Inequalities in emerging economies: What role for labour market and social policies?

The Organisation for Economic Co-operation and Development (OECD) held a one-day workshop in Paris in May 2010 to present the findings of a series of papers commissioned on this topic from Brazil, India, China and South Africa. KATE PHILIP was there.

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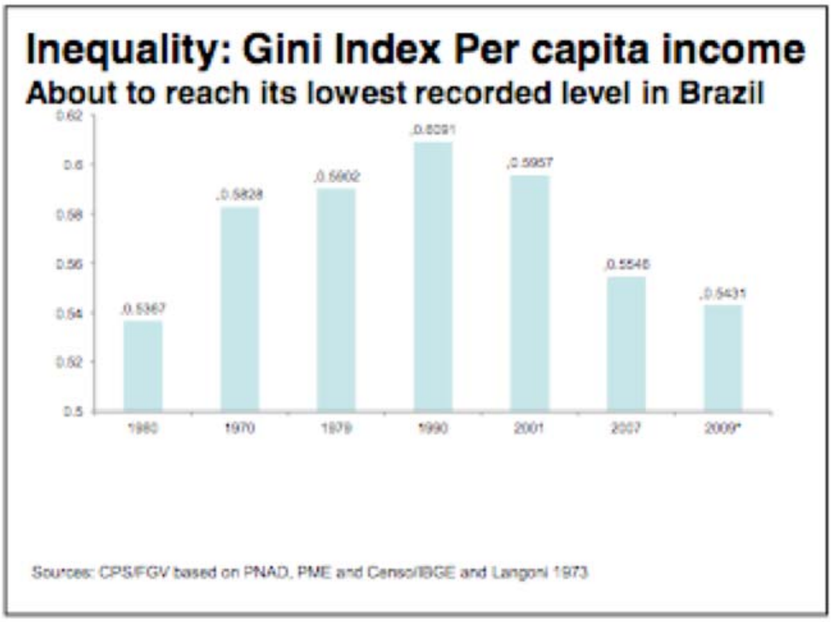
For South Africans attending the OECD conference, watching the comparative slides on global trends flashing up on the screen is a bit like attending a performance review that you know you have failed.

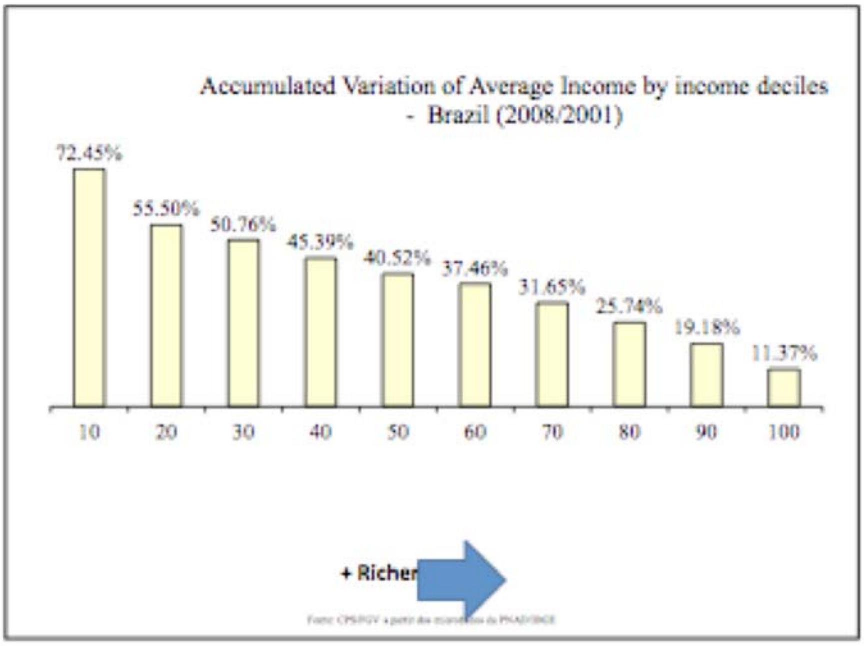
'Inequality got *worse* since the end of apartheid? What happened?' asked an incredulous panelist. The South Africans present looked contrite.

By contrast, Brazil has reversed its trend of rising inequality for the first time since they started to track inequality in 1960. 'People had come to think of rising inequality as a natural state of affairs, as how thing are,' explained Brazilian panelist Marcelo Cortes Nero; 'Now it is clear policy action can make a difference.'



From Neri, presented at the Conference

Even more dramatic is the decomposition of this outcome by income deciles from 2001 - 2008:



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So, what happened?

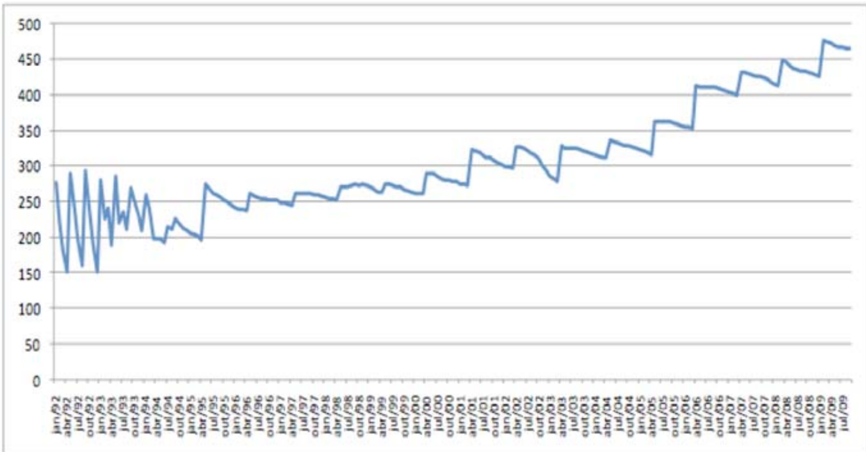
Brazil-watchers might assume that this outcome was, to a large extent, a result of *bolsa familia*: Brazil's highly successful conditional cash-transfer scheme: but crucial as *bolsa familia* has been in reducing chronic poverty, its impact on inequality is overshadowed by other factors: in particular, a significant rise in formal jobs, a reduction in informality, coupled with rising wages for unskilled workers. These factors have contributed to closing the wage gap, and to significant growth in the middle class. This in turn has helped fuel growth, which has been at least in part consumption driven.

According to Neri, a massive three quarters of the change in mean per capita earnings comes from changes in labour income.

Yes, that's right.

Here are the real minimum wage trends since 1992:

Figure 2.1. **Real minimum wage trends since 1992**



Source: Labour Ministry and INPC/IBGE.

From Neri, presented at the Conference

These have gone hand in hand with rising growth, and a drop in unemployment.

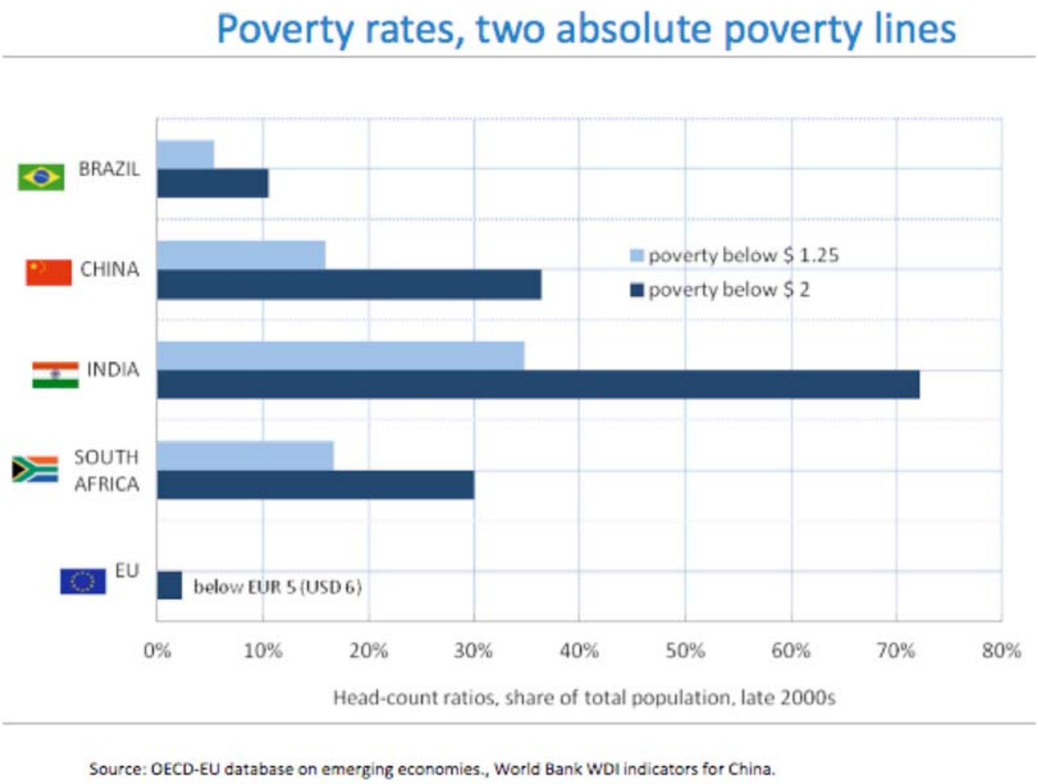
How did this happen? And why can't we do the same?

Neri argues that after a concerted focus on poverty, Brazil turned its policy attention to reducing inequality and to increasing formal employment, making these policy priorities. Part of this was a focus on education - and the dividends from this are clear: for the lowest income decile, 60% of the rise in wages can be attributed to increases in their level of education; with a 15% wage premium for every year of high school attendance after age 15. Yet Neri remains sceptical about the quality of education received.

This is remarkable. For South Africans, the key question is: what composition of growth placed this level of premium on high-school skills within the formal economy? No such premium exists in South Africa: meaningful returns to increased education only kick in post-matric. And in policy terms, which is the chicken and which is the egg? Did education policy enable new kinds of growth or did the composition of growth create new kinds of demand?

A key theme in the conference was on the fact that it's not employment levels per se that make the difference to either poverty or inequality: it's the quality of employment that matters – and the quality of social protection where employment fails.

The key contrast in this regard was between India and South Africa. While India's unemployment levels have risen steeply to 10.7% (from 6.8% last year), India has nevertheless had relatively low levels of unemployment over the last decade: yet its levels of poverty are extreme. Despite South Africa's far higher levels of inequality and unemployment, our poverty levels are not nearly as deep as those in India: bad as they certainly are.



Quoted in presentation by Michael Forster, OECD

In India, it was argued, the critical issues relate not to the rate of unemployment but to the conditions of employment, in particular in the informal sector – which constitutes a massive 86% of the economy. How does an economy operate if 86% of it is 'informal'? Apart from anything else, where does its tax base come from in a context of informality at this scale?

For India, it is low wages in the informal sector coupled with underemployment that combine to give these poverty outcomes – and without the scale of social protection in place as in South Africa to cushion this effect.

It is, however, in India that the most profound policy innovation has taken place to address these challenges. India's Mahatma Gandhi National Rural Employment Guarantee Act (MGNREGA), promulgated in 2005, creates a statutory guarantee of 100 days of work per annum to each rural household.

By taking a rights-based approach to employment, the Indian state now acts as the 'employer of last resort' in rural areas, where markets fail to create jobs at the scale required.

In addition to its impacts on poverty, the National Rural Guarantee Scheme (NREGS) is having a range of labour market consequences – which have been hotly debated in India. By paying minimum wages and honoring minimum employment standards, NREGS provides people with an alternative to work below these levels - for part of the year at least. This is increasingly setting a de facto 'floor' for wage rates and labour standards in a way that other enforcement mechanisms have previously failed to do in rural India. The most immediate impacts on equity have arisen from paying equal wages to men and women.

The scale of NREGS is breathtaking: over 55 million people are now registered on the scheme. This data is available, including copies of the job cards, the days worked and the payments made to every participant on the (remarkably transparent and comprehensive) NREGS website (www.nregs.nic.in).

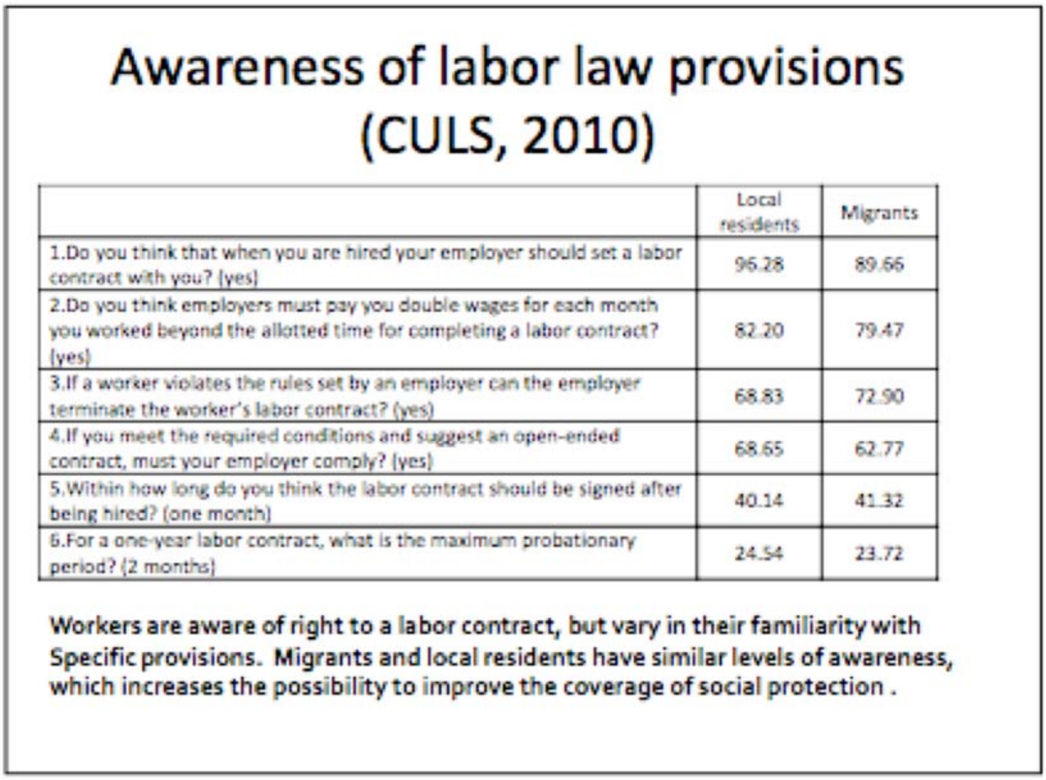
This is the world's first example of a *de jure* (and increasingly, *de facto*) right to work, in rural areas. Of course it faces many challenges (providing employment on demand to 55 million people will do that): it nevertheless remains a remarkable story – somewhat underplayed in the OECD conference, however.

The focus in China was on policies to reduce informality, to reduce the vulnerability of migrant workers, to bring greater numbers of workers into the ambit of social protection, and to raise the levels of protection of workers in the workplace, as the critical levers for addressing poverty and inequality.

In the OECD paper by Fang, Mang and Weiyang, they highlight that the combined effect of rapid economic development and an aging population has been to end the era of unlimited labour supply in China, and structural labour shortages have now emerged. This has given urgency to the creation of new labour market institutions, and impetus to improved conditions of work.

In the presentation, Du Yang refers to a 'flock' of new labour regulations in China. These include the Employment Contract Law, a Labour Disputes and Arbitration Law, The Wage Guideline System, the Minimum Wage Regulations and the Employment Promotions Law. Not too sure where trade union rights fit into this picture, but it's certainly a step-change from what existed before. For South Africa, the mechanisms China has introduced to limit the use of short-term contracts to undermine labour standards is of particular interest in the context of the labour-broker debate.

The slide below gives some taste of the kinds of protection to which workers are now entitled:



Awareness of labor law provisions (CULS, 2010)

	Local residents	Migrants
1.Do you think that when you are hired your employer should set a labor contract with you? (yes)	96.28	89.66
2.Do you think employers must pay you double wages for each month you worked beyond the allotted time for completing a labor contract? (yes)	82.20	79.47
3.If a worker violates the rules set by an employer can the employer terminate the worker's labor contract? (yes)	68.83	72.90
4.If you meet the required conditions and suggest an open-ended contract, must your employer comply? (yes)	68.65	62.77
5.Within how long do you think the labor contract should be signed after being hired? (one month)	40.14	41.32
6.For a one-year labor contract, what is the maximum probationary period? (2 months)	24.54	23.72

Workers are aware of right to a labor contract, but vary in their familiarity with Specific provisions. Migrants and local residents have similar levels of awareness, which increases the possibility to improve the coverage of social protection .

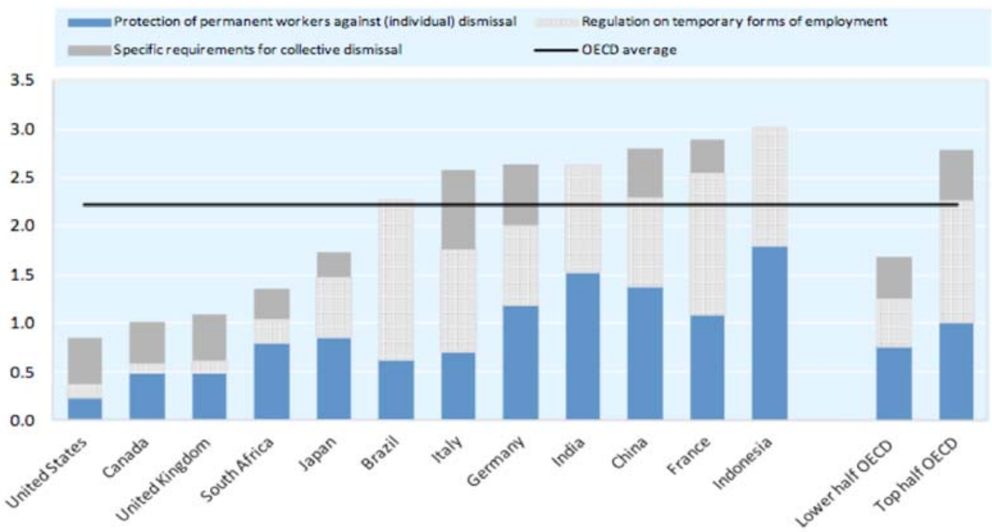
When it comes to retrenchments, China now proscribes one month's pay for every year of service: double the minimum requirement in South Africa's Basic Conditions of Employment Act. China with stronger labour regulation and better labour standards than South Africa? That will change the debate in interesting ways.

What was fascinating about this conference was that the default arguments that have come to dominate much of the South African debate were simply absent. Instead, the 'default assumptions' in this forum were that informality promotes vulnerability and that policies should aim to reduce it; that ensuring worker rights, decent labour standards and social protection don't just matter for those affected, they matter for societies as a whole; and that equity matters for its own sake as well as for more instrumentalist reasons – such as that high inequality constrains growth.

So, does this focus on rights and standards reflect a shift in the content of the international consensus? Or was South Africa just more affected by the dominant arguments in the Anglophone discourse? Certainly the OECD indicators on labor market regulation paint an interesting picture, in which rather large disparities clearly exist between the approach to labour market regulation taken in the Anglophone countries – and in much of the rest of the world. On the basis of the OECD's comparative assessment, it becomes quite difficult to characterize South Africa as having an excessively rigid labour market – and rather hard therefore to sustain an argument that this is a prime factor inhibiting our ability to address problems such as unemployment and inequality.

The EPL indicator has also been compiled recently for non-OECD countries, showing that the overall level of stringency of employment protection varies significantly across countries (Figure 2). Whereas in Brazil the employment protection regulation is similar to the OECD average, "de jure" regulation seems excessively strict in India and China, but is below the OECD average in South Africa.

Figure 2. Strictness of employment protection legislation in selected OECD and non-OECD countries, 2008a



A note on the limits of the Gini:

So where's the new improved instrument?

South Africa certainly has high levels of inequality; but the use of the gini co-efficient to measure it nevertheless paints a skewed picture, because it measures income inequality, and does not capture the redistributive impact of non-income transfers. So the social grants show up in the numbers – but the redistributive impacts of service delivery do not.

If the 'scorecard' for reducing inequality is based simply on the gini, then the policy bias will be towards cash transfers. This is by no means an argument against cash transfers: but the short and long-term impacts of access to water, energy, sanitation, schools, health services and infrastructure matter for equity also: and for the kinds of development necessary to make a sustainable shift in patterns of human capital development, and in access and opportunity.

Surely it's untenable that the main instrument used to measure inequality ignores these issues? Surely a more nuanced instrument would enable more nuanced assessment of the state of equity in societies: and the role of the state in that? At present, the Gini largely measures the distributive outcomes of market processes, leaving out many of the redistributive impacts of state interventions to remedy these. This makes it a very blunt tool.

So, where is the new improved instrument? Where better to design it than in SA?