Policy Responses to Unemployment in South Africa

Unemployment in South Africa has about doubled since transition. Using more realistic and broad definitions of unemployment that include so-called discouraged workers, unemployment is about 30 percent for men and 48 percent for women. Alone, these figures suggest that there is substantial potential growth to be unleashed if unemployment can be reduced. In fact, these figures are even more distressing than they initially appear, since labor force participation in South Africa (the fraction of adults who are in the labor market (employed or not) is itself very low by international standards.

We propose two policies to alleviate this unemployment. Each policy is designed to address aspects of the unemployment dilemma that are uniquely South African. The first policy is a targeted wage subsidy that every South African will receive when he or she becomes 18 years of age. The second policy is immigration reform to encourage the immigration of highly skilled individuals.

Three key patterns in employment data motivate the recommended policy responses. First, unemployment is much higher for younger workers than for older workers. Second, unemployment is quite high even for those with a Matric, but is very low for those with a university degree. Third, obtaining the first job in the school to work transition is a particular bottleneck. Once one has a job in the formal sector, one tends to stay employed in the formal sector, albeit not always at the same job. Getting that first job, though is quite difficult for most young South Africans.

The first policy recommendation is a targeted wage subsidy. We propose that at age 18, every South African receive an account in his/her name. This Subsidy Account would be funded by Government. It is proposed that the account start with a balance of R5000. When an account holder is first hired by a registered firm, the firm will receive up to R417 per month for the newly hired worker. This amount is withdrawn from the employee's Subsidy Account. At the end of 12 months of employment, the Subsidy Account will be exhausted. For a job that puts one at around the 20th percentile of the wage distribution, this amounts to a 50 percent wage subsidy for 12 months of employment. For higher paying jobs, the subsidy rate is lower although the absolute amount of the subsidy is unchanged. The first ten weeks of a new job held by a subsidy account holder will be a probationary period during which a "no questions asked" dismissal policy will be in effect. Subsidy accounts will not expire and can be used whenever the account holder decides to enter the labor market. If 75 percent of 18 year olds eventually used their Subsidy Accounts, this policy would cost Government approximately R3.75 billion exclusive of administrative costs. Prior to a broad roll-out, Government should conduct a small-scale experiment to evaluate the efficacy of a targeted wage subsidy.

The second policy recommendation is immigration reform to encourage the immigration of highly skilled individuals. It is proposed that anyone with a post-graduate (beyond university) degree from an accredited institution be given a fast-track visa with automatic renewal. South Africa has a shortage of highly skilled workers and highly skilled workers are a complement, not a substitute, for less skilled workers. Increasing the supply of highly educated workers will alleviate unemployment. This policy has no direct financial cost to Government and is expected to increase tax revenues.

While each policy will alleviate unemployment, the targeted wage subsidy is both a more ambitious and more effective policy.

A more detailed description of the proposed policies and the facts motivating them is found in the paper accompanying this policy brief, "Two Policies to Alleviate Unemployment in South Africa."

Jim Levinsohn

University of Michigan