UNEMPLOYMENT / JOB CREATION IN SA

Milani, C.

Fedusa, E-mail: chez@fedusa.org.za

FOREWORD

Despite the job summit and related initiatives, our economy continues to yield jobless growth. In this special edition of the Fedusa Debate we aim to add impetus to the social partner debate on the question of job creation, by providing some views and insight into workable and available options at grassroots level.

Let us firstly learn from the job summit

While the job summit was a success in certain areas, it ultimately failed to stem unemployment and create sufficient jobs. This is due to the following five reasons:

1. Sufficient information was not made available. A prospective entrepreneur or employer should readily be able to access the following information:
- consumer needs in a particular geographic area;
- export demands;
- available resources; and
- available incentives.

2. A lack of coherent co-ordination. It is important that the left hand knows what the right hand is doing so that the necessary momentum and synergy is built up around the activities and programmes embarked on.

3. It is of no use if the leadership of the social partners debate and agree on issues without the matter going any further. At the end of the day it is the union members, public servants, small and big businesses and the community at large that will be required to give practical effect to what the social partner 'think tank' has come up with.

4. The implementation of any project or initiative at grassroots level must be managed properly.

5. Everybody must see the value of the project(s) and must want to get involved. No player should feel obliged to partake in any process to safeguard existing interests.

Fedusa believes that any of the above-mentioned areas may be addressed with reasonable ease should they be properly identified in the first place.

What should the job-creation framework look like?

Any job-creation project embarked on should be clustered around one of the following four distinct areas:
· basic needs;
· manufacturing;
· service; and
· technology.
Basic needs must be met

All South Africans must have access to food, water, a roof over their heads and clothes to wear. Each of these issues is inextricably linked to land and its redistribution. The situation in Zimbabwe is a clear example of what happens when land is not properly utilised or distributed.

Firstly, an extensive land reform distribution programme should be embarked upon, making use of large inactive tracts of government-owned land. Secondly, expropriation of land should take place at fair market-related prices. Land should only be allocated to persons who have the competence to productively farm the land as a result of past experience or training.

A situation must be avoided where land is distributed solely for subsistence farming, with no job creation taking place. The results of a land distribution programme should also be regularly monitored to ensure that the desired outcomes are being achieved at all times.

This land should be used to generate food for local as well as export markets. Farms should strike a balance between being labour intensive and mechanised, so that they do not become unproductive as technology improves. It should be kept in mind that the agricultural sector holds the potential to create many thousands of jobs.

Public works programmes, aimed at building houses, dams, roads, bridges and so forth, should be actively pursued. The community, especially in rural areas, should be central to such an initiative. Take Europe as an example: it was destroyed after the Second World War and was rebuilt while infrastructure and jobs were created.

Surely we can harness the same kind of approach and synergy in addressing our job-creation and infrastructure problems. We believe that labour-based jobs hold the answer.

Manufacturing

Many of our industries are shedding jobs at an alarming rate. The effects and result of globalisation, such as the opening up of markets and free flow of goods, can be blamed for much of this. The whole question of trade tariffs and the importing of inexpensive goods produced by cheap and exploited labour is clearly a bitter pill to swallow for many reasons, not least of all the closure of South African businesses and resultant job losses.

Whereas the tariff debate will continue, it is important that the social partners have concurrent and effective strategies relating to manufacturing.

We should answer the following questions:

1. Why do we export a wide range of raw materials and then import the processed products back into South Africa? Why don't we do more processing locally?
2. Are we providing a sufficient focus on niche markets? Instead of only trying to compete with countries which produce the cheaper line mass-market goods, we should focus on producing quality products, such as top-quality leather shoes, jackets, jewellery and machine components, to name but a few.
3. Is sufficient information being made available in relation to consumer needs, both locally and abroad? This fact is of vital importance in the focussing of production lines and the founding of new initiatives.
4. Is the entrepreneurial spirit and development of small businesses being sufficiently encouraged in South Africa? Eighty percent of the jobs world wide are found in SMMEs (small, medium and micro enterprises).
5. Should we not be placing a larger emphasis on building more reliance on co-operatives, especially in vulnerable sectors?

Service

Tourism has been correctly identified as a major source of job opportunities and revenue for South Africa. Despite this our service culture and professional approach to clients is weak. Many porters, waitresses or barmen think that they are doing you a favour, rather than performing their duty. As South Africans we should firstly not accept poor service, thereby raising the existing standards. Secondly, a major service-drive campaign should be embarked upon in this sector.

The public service is the largest employer in the country and this should not be changed. If financial considerations prevent employment levels from increasing beyond 1 100 000 employees, then this level should be maintained. More emphasis should be placed on service and efficiency, thereby enhancing the value added by the public service at all levels. The public service is the backbone of social service delivery. This important fuction should be enhanced rather than curtailed through restructuring and privatisation.

Hi-tech areas

Technology is here to stay and is becoming more advanced all the time. We need to consciously focus on information technology in its own right, and encourage its integration within all areas of business as far as possible. We need to develop our future engineers, mathematicians and scientists from an early age. This is the only way in which we would be able to integrate our activities in the global market place in a meaningful way.

Conclusion

It is important that we all know where we are going before we attempt to get there. If we aim at nothing, we will definitely achieve it each time and fool ourselves (and nobody else) in the process.

It is therefore proposed that focussed and practical discussions on job creation should take place in all earnest at the Presidents' International Investor Council. Focussed talks should also take place at Nedlac in conjunction with the Minister of Labour's fifteen-point plan.

The aim of this document is to focus the debate, consider South Africa's strengths and weaknesses and provide some building blocks and guidance for a result-yielding job-creation plan for South Africa.

Chez Milani
General Secretary

7 July 2000

BENCHMARKING SOUTH AFRICA FOR LABOUR-INTENSIVE DEVELOPMENT

South Africa ranks high in two fields, namely supply of labour and physical infrastructure. Concerning labour, the South African labour force of 16 million people is generally under-utilised and motivated to work.

The country's physical infrastructure, including telecommunications, the electrical power system and transportation infrastructure, is superior to most of its competitors' from developing and middle-income countries. The country also has well-developed capital markets.

These assets are formidable in comparison with many competitor nations and need to be emphasised and built upon as a source of competitive advantage.

South Africa ranks in the middle to competitive range in business costs such as electricity, rent and transportation costs. The country's power costs are competitive. Telecommunication costs, sea freight and wage costs are in the neutral range, being neither assets nor liabilities for developing labour-intensive industries.

South Africa is falling short in three competitiveness factor areas, namely: skills/productivity; management/labour relations; and the incentive structure. The country ranked at the bottom of all benchmark countries when looking at the productivity adjusted cost of labour (wages and salaries divided by value added in the manufacturing sector).

South Africa ranked low in management skills and the cost of management personnel, in comparison with many of its competitor countries. The country also ranked near the bottom in literacy rates, education and some of the other indicators of a qualified and skilled labour force. South Africa is not competitive in most measures of management-labour relations.

Finally, South Africa is very weak in the incentive structure it offers to investors. The benchmark countries typically offer a host of incentives, including the following: tax holidays for exporters; automatic duty-free imports for exporters; EPZs; and training grants and incentives in various forms.

These weaknesses or liabilities should become part of policymakers' checklist for action. In the short term the objective would be to neutralise them or minimise their adverse effects. Over the long term the objective could be to transform them into assets, making South Africa a very competitive site for economic development, including labour- intensive industries.

The Stanford Research Institute (SRI) conducted a SWOT analysis (strengths, weaknesses, opportunities and threats) for the development of labour-intensive development in South Africa. The summary of this SWOT analysis is presented on the following page.

STRENGTHS, WEAKNESSES, OPPORTUNITIES AND THREATS FOR LABOUR-INTENSIVE DEVELOPMENT IN SOUTH AFRICA

Strengths

- Abundant supply of labour.
- Natural resources.
- Good infrastructure.
- World-class companies in some industry segments (such as mining equipment and technology, infrastructure, construction, finance and information technology).
- Low real estate costs.
- Well-developed capital markets.
- Good climate.

Weaknesses

- Real or perceived low productivity of capital/management and labour.
- Low levels of literacy and numeracy in the work force.
- Strained management/labour relations in many sectors.
- A formerly closed and inward-looking economy shielded domestic companies from international competitive pressure.
- Insufficient incentives for investment, exports, training and the research and development of technology.
- Rising crime rates.
- High cost of capital.
- Insufficient institutional support of labour-intensive activities, especially investment promotion and export promotion in those sectors.

Opportunities

- New trade agreements create new market opportunities.
- Increased regional integration in Southern Africa allows specialisation and efficiency gains.
- Foreign direct investment and subcontracting form part of the world-wide business globalisation trend.
- Infrastructure and public works can stimulate employment while addressing equity issues.

Threats

- Further job losses if business, labour and government carry on as usual.
- Tariff reduction under the WTO schedule exposes unprepared domestic companies to international competition.
- Increased global competition from low-cost competitors (such as China, India, Pakistan and Malawi).

COMPARATIVE DEVELOPMENT FACTORS

The following development factors were used to compare South Africa to other countries (Chile, Malaysia, Ireland, Portugal, Korea and Kenya):

- the policy framework for labour-intensive development;
- institutional arrangements;
- tax incentives;
- labour availability;
- skills and training;
- the quality of the infrastructure; and
- international trade agreements and trade blocs.

The following lessons were learned from the comparisons made:

- Countries such as Chile, Korea and Malaysia demonstrated that labour-intensive development requires a solid and stable macro-economic environment. All those countries maintained stability in their public finances and balance of payments (at least until recently) and they generally kept inflation under control. Macro-economic stability served as a requirement for employment growth in these countries.
- In Korea, Ireland and Malaysia the goal of increasing employment (labour absorption) was the first priority. Labour-intensive industries were used by many of the newly industrialised countries (NICs) as a platform for further development. Following absorption of labour into the market, productivity improvements and tighter labour markets helped raise real incomes over time.
- The mentioned countries all placed major emphasis on skills development and productivity improvement as part of their strategy to compete in competitive world markets.
- Countries, including Korea, Malaysia, Ireland and Chile, identified target industries that offered the best prospects to meet their particular economic objectives. Incentive and promotion programmes were designed to encourage target industries or clusters. Development institutions promoted the target sectors in complementary ways.

Given the magnitude of the unemployment and under-employment problems in South Africa, job creation should become the single most important economic policy objective. In a similar vein, sectors which offer the best prospects for job creation should be given the highest priority in terms of government resources, incentive schemes offered, promotion programmes and cluster development strategies.

Sector or cluster-based action plans are the most suitable way to achieve the quick response needed to attain rapid employment growth. The following sectors should be selected and are listed in rank order in terms of short-term prospects for job creation within the South African context:

- tourism;
- construction / infrastructure;
- agriculture;
- furniture manufacturing;
- labour-intensive export manufacturing; and
- information service industries.

South Africa possesses the capability to combine its technical, management and financial strengths with the nation's largely untapped labour resources to develop internationally competitive activities to produce labour-intensive products and exports. This would address the twin challenges of generating new employment opportunities and diversifying the country's sources of export earnings. Achieving such an end is far from easy. Much of the economy is biased towards capital-intensive production due to policy stances, strained management-labour relations and other factors. Also, the tradition of labour-intensive production is limited.

Nevertheless, South Africa faces a unique situation - we have an economy with elements of both highly developed countries and developing countries - and this could be turned to the nation's advantage by stimulating labour-intensive growth, supported by advanced technology, management and corporate structures.

Success will depend on the degree to which relevant stakeholders - labour, business, government and non-governmental organisations - are able to build new opportunities through effective forms of co-operation. This is a key goal in South Africa, and is a requirement for successful employment growth.

What do potential investors look for when they are considering investing in a labour-intensive industry? What are the key factors that make some countries more attractive than others in drawing firms to their labour-intensive sectors? These are questions we must answer.

Based on investor surveys, the most important hosting factors for labour-intensive investment fall into the following six broad categories; namely human resources; costs; incentive structures; access to markets; capital resources; and infrastructure.

Cost is obviously a major consideration that affects the bottom line of business. It includes wages, purchased facilities or leasing, energy and other utilities, tax rates, telecommunication, transportation charges and more.

Another important factor is the availability, access to and the cost of capital. Infrastructure not only affects operating costs, but also travel time to markets, which is crucial for most manufacturing industries.

Human resources, which include both labour and management, are increasingly a key determining factor of investment location, particularly for labour-intensive industries. Similar to physical infrastructure, human resources are basically immobile.

In today's global economy, many manufacturing industries are considered to be 'footloose', ready to relocate anywhere in the world for the most skilled and 'best-value' labour force. International experience has shown that a productive and competitive labour force provides the strongest 'anchor' to labour-intensive industries.

Access to markets, particularly regional and international, is important for the development of labour-intensive sectors. Export markets hold great potential as a platform for economic take-off, as evidenced in the economic development experience of the Asian NICs as well as nearby Mauritius.

Finally, incentives, especially tax incentives for investment and export, are often considered important by businesses. While incentives alone are usually insufficient to attract investors to an otherwise undesirable location, they may become a deciding factor when a firm is considering two locations with similar attributes.

Labour force characteristics

South Africa's labour force is estimated at around 16 million, of which 55 percent are engaged in services, 31 percent in industry and 14 percent in agriculture. The size of its labour force places South Africa in the middle range among the benchmark countries (Brazil, Chile, Egypt, Greece, Ireland, Malaysia, Mexico, Portugal, South Korea, Thailand and Turkey).

While precise figures are difficult to obtain, estimates have put South Africa's unemployment rate at around 35 percent, which is the highest among all the benchmark countries. The magnitude of South Africa's unemployment becomes clear when compared to other countries. For example, Ireland's unemployment rate, the second highest among the benchmark countries, is only 13 percent.

While the high unemployment rate is a serious matter of concern to policy makers, it can also be viewed as strength for future labour-intensive industry development in that there is a large pool of labour that is available and motivated to find work.

Education and skills

The high national unemployment rate is aggravated by serious structural imbalances that exist in the South African labour market. While the number of unskilled and semi-skilled workers exceeds the number of jobs available, there is a shortage of skilled workers.

WORKERS AND MANAGEMENT

Wage levels in South Africa are average compared to the benchmark countries. South Africa's average hourly wage for manufacturing workers places it in the middle among competitor countries, lower than most European countries and the more developed Asian countries, and higher than the developing countries in Latin America and Asia.

However, the total wage bill is not only determined by the hourly wage, but also by productivity. While hourly wages per se are not high in South Africa, labour could be considered expensive when wages are adjusted according to productivity.

For labour cost at the management level, South Africa also ranks in the middle when it comes to annual compensation for a manufacturing director. Overall, cross-country comparisons showed that South Africa's labour cost is not an asset and is probably a liability.

This would imply that South African businesses might find it difficult to compete with low-wage countries (such as China and India) in mass-produced, light-manufacturing, labour-intensive products.

Comparing the labour's share of income generated in manufacturing across countries, South Africa came up the highest, exceeding those in both developing and industrial countries. This means that, for the same level of manufacturing output, labour accounts for a higher percentage of the total cost. This fact suggests that labour productivity in South Africa is below that of the benchmark countries.

Relatively high wages in South Africa, adjusted for productivity, could raise labour costs relative to output. A high employment level in South African manufacturing enterprises could also boost total wage earnings as a percentage of value added, raising unit labour costs and reducing output per worker.

Productivity of management and labour

It is very difficult to compare labour costs without considering productivity, as the two are intertwined in determining cost competitiveness. Productivity is an extremely contentious subject in South Africa. Businesses often blame their poor performance and their lack of competitiveness solely on labour productivity, while labour groups frequently view the productivity issue as an excuse for further job shedding, wage freezes or aggravating 'sweat shop' conditions.

In an effort to develop a constructive debate, a broad interpretation of the term 'productivity' should be taken to include not only labour productivity, but also productivity of capital and management.

Theoretically, the best measure of productivity is total- factor productivity, which includes labour and capital as factors of production. However, data on fixed capital stock for various countries are very limited and often not available at all, making cross-country comparisons extremely difficult.

Short of that, the best available and most often used proxy for comparing labour productivity across countries is the value added per employee in the manufacturing sector. South Africa ranks fourth from the bottom among the benchmark countries in value added per manufacturing employee, behind countries such as Mexico, Turkey, Brazil, Thailand, South Korea and Ireland.

Perhaps more importantly, productivity gains on average were minimal in South Africa in the 1990s. This is reflected in the real average growth rate of per capita manufacturing, value added, in 1990 to 1995.

In contrast to South Africa, countries that enjoyed high rates of economic growth during this period (Thailand, Malaysia, Ireland, South Korea and Chile) attained much higher average increases in per capita manufacturing, value added, than South Africa, ranging from five to 11 percent.

While the value-added comparison suggests that labour productivity in South Africa could be improved, this assertion could be misleading because it implies that any improvements in productivity is attributable to the efforts of labour alone.

In reality, an increase in labour productivity reflects output gains from many inter-related factors, including the following:

- the efficiency of employees;
- employees' attitudes and skill levels;
- the incentive system used to motivate employees;
- investment in machinery and equipment;
- technology levels; and
- the organisation of production systems.

All these factors could again be traced back to management's effectiveness.

Since the mid-1960s, gross domestic fixed investment as a share of GDP in South Africa has been in decline. The principal reasons for this have been the international drive towards divestment during the 1950s and 1980s and, more recently, the low levels of business confidence.

Declining investment means that machinery, equipment, technology and the organisation of production have not been receiving the kind of upgrade and efficiency improvement which allow labour productivity to rise. Thus, lagging investment by businesses and the causes thereof should be examined when labour productivity is considered.

Labour productivity is also affected by the way in which the production system is organised and managed. Labour is not the only side that needs training. Management also needs training, particularly in organising production more effectively, improving quality, motivating and supervising workers more effectively, communicating with employees and managing relationships with workers better.

While some South African companies are world-class competitors and extremely advanced in management and technology, others have yet to catch up with international best practices and adopt modern management methods and production systems.

This can largely be attributed to the closed economic system and international isolation in which many South African businesses had operated in the past. However, increased exposure to international market pressure will increasingly require businesses to modernise their production and management systems in order to be competitive in the world market. Such management improvements will also allow labour productivity to rise.

Multi-shifting in production is not commonly used in South Africa in many labour-intensive industries. The use of more than one shift usually has the advantage of reducing overhead costs, thereby lowering per-unit costs and making products more competitive.

It theoretically also allows employers to compensate workers better due to the cost savings in the overhead items. There are cases in which multi-shifting was abandoned because the employer refused to compensate the late-shift workers for their additional transport costs or make allowances for health and safety considerations.

A commonly used incentive system, namely the use of productivity wages, such as piece rates in labour-intensive manufacturing sectors, has not been widely adopted in South Africa.

In certain labour-intensive industries, the use of piece rates instils an atmosphere of fairness among employees and is an excellent motivation for workers to be as efficient as they can. Another advantage of the piece-rate system is that since compensation is essentially based on output instead of input (time), it allows the employees to be responsible for their own work, fostering a more businesslike relationship between the employer and the employee.

The piece-rate system obviously works better in some sectors than others, and cannot be used in certain industries at all. Generally it is more suitable for sectors in which production phases can be compartmentalised.

The slow adoption of some of these standard industry practices to motivate workers and increase productivity (such as piece rates and multi-shifting) in South Africa is partially due to the often acrimonious relationship and suspicion between management and labour, which creates inflexibility on both sides.

Management tends to blame labour for production that is not competitive enough, and labour tends to view changes in the incentive structure or production system as new means of exploitation. In this kind of environment, improvements in management-labour relationships and the building of trust between the two parties can go a long way towards establishing mutually beneficial arrangements that would increase productivity, wages and business competitiveness.

Manager-labour relations

The current state of management-labour relations in South Africa is perhaps the most serious obstacle to a dramatic increase in labour-intensive employment in the country. Overall, the state of management-labour relations in South Africa is characterised by suspicion at its best and hostility and conflicts at its worst.

Strikes and work stoppages represent real costs to businesses and the mere perception of poor labour relations often deter international investment due to the uncertainties involved.

There is also anecdotal evidence that some businesses are increasingly investing in labour-saving technology, even when it is not the most cost-effective, due to the desire to reduce the so-called hassle factor related to managing labour relations. This, if confirmed, could be an alarming trend that works against the country's current need for expanding labour-intensive employment.

INCENTIVE STRUCTURES

The investment incentives offered by South Africa are in the lower to middle range among the benchmark countries. Incentives are an important attraction factor in labour-intensive industries such as export-oriented clothing manufacturing, electronics assembly or tourism.

The six-year tax holiday offered by South Africa to investments that meet the three requirements (namely spatial, industry and human resource components) are more generous than in countries that do not offer tax holidays (such as Chile, Portugal, Turkey and Mexico).

However, the countries that offer partial or total corporate tax exoneration generally grant it for eight to ten years when extensions are included. This includes ten years in South Korea, eight years in Thailand, ten years in Malaysia, and a reduced corporate tax of ten percent until the year 2010 in Ireland. Most countries have priority regions or industries for which tax incentives apply.

Several European countries in the benchmark offer very generous grants for strategic investments. In particular, Greece, Portugal and Ireland offer some of the most generous capital grants in the European Union.

Greece provides grants of up to 60 percent of project investment (including EU matching grants) in priority sectors, which include mining and high-income tourism among other industries.

Portugal offers cash grants of up to approximately US$1.7 million to companies in non-manufacturing investments. The country also offers five to seven-year interest-free loans of up to approximately US$3.2 million per company as an incentive for manufacturing investments. Portugal targets tourism projects in most parts of the country.

In Ireland, grants for fixed assets may be negotiated up to a maximum of 60 percent of cost in designated under-industrialised areas and up to 40 percent in most other areas.

Increasingly, countries that have signed customs union agreements with the EU are shifting their incentive regimes from sectors to regions, mainly to alleviate regional imbalances and to address high employment in economically depressed areas. In many cases, regions and provinces in Europe and north America offer their own tax incentives (in addition to national programmes) to retain or attract target industries and companies.

Regions and provinces (or even countries in the United States) have the flexibility to negotiate incentive packages with investors on a case-by-case basis. These packages often include tax incentives, infrastructure improvements, training assistance, one-stop-shop assistance in obtaining permits and approvals.

A variety of other investment incentives are offered by the benchmark countries, including the following:

- accelerated depreciation (for example in Thailand, Brazil and Chile);
- tax credits and other incentives on using technology or conducting research and development (for example Ireland, South Korea, Malaysia and Brazil);
- subsidised energy provision (for example Turkey and Malaysia); and
- double deductions on water, electricity, and transport costs (for example Thailand).

South Africa's investment incentives are considered weak compared to many of the benchmark countries and others outside the benchmark.

Job-creation incentives

Among the benchmark countries, Ireland offers the most comprehensive and generous job-creation incentives. The Industrial Development Authority of Ireland offers cash grants towards the cost of fixed assets for new industrial investments based on job-creation incentives. Usually 50 percent of the agreed amount per job is paid once the job is created.

Special incentive packages are also negotiated on a case-by-case basis for larger and more capital-intensive projects, usually based on the number of workers employed. In 1996 the Irish government began offering, under the 'Job Start' programme, 80 Irish pounds per week to employers who hire persons who have been unemployed for more than three years.

In Greece, job targets are also established for investments exceeding a certain size, which are seeking government grants. In Mexico, companies generating additional employment are allowed to credit an amount equal to 20 percent of annual minimum wages against their income tax (or asset tax) for each additional job created. In most non-European countries in the benchmark, job creation per se is not always a pre-condition for granting investment incentives. Countries that seek to stimulate job growth in certain underdeveloped, under-industrialised or high-unemployment regions often designate those areas as high-priority regions for granting investment incentive approvals.

However, in cases where regional incentives are negotiated on a case-by-case basis, the anticipated number of jobs created is often one of several determinants of the magnitude of the incentives granted.

Most benchmark countries have also not targeted labour-intensive industries per se for employment generation. More commonly, countries tend to focus on attracting investment in the following sectors:

- high-tech industries such as information technology and software development;
- strategic sectors such as mining and public utilities; and
- emerging, value-adding sectors such as paper products, food processing and high-income tourism.

It should be noted that sector-targeted investment incentives in most countries are co-ordinated with their macro-economic objectives to address their unique national economic conditions.

In countries such as South Korea, Malaysia and Thailand, where national unemployment is not the principal economic issue, investment incentives are often designed to attract technology and infrastructure upgrade in order to improve productivity and dynamic competitiveness.

Training incentives

Training incentives are quite common among the benchmark countries and these come in different forms, such as tax incentives, training grants and subsidies. In Portugal investors may also apply for separate cash grants to cover up to 90 percent of training expenses.

In Ireland grants are available to cover trainee wages for workers stationed in Ireland and for travel, wages and living expenses of workers trained abroad. Chile offers incentive schemes for apprenticeships for young people in addition to allowing companies to deduct training costs from their corporate income tax (up to one percent of the tax).

In Malaysia a double-cost deduction is granted to firms that enrol their employees in Ministry of Finance-approved training institutions or in other approved training programmes.

World wide the trend in both industrial and developing countries is to offer training subsidies, grants and tax incentives to induce companies to provide more training voluntarily. To date South Africa has not offered training incentives similar to those described above. The training levy being considered in South Africa is essentially a new tax to finance training and is not comparable to a tax deduction, which is a financial incentive for firms to spend more on training.

Export Incentives

Most of the benchmark countries offer duty drawback or duty exemptions on machinery, equipment, raw materials and other inputs used to manufacture export products. It should also be noted that, in most countries, duty drawbacks are usually more automatic, more streamlined, less onerous and more widely used than in South Africa.

In South Africa the criteria for duty drawbacks are complicated since they are not only linked to exporting performance, but also to training performance. None of the benchmark countries used labour training as one of the criteria for granting duty drawbacks.

Many countries provide additional tax incentives to encourage exports. Thailand, for example, grants up to three years of tax holidays to firms that export at least 80 percent of their production. Ireland, Chile and Thailand, among other countries, provide exemptions from VAT for raw materials and intermediate goods imported by companies that export most or all of their output.

Chile also offers a three to ten percent subsidy on export items that are considered non-traditional exports (products of which Chile exports less than $18 million worth). Exporters in Turkey can apply for special discounts for electricity, natural gas and water used in the production of export goods.

Malaysia allows a double tax deduction on expenses incurred by companies seeking export opportunities in manufactured or agricultural products. These incentives are more generous than those currently offered in South Africa.

Since most of the benchmark countries belong to the World Trade Organisation (WTO), their export incentives eventually will have to comply with commitments under the WTO. However, countries that have developing-country status are allowed to reduce their export subsidies and incentives over a longer time period than South Africa.

EXPORT PROCESSING ZONES (EPZs)

While Greece does not have official EPZs, it has several free zones for warehousing and light manufacturing. Ireland does not offer EPZs, but provides incentives to exporters similar to those in EPZs, such as low tax rates and duty exemptions.

Typically, EPZs provide automatic duty-free imports of machinery, equipment, raw materials and supplies. Exemption from value-added taxes and other national taxes, express customs clearance, freedom in conducting foreign exchange transactions and multi-year tax holidays on corporate income tax.

National investment laws and labour regulations typically apply and are enforced in the zones. Many successful exporting countries have used EPZs and FTZs (foreign trade zones) to jumpstart their export sector, particularly when the regulatory and incentive structures in the rest of the economy have not been streamlined.

ACCESS TO MARKETS

With a 41-million strong population, South Africa has the advantage of a large internal market for its products. Most observers would agree that in order to jumpstart an expansion in labour-intensive employment, South Africa must increasingly look to export markets for growth.

Currently, the country's largest export market is the United States, followed by Zimbabwe, Japan, Germany, the United Kingdom, Taiwan and Mozambique. Exports to Europe mainly consist of agricultural goods, mining products and processed goods. Principal exports to North America are metal products, chemicals and tobacco products. Japan is a major importer of South African metal products and leather products.

Recently there has also been a substantial increase in exports of transport equipment - export sales doubled - mostly in railway locomotives and aircraft. South Africa's largest export markets for transportation equipment are currently Taiwan, the United States and Malaysia.

CAPITAL RESOURCES

South Africa's financial sector is highly developed, with sophisticated capital markets and a first-world banking system. The Johannesburg Stock Exchange (JSE) is the world's tenth largest stock exchange in terms of market capitalisation and is an important source of raising capital in South Africa.

Despite the depth of the financial markets, South Africa’s financial sector has not provided sufficient investment to stimulate economic growth.

CONCLUSION

It is vital that the social partners focus on exploiting South Africa’s strengths and opportunities, while at the same time limiting and ultimately eliminating the country’s weaknesses and threats. It is clear that the job crisis will not be addressed if business, labour and government carry on with “business as usual”.

LABOUR-BASED METHODS INCREASE EMPLOYMENT

Labour-based methods increase employment and stimulate the economy. One important reason behind this fact is that labour requirements vary tremendously with different technological approaches.

For example, when equipment-intensive construction methods are used in an average kind of gravel-road project in low-wage countries, the cost of equipment amounts to 80 to 85 percent of the total project cost, with a wage bill of 10 to 15 percent.

If, in the same project, labour-based methods are used, the cost of equipment would amount to 30 to 40 percent of the total project cost, while the wage bill would account for 40 to 60 percent for the same quality of output. Moreover, in such countries labour-based methods usually are cheaper.

Furthermore, while equipment-based construction employs primarily small numbers of skilled and semi-skilled labour, the labour-based options additionally employ large numbers of unskilled people, contributing to job creation for the very poor.

Therefore, for a comparable level of investment, the labour-based approach transforms a greater part of the investment into cash incomes for people, instead of into equipment, spare parts, fuel and foreign expertise. Cash incomes then stimulate households' consumption and the local economy.

When the volume of labour-based projects becomes large - say about ten percent of the total investment in infrastructure - this can have a measurable impact on the national economy, as evidenced by a macro-economic study carried out in Madagascar in 1995 (footnote 1).

The study compared the impact of the ongoing labour-based programmes to that of equipment-intensive programmes in respect of key economic variables: cost, foreign exchange expenditure, job creation and household consumption. It found that the impact of using labour-based methods on the national economy was measurably and significantly positive.

When the income of households exceeds what is needed for basic consumption, then there is a possibility of savings and paying taxes, i.e. of gradually expanding the local and national capacity for investment.

A similar study (footnote 2) in the Philippines concluded that the wider and improved use of labour-based, equipment-supported methods in three government departments dealing with infrastructure would result in the creation of between 150 000 and 260 000 additional full-time jobs in 1999.

Employment and investment impact of technologies

Gravel roads Equipment-based Labour-based

Total cost (index = 100)* 100 70 - 100

Foreign exchange 100 40 - 90
requirement (index = 100)

Employment generated per 100 200 - 400
unit of investment (index = 100)

Equipment cost as a percentage 80 - 85 30 - 40
of total cost

Labour cost as a percentage 10 - 15 40 - 60
of total cost

* wage rates between $1 and $3 per day

Less measurable additional social benefits

An important side-effect of labour-based methods in rural areas is to increase the flow of money through rural economies, a pre-condition for diversifying out of agriculture. Income earned by local workers (non-existent in equipment-intensive investment) creates additional demand for other locally made products, thus generating indirect employment.

The number of indirect jobs created can range between one and a half to three times the number of directly generated jobs (footnote 3). If the choice of infrastructure includes productive infrastructure such as electrification, irrigation and telecommunication, and if this is accompanied by an expansion in means of transport, then growth becomes a very real possibility.

The introduction of simple planning methodologies is essential in this context. These would include methodologies that would enable communities and district planners to objectively decide on the infrastructure priorities in their areas and to use available investment in an optimum manner.

Many other positive effects can result from a policy decision to adopt labour-based methods. Firstly, elaborating the policy can bring the government departments, which are responsible for labour and economic planning, together with the technical departments in deciding how to link up economic and social policy.

Secondly, if the promotion of the private sector is part of government policy, then the adoption of labour-based methods as a technical option, along with targeted procurement, will expand the domestic construction industry and make it more dynamic. (Targeted procurement is the modification of the tendering system to give small and medium contractors a chance to obtain public investment contracts.)

Thirdly, in the process of strengthening the capacity of small and medium firms to manage a large workforce, they are introduced to the relevant labour standards. This is again done through the contract system: by introducing socio-economic objectives and conditions into the tenders, contractors are encouraged to work in a socially beneficial and responsible way.

As a result, a much wider group of people, the rural and urban poor who provide their labour, get to know and enjoy their basic rights as workers.

Self-reliant development

Moreover, where a decentralisation of authority and funds to local authorities is in operation, labour-based methods make it possible for local institutions and communities to take the initiative in solving some of their problems, and to acquire useful technical skills as well as skills in project financing and management.

All in all, adopting the labour-based approach to investment introduces the capacity for self-reliant development that is sustainable.

To fight urban poverty, the creation of productive employment and the improvement of infrastructure in deprived urban areas are essential. Most of the following basic infrastructures needed in poorer urban settlements can be built and maintained by labour-based methods:

- drains;
- service roads;
- pathways;
- water supply;
- latrines;
- bridges;
- erosion control structures;
- urban forestry; and
- street paving.

When the work is done by small local contractors or contracted to the communities concerned, it brings community organisation, technical and managerial skills into the community. The perception is growing that employment-intensive improvements of settlements, and projects to move the urban informal sector towards mainstream economic activity, can be very much one and the same thing.

Labour-based methods: too important to overlook

In conventional thinking, infrastructure is about physical assets and rates of return on investment, i.e. whether and how soon they can be expected to pay for themselves. Investment decisions are taken without asking which technology is to be used to carry out the projects. It is simply assumed that there is only one way to build.

A much broader perspective on infrastructure investments should, however, be taken. Labour-based infrastructure investments have come to represent another point of entry into the world of work, through which to introduce the key ILO concerns of this decade, namely job creation, workers' rights, social protection and social dialogue.

For governments and their populations, the adoption of labour-based approaches represents a concrete opportunity to make infrastructure investments yield a wide range of returns. The scale and diversity of infrastructure needs represent work for many people for many years. The large flows of money going into the infrastructure sector represent a huge potential source of income for a population.

By systematically making an informed choice of technology, more and more governments are giving themselves the means by which to link their economic and social policies. Countries such as Cambodia, China, India, Mozambique and the Philippines have all adopted the labour-based approach as part of their economic and social investment policies.

For low-wage countries confronted with transitory or structural underemployment or unemployment, and needing to expand national wealth on a steady and sustainable basis, labour-based methods are simply too effective a policy tool to be neglected.

Labour-based construction sites can be places where people acquire life skills

Advantages of the local resource and labour-based approach to investment

• It creates jobs for large numbers of unskilled and some skilled labour directly, and indirectly through backward and forward linkages, such as consumption and increased output and subcontractors. For each person directly employed, one and a half to three are employed indirectly.
• It acts as an entry point for ILO concerns. 'Core' labour standards are put into practice (such as non-discrimination, freedom of association, equality, workers protection and minimum wage) and communities are helped to organise (such as farmers' or women's groups and others).

• It is self-targeting - it attracts the poorer people.

• It produces quality outputs that are as good as those achieved with equipment-based technology.

• The emphasis on maintenance contributes to sustainability of the productive resource base and of the assets created.

• It is more cost-effective than equipment in low-wage, labour-surplus economies.

• The technology can be used in places where equipment cannot.

• It contributes to economic growth and improves the distribution of income.

• It helps to ease the balance of payment constraints, while increasing household consumption and national income.
• It saves foreign exchange and reduces debt.

• It trains unskilled / semi-skilled workers up to professionals such as engineers.

• It helps to promote small contractors and enterprises.

• It develops a sense of ownership in local communities that is lacking when equipment-based methods are used.

• It lends itself well to community initiative and management, and so enhances democratic participation.

• It opens up the way for a social dialogue on linking economic and social policy.

• It is environmentally friendly.

Reaching the potential

Maximising the economic and social efficiency of infrastructure investments requires that certain obstacles to an employment-intensive approach be removed, freeing the public and private sectors to use this approach whenever it makes technical and economic sense to do so.

Given that governments, donors and financial agencies are responsible for the bulk of investment in infrastructure, they are the ones who carry the responsibility for technology choice, and for the greater or lesser impact of investment on the productivity and well-being of the populations concerned.

To maximise this impact, they firstly need to remove the biases that act in favour of equipment and against people. These biases include the following:

• Macro-economics
For example, overvalued local currency or negative real interest rates favouring borrowing in order to buy equipment. These biases mask the real cost of imports and make them seem cheaper and more competitive than they really are.

• Donor-induced
For example, insistence on importing equipment duty-free, financing only foreign costs or 'tied procurement to the donor country', insistence on international competitive bidding or selecting contractors from the donor country or pressure for fast delivery. These compel the recipient country to repatriate or export the investment or they exclude small domestic firms from obtaining construction contracts.

• The wrong perception
The wrong perception that labour-based approaches are slower, more expensive and produce low-quality outputs.

• Resistance to change
The traditional equipment-based methods are better known, appear easier and provide more possibilities of corruption to a selected few powerful suppliers and contractors.

Constructive measures

To remove these biases and help countries to attain their potential, which had long seemed out of reach, the following is recommended:

1. Cost-benefit analyses of investment projects should be carried out for different technological options, using market interest and exchange rates.

2. Donors, funding agencies, governments and social partners insist that whenever cost-benefit analysis favours labour-based approaches over equipment, infrastructure projects be carried out by local firms, using labour, with capacity building included as necessary.

3. Development banks and donors insist less on international competitive bidding and fast delivery when labour-based implementation of a project will produce the same physical output within a reasonable time frame with social benefits and similar or lower costs.

4. Governments, workers' organisations and contractors as well as donors collaborate with the ILO to raise awareness of the more widely spread benefits of adopting a labour-based strategy to infrastructure investments.

MENTORSHIP EMPOWERMENT SCHEME

It is proposed that a mentorship-empowerment scheme be discussed, agreed to and subsequently implemented. This scheme will aim to create jobs in South Africa by establishing business opportunities through successful joint ventures between proven entrepreneurs (mentors) and retrenchees/unemployed via competent empowerment groups. This is, inter alia, intended to support the redeployment strategies of the social plan.

The social plan

The Declaration of the Presidential Jobs Summit in October 1998 was the direct result of an agreement reached through labour, business and government at Nedlac. It provided a framework for a social plan that aims to prevent job losses and a decline in employment where possible, and seeks to manage retrenchment and reduce its effects on individuals and local economies. The Department of Labour formally issued the framework as a White Paper during 1999.

The social plan envisages the following three phases:
- proactive phase - preventing job losses through 'turn-around' or 'redeployment' strategies;
- reactive phase - managing retrenchment through counselling and retraining retrenchees; and
- growth phase - creating new jobs through local economic development.

These initiatives are closely linked and will be co-ordinated through a proposed national social plan committee.

The Social Plan Technical Support Facility (SPTSF) has, inter alia, been tasked with developing 'turn-around' and 'redeployment' strategies for selected industry sectors and enterprise Future Forums participating in the social plan.

This includes state-owned enterprises such as Transnet, Eskom, Telkom and Denel, which have indicted that they intend implementing a retrenchment process over the next three to five years.

Involvement of state-owned enterprises in the social plan

State-owned enterprises, such as Transnet, Eskom, Telkom, SABC and Denel, are involved in the social plan to a greater or lesser extent, depending on their envisaged retrenchment programmes. Other organisations, such as SAB, have also indicated their strong support of the social plan.

During March 2000, a separate social plan task team for state-owned enterprises was formed under the joint leadership of the Department of Labour and the Department of Public Enterprise. This process has been endorsed at the Inter-Ministerial Cabinet Committee level.

Discussions with Transnet around its social plan centres and retrenchment procedures, highlighted the hidden costs such as bitterness associated with retrenchment and the possible long-term negative associations that retrenchees and their extended families would have about Transnet.

The question around the possibility of providing alternative jobs for retrenchees through a redeployment strategy was raised, and what such a strategy would look like and how it should be implemented.

To be effective, drastic approaches to developing 'redeployment' strategies are urgently needed. Members of the social plan task team for state-owned enterprises have requested the National Productivity Institute (NPI) to have these social plan processes established before September 2000. It is important that social partners are fully aware of this initiative and that they provide the necessary support.

Mentorship empowerment

The first phase of the social plan is concerned with preventing job losses through turn-around and/or redeployment strategies (pro-active phase). During this phase the opportunity cost of having people unemployed should be considered.

This is a typical local optima / global optima trade-off: individual firms may improve their bottom line profitability through retrenchments, but to the extent that meaningful alternative employment is not found, the country as a whole will certainly be worse off.

There is considerable pressure on large well-established companies to become globally competitive, and the public sector to become leaner. In the short and medium term this will continue to translate into an uncomfortable shift in employment patterns from the larger corporate institutions and the public sector to SMMEs (small, medium and micro enterprises) and the informal sector.

Despite national initiatives, such as Ntsika and Khula, which concentrate on developing the small and medium enterprise (SME) sector, the estimated failure rate of SMMEs within the first three years remains between 70 percent and 80 percent, and South Africa continues to have an untenable rate of unemployment.

Given the urgency of its task, the social plan cannot rely solely on the traditional initiatives to develop SMMEs as a redeployment strategy. It needs to focus on the mechanisms to create sustainable jobs in this target sector. This should include promoting franchising opportunities, business linkage programmes, such as Danida and Sida, and joint ventures with corporate institutions and the public sector.

National wealth is created at the level of the firm. To develop redeployment strategies necessitates a strong partnership with the private sector. Furthermore, target growth sectors, such as tourism and its related sub-sectors (hotels and leisure), the service and retail sectors and niche manufacturing, should, inter alia, be considered as opportunities for redeployment.

The NPI has been involved in preliminary discussions with a number of institutions and individuals and all of them have indicated their strong support for the proposal. These institutions and individuals include:

- South African Breweries (project Noah);
- Deloitte and Touche's Business Beat;
- entrepreneurs such as Mr Taki Xenopoulos (chairman of Fontana Holdings) and Mr Brand Pretorius (chairman of McCarthy); and
- business leaders such as Mr James McLuckie from the Institute of Marketing Management.

Potential job opportunities at this early stage (from franchising bakeries, chicken outlets and reviving the Mabaleng concept alone) are estimated to be approximately ten thousand over five years. This estimate is based on each franchise creating direct employment for approximately 25 people. In addition, direct marketing and other opportunities provide an enormous potential for employment.

The intention is to extend the concept to a wide range of industries, including assembly operations in manufacturing. The common vision is to provide sustainable job opportunities through a mentorship process coupled with training to build capacity around best practices.

According to South African Breweries (project Noah), the average cost of creating a sustainable job is approximately R30 000. This is in line with overseas experience.

Proposal

1. Transnet, Telkom and other state-owned enterprises have indicated that they are looking to implement retrenchments over the next five years.

2. It is accordingly proposed that a social plan venture capital fund be established with the primary objective of creating sustainable job opportunities through a mentorship process coupled with training to build capacity around best practices, while retaining its capital base and covering the management fee.

The objective is not to make super profits by competing with private equity funds, but to develop sustainable jobs.

3. It is further proposed that a mentorship round table be formed which would interact on a regular basis to generate projects providing job opportunities. Mentors should be amongst the top entrepreneurs in South Africa with a proven track record.

There should be incentives for both the mentor and the empowerment group to establish the new business opportunity as a joint venture. This formula of empowerment, delivery and sustainability should ensure at least 80 percent probability of success during the first three years of the operation of any project.

4. The following broad criteria should apply:

a. The fund should be guaranteed by the affected state-owned enterprises, and managed as a joint venture between government, labour and private enterprise.
It is proposed that the development fund should be jointly managed by:
- a public institution such as Khula or IDC;
- a private institution such as Gensec, which has a proven track record in this area (it is currently managing development funds of approximately R2 billion); and
- the National Productivity Institute (responsible for implementing turn-around and/or redeployment strategies as part of phase 1 of the social plan).

b. Sustainable employment opportunities should be aggressively sought through the mentorship round table. Jobs should have a high probability of being sustained for at least three years (preferably five years or longer).

c. Employment opportunities and funding should be made available to potential retrenchees through an enterprise future forum as part of its redeployment strategy.

d. The Department of Labour or appointed consultants should manage the process of application and selection for recruitment into each project, with complete consensus from all parties.

5. The requirements for a venture capital fund is estimated at R12 000 per sustainable job over five years. In other words, a mentorship-empowerment venture capital fund of R200 million would create opportunities for approximately 16 000 people over five years and 32 000 people over ten years.

If it is well managed, the capital base should remain intact and the cost of managing the fund should be recovered from the beneficiaries. It is important that the fund's performance should be assessed on jobs created and not on super profits - it should not compete with private equity funds.

Although the risk of each investment would obviously be assessed, this fund should allow for entry into higher risk projects

The social plan centres would provide information on job opportunities created through the mentorship-empowerment scheme and would track the involvement of enterprises participating in the process. It is proposed that an academy be established to provide specialised training for the different schemes in conjunction with existing entrepreneurial development programmes.

CREATING JOBS THROUGH SMMEs

The world of work is changing. Government and big business were previously the main source of jobs, but this has changed. Privatisation, restructuring and down-sizing have taken root in the workplace, resulting in people losing their jobs.

Machines and computers have now replaced workers who were previously used in manufacturing and production processes. All this points to one thing - further job losses on an unprecedented scale - unless something is done.

Where does the answer to this problem lie? Many people would say that the answer lies with the small, medium and micro enterprises (SMMEs). Eighty percent of jobs world wide are created through SMMEs. SMMEs have previously been identified as a job-creation vehicle in the South African context, but not much has happened in this regard, raising the obvious question - why not?

South Africans generally have a lukewarm attitude to SMMEs. It is now time for South Africans to change their mindset away from focussing on one grand idea, the perfect solution, to a life revolving around many little activities and aiming to get as many as possible of these activities right. Such people are called entrepreneurs and their activities result in the creation of jobs.

We must learn from the experience of other countries. California is a good example. In 1990 the US government cut back on defence spending and this resulted in about 500 000 jobs being lost over two years.

California has very few natural resources, little water and the occasional earthquake. Measures to address the job losses were immediately put into place to stimulate small businesses and recreate the 500 000 lost jobs in three years. California has created 1 000 000 jobs since 1995 - all through small businesses.

The most critical issue for a small business is access to capital. The US State government operates a credit guarantee scheme, providing the required money for Californian businesses. California also has 2 500 venture capital companies, which specialise in investing in small, micro and medium enterprises. The entrepreneur contributes the idea and time, and the venture capital company the money. The profits are split on a fifty-fifty basis.

Many South Africans have not even heard of venture business with simple flotation rules, minimum transaction costs, Internet stock brokers and trading. It costs R500 000 to list on the Johannesburg Stock Exchange (JSE) and flotation rules for small and big businesses are the same.

Government must put the necessary tax incentives in place to make risking capital worthwhile. Small business should also be exempt from unnecessary permits and red tape. In short, life should be made easier for SMMEs, not harder.

Government and the educational system should aggressively encourage the development of entrepreneurs. In South Africa we must change our attitude and should stop looking down at people such as the corner café owner. We should rather realise that small business is a key cornerstone of job creation and economic growth in this country.

REFERENCES

International Labour Office Geneva. Employment-intensive investment in infrastructure: Jobs to build society.

Economics Practice SRI International. Benchmarking South Africa for Labour-Intensive Development. January 1998.

Clem Sunter, Anglo American Corporation, Gillian Godsell, CPS research associate. Centre for Policy Studies. CPS Policy Forum. December 1999.

Footnotes

Footnote 1
L'Approche á Haute-Intensité de Main d'Oeuvre (HIMO: une opportunité pour Madagascar.
Essai de cadragemacro-économiuq. Réflexions sur le développement, Document de discussion n°18.
Département des politiques du développement, BIT/ILO, Genéve 1997.

Footnote 2
Study on the potential expansion of labour-based, equipment-supported infrastructure programmes in the Philippines. ILO/ASIST Asia-Pacific and the Development Academy of the Philippines, Manila, December 1998.

Footnote 3
Of nets and assets, a study on effects and impacts of employment-intensive programmes, Willem Keddeman, ILO Geneva, 1998.

Acknowledgements

Dr Dudley Jackson - NPI
Mr Karl Gostner - Nedlac