations in the scheme's grant payments. Hence, higher unemployment or poverty levels in the society, brought on for example by poor labour absorption rates, may see a rapid expansion in the scheme that could make it unaffordable very quickly.

Reduced employment incentives

A third very serious drawback of the scheme is that does not take employment incentives into account. Simply put, the offer of an income grant to employed or unemployed individuals, may induce many to stop working or looking for work and live solely on the grant. Studies of employment patterns in the economy though, have argued that in many cases, individuals at the low-end of the labour market are

not going to be in great demand and indeed, large sections of the unemployed are highly unlikely to be employed anyway. In this environment, an income grant could offer much needed respite from indigence in an economy with very low job prospects.

Imperfect targeting

A further drawback of a national welfare scheme, is that it assumes perfect targeting. In other words, it is assumed that every Rand spent in the grant, will go to the correct recipient. There would be no individuals or households getting the grant who are not eligible, and vice versa. Clearly this is an unlikely outcome in reality. Hence the spill-out effects of such a scheme are serious, and could mean that the scheme does not effectively reduce poverty to the levels initially aimed at.

Policy implications

For policy makers, the above are serious considerations that require intensive investigation before any agreement can be reached on implementing such a scheme. Hence it is firstly vital that the potential capital and operational expenditure estimates of the grant scheme be calculated and incorporated into the above estimates.

The old age pension scheme may be used as a guide to these associated costs. In addition though, the potential for expenditure in the scheme to grow as more recipients gain access to the grant, is particularly worrying. Indeed, the incentive effects alluded to above, could be a significant factor in expanding the commitment of the scheme to levels well beyond what the state can afford.

Even if the state were to consider redistributing within the budget to make finance available for such a scheme, the potential for it to expand as a result of a spurt in qualified recipients, is a risk the fiscally constrained state cannot be expected to take.

Taking into consideration that a more generalised scheme may furthermore not be perfectly targeted, government's reluctance to consider such a grant scheme is wholly understandable. If one adds to this, the fact that disbursements in the scheme would have to be undertaken at the provincial level, and the known difficulties with this, it is clear that a very strong, persuasive argument would need to be made to the Department of Finance concerning the feasibility of the scheme.

However, the evidence in other countries and in other studies, points unequivocally to the fact that transfer schemes are an effective and efficient manner in which to alleviate poverty in a society. Given this, is there any way in which to conceive of a grant scheme that would prove more amenable to the concerns of policy makers? There would seem to be two immediate alternatives in this regard.

Firstly, it may be useful to think of a grant scheme in more narrow terms, rather than the general far-reaching schemes suggested above. In this regard, one can conceive of a grant *only* targeted at a specific section of the population – for example unemployed individuals in rural areas who are over the age of 40. If the grant is focused in this manner, it may have more appeal to policy makers, given the economy's almost complete inability to absorb these type of individuals into long-term formal employment. The scheme could be further narrowed down, to include for example only those unemployed individuals who lost their jobs through structural decline in the economy - which would in essence mean targeting those who lost their jobs in the primary sectors. Such a scheme would dovetail well with the current Social Plan in the mining industry.

Secondly, it is possible to think of the poverty effects of an already existing income grant scheme that is up and running, that is well-targeted and does not have to concern itself with incentive effects. One can think of the old age pension scheme here. A key issue is the impact on poverty at the household level of increasing the value of the pension. Indeed in most poor households, the only regular form of income is the old age pension. A more detailed analysis of the possible poverty effects of raising its value would be an ideal avenue for initiating policy discussion with the relevant fiscal authorities.

While the budgetary constraints are recognised, it is well-known that the current, most effective mechanism for household poverty alleviation goals is the old age pension system. In this way, redistributing within the budget toward this grant scheme could be achieved, particularly in the context of alleviating poverty in a cost-effective and efficient manner.

Ultimately, it is clear that the Department of Welfare and Development is rightfully concerned with expanding the current welfare net, to include those who are particularly disadvantaged in the society. However, these proposals, it would seem, need to be significantly buttressed to take into account all the understandable, and serious concerns, that inevitably arise when considering a national income grant scheme.

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4th February 2000, Mail & Guardian

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Benefits of Wage Law could be Marginal

The Department of Labour has recently called for public submissions and public comment on the issue of minimum wages and conditions of employment for domestic and farm workers. An analysis of the first of these two issues, namely wages, will place into sharp focus the stringent trade-offs faced by the Department of Labour in this part of the workforce.

Basic wage and employment statistics

It is important, at the outset to get a sense of the basic wage and employment statistics governing domestic and farm workers in the economy. There are approximately 700 000 household domestic workers in the society, compared with just under 1 million farm labourers.

The imposition of any labour law legislation will therefore impact on close to 2 million workers, and their respective dependants. One is not therefore talking of an insubstantial number of affected individuals.

The overwhelmingly majority (96%) of domestic workers are female, while the majority of farm workers (78%) are male. Hence the legislation would have a near equivalent impact on both males and females in the workforce.

But perhaps the most important reason for the Department of Labour seeking to isolate these two occupations for special consideration, lies in the pitifully low wages earned by these two groups.

Domestic workers on average earn just over R300 per month, while farm workers earn approximately R400 per month. These two occupations are far and away the lowest paid in the South African labour market. To put into perspective how low these earnings are: domestic workers earn a third of what the average miner earns, and fourteen times less than the average skilled professional. Extremely low wages lead to the familiar outcome of individuals having a job, yet living in deep poverty. Given these earnings of domestics and farm workers, it is not surprising that over 80% of all these workers remain below the poverty line.

Minimum wage considerations

In this environment of extreme levels of indigence, it is tempting to give serious consideration to a legislated policy of minimum wages for these workers. It is possible, given the above parameters, to undertake a carefully conceived thought experiment, wherein the dilemma of the choice between higher wages and lower levels of employment is vividly displayed. We can think of such an experiment in the form of two scenarios:

Scenario 1 where the wage of domestic and farm workers is increased by 10%, and Scenario 2 where the wage is doubled. The first scenario is of course a far more likely outcome than the second. But the purpose of the extreme second case is to display how harsh some of the trade-offs between wages and employment are. The effects then, in a world where nothing else changes, of the above two scenarios are as follows:

Scenario 1

The increase in the wage of these two occupations by 10% will reduce the percentage of workers in poverty to 75%, a five % reduction to the poverty level prior to the wage increase. For domestic workers, this means that about 32 000 of them will no longer be in poverty. For farm workers, the wage increase will extricate 47 000 of them from poverty. Given the large numbers of these workers, this is not by any means a significant poverty reduction effect. This does not mean that the wage increase will not be beneficial, but it is clear that its benefits in terms of alleviating poverty will be marginal.

It has to be remembered though that along with a wage increase, there is a serious danger of employment losses, as some employers perceive the cost of employment as being too high. The results with this employment effect show that the 10% increase will cause, over a 2 year period, 50 000 domestics to lose their jobs and close to 70 000 farm labourers to be laid off. Clearly these are large employment losses associated with a seemingly reasonable wage increase.

The trade-off between poverty reduction on the one hand and employment losses on the other, is thus brought into stark contrast with the above exercise. Should the Department of Labour opt for a fairly reasonable minimum wage level, such as a 10% increase, the poverty impact for these two groups of workers will be modest, while the disemployment effect particularly large.

Scenario 2

The highly unrealistic case of a 100% increase or doubling of the wage for domestics and farm labourers, serves the important function of showing the depth of poverty prevalent amongst these workers. With this wage hike, the results show that about 45% of domestic workers will remain in poverty, while 34% of farm labourers will still be poor. Put differently, over 300 000 domestics and the same number of farm workers will continue to work below the poverty line, despite a doubling of their wage. It is clear therefore that even with such huge, and unrealistic wage increases, the poverty reduction impact remains relatively small. Put differently, the size of the reduction in poverty is far below the size of the wage increase offered to the affected groups.

Drawbacks of minimum wage policy

Unemployment

The disemployment effects of course, are significant. A doubling of the wage would, in the long-run, see about 500 000 domestics lose their jobs, which amounts to a 70% reduction in the size of the household domestic workforce. For farm workers, 670 000 will lose their jobs, which is the equivalent again of a 70% reduction. Clearly, a doubling of the wage will decimate employment levels in these two occupations.

There can be no doubt though that the Department of Labour is not considering a minimum wage set at double the current average wage of these occupations. So the employment consequences of this second scenario are less interesting. It is on the poverty impacts that the results from the second scenario are important. What these suggest is that even with a doubling of the wage, poverty levels amongst farm and domestic workers will remain high and significant. The wage, it would seem, has a

limited role to play in eradicating poverty amongst these two groups of workers.

In essence, the analysis suggests that poverty eradication amongst domestic and farm workers cannot take place solely through a minimum wage policy. This is not the problem of minimum wage legislation *per se*, but rather the very high incidence of poverty found amongst domestic and farm workers. Ultimately, if the Department of Labour were considering a minimum wage policy directed at reducing poverty levels amongst these workers, it would not serve the purpose of significant poverty alleviation amongst its target population. This is true, it must be remembered, irrespective of what employment losses may occur from the minimum wage as well.

Should the Department of Labour opt for a modest minimum wage, the poverty reduction consequences would of course be minimal and so too would the disemployment effects. The Department would implicitly then be issuing a 'moral signal' to employers – that improved wages for these workers are to be striven for. Such a wage would set a first-step benchmark for good wage practice amongst employers. Indeed, such an initial minimum wage may set a positive trend, and see employers gradually increase the wages paid to these workers. Ultimately, given the above figures, this option may be the best and most optimal available to the Department.

Aside from the concerns around the trade-off between poverty and employment, there are two other relevant issues surrounding the minimum wage. These are the effects a minimum wage may have on *payments in kind* and secondly, the *monitoring* of minimum wages should they be set.

Deduced payments in kind

On the first, it is true that a large number of employers do offer transfers in kind to their employees. By this, one is referring to for example, food given to domestics or bags of mealie meal to farm labourers, by their respective employers. The imposition of the minimum wage may see employers rescind these free transfers and begin then to charge employees for these products. So, an employer of a household domestic may decide that the new higher minimum wage is not affordable given the current working arrangements. In order to retain the services of the domestic, the employer will begin to include the free meals and so on as part of the wage paid to the domestic. In such a case, the cash wage received by the domestic may not change, and in some cases may go down. The potential for circumventing the minimum wage law arises thus from the existing and significant free transfers flowing from the employer to the employee.

Monitoring

The second concern around the minimum wage, that of monitoring its implementation, is in many senses what the effectiveness of the legislation hinges on. For example, even a minimum wage at double the current average wage is only effective if government can ensure that such legislation is implemented and adhered to by employers. The Department of Labour is currently under-resourced in this arena, and effective monitoring of such legislation will be extremely difficult. In addition, and more importantly, domestic services and farming, are sectors notoriously difficult to monitor, even if the Department did have an adequate supply of labour inspectors. This is because employers in these sectors are widespread, often in unreachable areas and seldom a visible presence in the economy. If one thinks of the impossibility of trying to track down even a small national sample of households that employ domestic workers as well as extracting wage information from the employer or employee – then the difficulty in monitoring these two sectors becomes evident. Simply put, the effectiveness of any minimum wage legislation will depend the state's ability to enforce and monitor the implementation by employers of the terms of the legislation. An inability to enforce the legislation, to all intents and purposes, nullifies it.

It should be evident then, that the Department of Labour has taken a laudable step in identifying the poorest workers in the society as requiring some form of legislative support and protection. The analysis however, has shown that the choices are difficult: that tremendous, and in reality unimaginable, increases in the wage will have a relatively small impact on poverty. Together with the difficulties in

monitoring such legislation, its employment effects as well as employers' possible responses - the minimum wage legislation proposed here should be at best viewed as setting a precedent for employers to improve their wages and other conditions of employment for these two indigent groups of workers. The goal of poverty reduction amongst domestic and farm workers is thus only realistically achievable through a combination of economic policy interventions.

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10th September 1999, Mail & Guardian

6

Look After Low-End Jobs

Structural and production changes

An analysis of economic trends in South Africa, over the last 25 years reveal two important and indeed striking changes.

- *Firstly*, a structural shift has occurred within the productive base of the economy. More specifically, the two primary sectors, agriculture and mining have witnessed a secular decline in their share of GDP. Hence the share of agriculture in GDP fell by about 4% since 1970, while mining's contribution declined by 3%. The decline of the primary sectors though, has been matched by a significant growth in the service sectors, most predominantly financial & business services and wholesale & retail trade. The service sectors' growing contribution to GDP is best reflected in financial & business services, where its share of GDP rose by over 6% between 1970 and 1995.
- *Secondly*, a major shift has taken place in the domestic economy - there has been a rapid rise across all sectors, in capital-labour ratios. Simply put, sectors have shown an increasing reliance for machinery over labour in this 25 period, in the search for productivity gains. In the primary sectors for example, capital-labour ratios increased by over 150% since 1970. In the service sectors the rise in capital intensity is manifest in higher rates of computerisation, brought on by the information technology revolution - a process which has intensified over the last decade.

Impact on employment levels

Given the shift away from the primary toward the service sectors on the one hand, and the rising capital intensity in the economy, on the other, it is important to determine what effects these factors had on employment levels and trends. In pure quantity terms, there were huge employment losses in agriculture and mining, amounting to 1.5 million jobs over 25 years.

In contrast, the service sectors gained over 2 million jobs. This employment outcome has been a result of both the decline in the primary sectors and the rising capital intensity in the economy. Employment needs in the economy have thus irrevocably shifted away from the primary sectors and toward the services industry.

Employment effects on skilled and unskilled sectors

It is necessary however, to unpack these aggregate employment changes. More specifically, we need to determine if the changing employment patterns observed were skills-neutral. Put differently - did the employment gains and losses over the last 25 years mean that certain skill groups benefited while others lost out?

Data for the period indicates quite clearly that skilled workers made substantial gains since 1970, while the proportion of workers in unskilled occupations was steadily eroded. Hence unskilled workers' share of employment fell by between 4% and 54% since 1970. In contrast the share of skilled occupations has grown, in some cases, by as much as 250%. Clearly the structural shift in the economy, combined with the rising capital-labour ratios have meant a preference for skilled over unskilled labour.

This changing employment preference is a result of the decline in the primary sectors, who are intensive in the use of unskilled labour combined with the rise in services, where the demand is primarily for those in skilled occupations (and more specifically, IT professionals). In addition, an environment of higher capital intensity invariably means that more skilled workers will be preferred to less skilled workers to operate the new machinery.

It is expected that the twin trends of rising capital intensity and the growth in services, coupled with the decline in agriculture and mining, will continue in the future. This means of course that these employment patterns will also remain the same, if not intensify. In the process of long-run economic growth, employment will benefit skilled and semi-skilled workers to the detriment of unskilled individuals. The winners in the next decade, all things held constant, will be those at the top-end of the job ladder and the losers invariably those at the bottom-end.

Policy implications

Wage restraint policy

In an environment of declining or stagnant demand for low-skilled workers it is relevant to raise the issue of labour market flexibility, a labour market policy intervention that is targeted essentially at this cohort of unskilled workers. The proponents of labour market flexibility argue that the wages of those at the bottom-end are too high.

Given the large pool of unemployed, it is argued, a manner in which to create more employment would be to lower the wages of those in unskilled jobs. This argument has often been captured as the wage restraint component of the labour market flexibility argument. It must be remembered that this is a discrete and separate argument, as will be expanded on below, from one which says that higher wages will mean greater employment losses for those at the bottom-end.

The analysis above has illustrated that the employment needs of firms has been and will continue to be for those in semi-skilled and skilled positions in the economy. No significant number of new jobs are going to be created at the bottom-end of the job ladder. If this is the case, then reducing the wage for those in unskilled positions, will not increase the quantity of unskilled workers hired as the demand for these skills simply does not exist.

Firms will simply not hire more unskilled workers if they become cheaper, as their preferences as we have seen, are primarily for skilled workers. Hence the arguments for the job-creating possibilities of a wage restraint policy, are simply not tenable if they are carefully tied to the employment needs of firms.

The employment needs of firms are for skilled workers and not unskilled workers, and so making the latter cheaper may simply see firms using the surplus funds from the lower wage bill, to hire (already employed) skilled workers. The unemployed who are in the main unskilled and have never worked before, are unlikely to see their job prospects improved by such a wage restraint policy.

The wage flexibility debate in South Africa, thus far has not taken cognisance of this fact, and has effectively rested on the assumption that all workers in the economy are homogenous in skill - that is they all possess the same quantum of skills - and are all in equal demand by employers. As soon as this assumption is broken, and one introduces the notion of differentially skilled workers, the argument that lowering the price of labour will create more employment for lower skilled workers is simply

7

Why Poverty's more than Sums

Identifying the poorest individuals

There can be no doubt that one of the key dilemmas facing the South African government is that of eradicating or at least reducing, the incidence of poverty in the society. The first step though in grappling with the problem of poverty is to try and understand who are the most affected groups in the society.

In the labour market there are three groups of individuals, who together explain over 80% of the poverty in the society. These individuals are the unemployed, domestic workers and farm workers. This means that while domestic workers and farm workers have jobs, they are still living in poverty. To give a comparison: While less than 4% of labourers in mining and manufacturing live in poverty, 38% of domestics are in poverty and 27% of farmers earn below the poverty line. Indeed, while the policies required to eradicate or at least reduce poverty are perplexing, the description of the problem and its various dimensions are depressingly simple in South Africa.

If we needed then to identify the poorest of the poor individuals in South Africa's labour market they would be the unemployed, followed by domestic workers and then farm workers. From a policy perspective, it means that labour market interventions that are concerned about poverty alleviation need to give credence to the fact that poverty exists not only amongst the unemployed, but also among narrowly (and indeed easily) defined sections of the employed.

Identifying the poorest households

Some commentators though, may argue that while these individuals identified are very poor, they could be living in households that are not poor. In other words, the collective income in a home that they may have access to, will make them non-poor. Examining the data, this is found to be patently untrue.

The three poorest individuals identified above, also come from the three poorest household types in the society. Put differently, this means that all homes in the country that have either an unemployed person, a domestic worker or a farm worker in them - are in fact the three poorest types of homes in our society.

Even in the homes these workers live in then, they are not able to access enough income to place them above the poverty line. Statistics show that in the homes where farm workers live, over 60% live in deep poverty. For the unemployed and domestics, over 40% of their homes are in poverty. A comparison with other households in our society gives a sense of the degree of inequity: A mere 0.5% of Asian homes are in poverty while 2% of White homes are poor.

Determinants of poverty

Of course in thinking of what factors cause these three individuals to be the most indigent in the society, a few obvious points come to mind.

Firstly, *location* is an important factor, and those that live in rural areas are more disadvantaged. Hence, farm workers in particular live in the poorest homes because they are located in rural areas where returns to labour are notoriously low.

Secondly, serious *gender inequities* operate in the labour market, and this explains a large portion of the domestic worker poverty. The two other factors that account for the observations above are *age and education*. Indeed, the young are particularly affected given the difficulty for new entrants to the labour market in finding jobs. As for education the message is relatively simple: lower education means lower income and therefore a greater chance of living in poverty.

Cost of poverty alleviation

One of the advantages of outlining poverty in the manner above is that we can undertake a basic, yet quite powerful, thought experiment. The experiment goes as follows: We know who most of the poor are, in which homes they live, and also how much money each of these homes earn. We can therefore undertake a theoretical exercise whereby we give each of these poor households enough money to place them above the poverty line. For example, if the home was earning an income of R500 and our poverty line is about R900, then we would need to give that home R400 and it would no longer be poor. We can then do the same thing for all the homes in the society.

If we use this approach then what would it, in theory, cost to eradicate most of the poverty in the society? In total the number of poor homes who have domestics, the unemployed or farm workers living in them amounts to just over 2 million. Our calculations show that it would cost about R10 billion per year to place all these homes out of poverty. So, how do we evaluate this number? Is it inordinately large or surprisingly small? To put the number in perspective: it represents about 6% of the government's total expenditure outlays. Government spends about 20% of its budget on paying the interest on its debt and about the same also on education each year.

This 6% then, is a very low number, and it would seem to indicate that the problem of poverty is easily solved. Does this mean therefore that all that needs to happen, is for government to make provision for an income grant of this sort on an annual basis, and we can immediately talk of a poverty-free society? The answer is no.

Drawbacks to the income grant scheme

The reason is that, as is the case with such appealing calculations, such a potential income grant scheme throws up a whole host of obstacles.

The first difficulty is that government will in no easy way be able to target the poorest of the poor effectively. Indeed, large wastage may occur through ineffective targeting, and the money may for example, get into the hands of poor homes, but not the poorest of the poor.

There is also the issue of the administration costs that inevitably go with the setting up of such a scheme, and this would substantially balloon the R10 billion figure quoted above.

Thirdly, giving grants to indigent homes, may result in an undesired outcome: that individuals will cease work or cease looking for work. Apart from the obvious individual morale issues here, such a withdrawal of labour would have serious negative economic consequences. One can think of the growing drain on the state of such a scheme, as new entrants to the labour market refuse to find jobs

8

Skills Initiative aim at the Wrong Target

There is a widespread belief that there is a need for job creation combined with skills upgrading in the economy. Part of the government's response to this has been the Skills Development Bill, while the union movement has put forward the Social Plan.

The *Skills Development Bill* aims to provide general skills to workers. This is to be funded through a payroll levy of 1% to 1.5% of the total wage bill.

The *Social Plan* aims to assist through a fund, workers affected by structural change in the economy.

The problem with both these policies is that the type of skills they intend to provide do not match firms' present employment needs.

Changing labour demand trends

An analysis of the labour market shows that total employment of unskilled workers (labourers, production, basic service and farm workers) has declined over the last twenty years. In contrast, skilled workers' (professionals, semi-professionals, technicians and managers) employment has increased at over 10% per annum since 1970. Therefore jobs have been lost at the low-end, and gained at the high-end. What lies behind this change in firms' demand for labour?

Causes of changing demand trends

The *first* cause of this change has been a dramatic structural shift in the economy. The primary sector has seen its share of GDP decline by 7% since 1970, while service sectors have increased their share by 8.5%. The type of workers hired differs between these sectors, with the primary sector making greater use of unskilled or semi-skilled workers and the service sectors making greater use of professionals. This means that because of the structural change, unskilled workers have lost while skilled workers continue to gain. This trend is set to continue in the future.

The *second* cause is production method changes – a dramatic shift to the use of microelectronics and increasing capital intensity in search of productivity increases. However, these changes do not affect employment evenly, with less skilled workers bearing the brunt of job losses while skilled workers often gaining employment.

Analysis shows that unskilled workers have shed jobs at a rate of 1%-2% per annum since 1970 due to changes in production methods while skilled workers have gained to the tune of 8% per annum. This trend is set to also continue.

What these trends indicate is that even in an environment of economic growth, unskilled workers

9

Is Economic Growth about Reducing Poverty or Inequality?

What's the difference you may ask? Essentially, the measure of poverty in its simplest form is the number of individuals earning below some pre-determined poverty line. Hence, in South Africa we can say that about 32% of all households are in poverty. Inequality though, is a very different social welfare measure.

Inequality measures the differences in income between individuals. So we may all be poor in a society, yet earning more or less the same, and hence inequality levels in the society will be low. Poverty levels in a society can thus be high, but inequality levels in contrast, very low. South Africa of course is not in this position, as poverty is widespread and, as is well-known, we are the 2nd most unequal society on the planet after Brazil.

Why is this distinction important? It is critical particularly when one examines the role of economic growth in reducing poverty and inequality. The two are often conflated and it is implicitly assumed that they are one and the same. More pertinently, policymakers generally believe that economic growth will together reduce both poverty and inequality.

New international evidence on the link between economic growth, poverty and inequality however, challenges this claim. Rather than the process of economic growth resulting in a tangible reduction in inequality, the evidence seems to suggest that while there is a link between growth and inequality, the impact of growth has been to reduce inequality by extremely small quantities over very long periods.

Economic growth and inequality

For example a study by the World Bank revealed that the average rate of decrease in inequality was 0.3 Gini points (the standard measure of inequality) a year. This implies that it would take a highly unequal society such as South Africa, some 60 years to reach the lower levels of inequality found in the developed world. This means that to use inequality reduction as a measure of how the benefits of growth are being dispersed is problematic.

If we did so, the results would show that economic growth is doing very little to reduce inequities in the society, and so perhaps place into question the very role of economic growth in development. This is clearly nonsensical. Policymakers then need be very careful about using inequality as short-term or even long-term measure of the positive impact of economic growth.

Economic growth and poverty

In trying to assess the importance of economic growth to welfare enhancement, it is the impact on poverty that will yield more useful information. International evidence in this regard indicates that poverty levels are very sensitive to the process of economic growth. Put differently, this means that small changes in economic growth will have a fairly large effect on reducing poverty levels in a society. International evidence indicates that in India for example, a 1% increase in the growth rate caused poverty levels to fall by 3%.

In Brazil, a 1% increase in the growth rate resulted in a 1.5% drop in poverty levels in the society. The growth process therefore, will have significant and relatively swift impacts on poverty incidence in the society. In other words, economic growth is an extremely powerful medium through which to reduce poverty in a society.

Ultimately then, economic growth will not, in the long-run, provide for a major reduction in inequalities in South Africa. We are likely to remain a highly unequal society for some time to come. The opportunity that the growth process offers is to significantly lower the numbers of individuals and households that are living below the poverty line. It is precisely in being able to reduce this number that the results of long-term economic growth can be evaluated.