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MASTERS RESEARCH REPORT

The Impact of the Institutional Structure on Wages and Employment: A Case Study of the Motor Industry and the Iron Steel Engineering and Metallurgical Industry Bargaining Councils with Reference to Labour Markets in South Africa.

(For the fulfillment of the final component for Masters Degree in Economics.)

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INTRODUCTION

The objective of this paper is to examine the effects of bargaining councils on the labour market in South Africa. The contention is that bargaining councils through the use of extensions introduce rigidities into the South African labour market. These rigidities distort the labour market and increase the level of unemployment.

The bargaining council system emanates from the Labour Relations Act of 1956. These agreements stipulate the regulations as regards the conditions of employment, wage levels, pensions and administration of labour. The purpose of their establishment was the regulation of the labour market to provide labour security for white insiders. Only since 1979 have black trade unions been recognized and incorporated into the bargaining council system. This eroded the power of the white unions. The result was that protection became a covered-uncovered worker issue and is achieved by virtue of the ability to extend the council agreements to an entire industry. I will argue that unions and the larger firms (that can afford to be involved in the negotiations) negotiate agreements that are in their own interests and then the agreements are extended to the rest of the industry. Thus the agreements and the terms thereof become legally enforceable. Thus the bargaining councils create a forum from which these select parties can create an environment favourable to their own interests.

The paper is divided into five chapters. The first chapter presents a theoretical analysis of the effects of bargaining councils in the South African labour market. I present two sides, the neo-classical (Moll) and the structuralist (ILO Report and the Labour Market Commission Report) viewpoints. These two are seen as opposing views of the labour market as well as regards solutions to the problem of unemployment. Both these models provide useful insight into the South African labour market and the effects of bargaining councils. The model presented by Moll focuses on the effect of the extensions of bargaining council agreements on the cost structures of firms. He finds that there is a difference in the cost structure between large and small firms. Large firms that are more capital intensive tend to incur higher labour costs than the smaller more labour intensive firms. Thus his contention is that the extensions of agreements increases the labour costs of smaller firms and decreases them for larger firms. This put pressure on the smaller firms and results in some of them closing down. Moll sees this from the point of view that larger firms that are party to bargaining council negotiations purposefully create these conditions to form barriers to entry. Furthermore, the unions also achieve their objective of increasing wage levels for members. The union behaviour is best explained by insider-outsider theory where the wage differentials created are between covered

and uncovered sectors. From this standpoint Moll calls for the deregulation of the labour market, i.e. the dismantling of the bargaining council system.

The structuralist approach sees the labour market in terms of the conflict between labour and business. The conflict arises out of the differing needs for security (labour) and flexibility (business). Security for workers is in terms of job security and income security whereas flexibility for firms is the ability to alter the number of workers it employs in response to changes in the conditions. These two needs are opposing, as more security is associated with less flexibility and *vice versa*. Given this characterization of the labour market the structuralist approach is opposed to the deregulation of the labour market and the reduction in the wage levels. They see the wage issue as being related to productivity in terms of an efficiency wage argument. A decrease in wages will lead to a decrease in productivity, so in order to reduce unit labour costs they prescribe that efforts should be directed at increasing productivity and skill levels. This is to be achieved through intervention into the labour market and one of the primary ways is through bargaining councils.

These two models provide crucial characterizations of the labour market that are important for this paper. The neo-classical model's characterization of the different cost structures of different firms and the objectives of the parties to the bargaining council negotiation process is crucial. However, it becomes evident at a later stage that the concentration of this model on the effects of wages is inadequate. It comes to light that it is not the level of wages that affects the firm's decision about the number of workers that it employs. The structuralist model's contention as to the existence of efficiency wages in the South African labour market is very important as this explains the level of wages prevalent in the market. It also implies that the deregulation will not affect the wage level, rather the wage levels are consistent with premiums being paid to skilled employees. The premiums are a result of the skill shortage in South Africa at present. This implies that the rigidities present are not a result of wage levels.

The second chapter examines the development of the bargaining council system. This system finds its origins in the apartheid labour market. This highlights the institutional background as well as the objectives that underlie the bargaining council system. These objectives include selectivity, duality and control. This chapter is looking at the characteristics of development of the bargaining council system in order to show that the bargaining councils system is not that different from the apartheid industrial council system. In the context of this paper the implications of this are that the councils will continue to operate in the same manner as before.

The third chapter looks at the issues of coverage, extensions and exemptions. These three issues define the institutional structure of bargaining councils. Coverage relates to the extent of the impact of the bargaining councils. Although coverage does not appear to be extensive in relation to the uncovered sectors it is important in terms of the new Labour Relations Act. The new LRA has strengthened the powers of the bargaining council system and thus the rigiditie. introduced by the system will become more extensive. The extensions are the mechanism by which the bargaining councils extend the agreements negotiated by unions and employer representatives to non-parties. It is these extensions that form the focal point of the criticism of the bargaining council system because they introduce the rigidities into the labour market. Exemptions are the relief given to parties adversely affected by the extensions. These are important as they form the main counter argument by proponents of the bargaining council system when confronted by criticism. They believe that the exemptions counteract the possible negative effects of the extensions. However, it appears that relative to the coverage of the councils exemptions are few. This chapter also introduces criticisms of the system, that the processes within bargaining councils are not fair and unbiased, that through the regulation regarding pensions, employment conditions and terms of employment they increase the costs of the firm. The main point is that the bargaining councils effect on the cost structures of firms is not only limited to minimum wages. This happens through regulation of the firm's internal environment such as prescriptions of what constitutes a permanent employee, and hiring and firing procedures, payments to pension scheme run by the council.

The fourth chapter presents the results from a survey of the Motor Industry and the Iron, Steel, Engineering and Metallurgical Industry. I undertook this survey for the World Bank in conjunction with Peter Moll. The purpose of the survey was to discover the extent and implications of bargaining council regulations. The number of firms in the survey is relatively small and thus the results are not definitive. However, they do suggest that the effect of the bargaining councils on cost structures is important and these effects are resulting in the firms employing a lower compliment of labour. The survey provides support for the argument that because of the difficulty of altering the number of workers that firm's employ they hire less labour than they otherwise would. This is in order to avoid the risk that conditions in the product market deteriorate and they get burdened with having to pay an oversized labour force. It is the constraint of not being able to readily adjust the labour component that constitutes the rigidity present in the bargaining council system.

The final chapter presents conclusions drawn from the previous chapter. The main conclusion is that bargaining councils do introduce rigidities into the South African labour market. This happens through the effect of regulations regarding the employment of workers on the decision-making capacity of the firm.

CHAPTER 1

LABOUR MARKET THEORY: THE CASE OF BARGAINING COUNCILS

Introduction

The theories of the effects of bargaining councils are intricately linked to theories of labour markets. There are two mainstream views of the South African labour market. The first is grounded in the neo-classical paradigm and the second finds its foundation in the structuralist view of the world. These two approaches are seen as opposing one another. Both approaches have their strengths and weaknesses; however, both are useful in explaining different aspects of the South African labour market.

My intention in examining these approaches is to form a base from which to analyze the impact of bargaining councils on the South African labour market. It is fundamental to understand the context in which a phenomenon operates before one assesses the impact of that particular phenomenon. The phenomenon in question is the bargaining council extensions and the context is the South African labour market.

Theoretical Explanations of the Labour Market and Effects of Bargaining Councils

Neo-classical labour market theory is based on the idea that properly functioning labour markets will equate the demand for labour with the supply of labour. Under these conditions the market will clear and there will be no unemployment. This equilibrium is defined by a market clearing wage rate. This wage rate equates the demand with the supply. These conditions will prevail if the labour market is flexible on two counts, firstly the wage must be allowed to adjust to the equilibrium rate and secondly, demand must be free to equate to supply. This flexibility is also referred to as the efficiency with which the labour market operates. The primary condition is that there is no impediment (rigidity) to the functioning of the market. A rigidity would be any mechanism that prohibited the attainment of the market clearing wage rate. (For example, minimum wage regulations that raised the actual wage rate above the market clearing wage rate.) This would result in an increase in the labour supply and a decrease in the demand for labour. The net result would be

unemployment. Rigidities enter the labour market through labour market institutions such as unions, wage setting boards and any other mechanism that artificially affects the wage rate, the allocation of labour and the income distribution. This results in a movement away from equilibrium.

The primary focus of this paper is an examination of the effect of bargaining councils on the functioning of the labour market. Given that the bargaining council system is designed to bring labour (unions) and employers together in order to negotiate employment conditions, a good starting point is to examine the effects of unions on the labour market. Unions seek to protect their workers and further their interests. Their main aim is to provide security for their members, such as job and income security. In order to achieve this unions try to increase the income of their members by negotiating higher wages and endeavour to create conditions where the laying off of workers is as cumbersome and difficult for employers as possible. The effect of the unions is twofold, first the increasing of the actual wage rate above the market clearing wage rate and secondly by making it administratively more difficult for firms to operate and increasing administration costs. The effect of this is the reduction of the firm's demand for labour and thus unemployment.

The negotiation of agreements (within the bargaining council forum) is not limited to those parties present. Through the extension of agreements the conditions decided on by the parties become binding on the rest of the industry. Two models in the neo-classical tradition are put forward by Moll (1995) and, Moll and Boccara (1996) to explain the effects of the extensions. The first is contained in *Wage Developments in South Africa in the 1990's* (August 1995) and the second in *Labour Market Flexibility and Industrial Councils in South Africa* (December 1996).

The first model is one of unions, industrial councils and "ergo omnes" rules. Moll (1995) argues that, in a free market economy, wage levels, firm size and capital intensity are correlated and this is due to differential access to capital combined with the higher skill requirements of heavy machinery. There may be other elements present such as high managerial skill that tends to surround itself with high technical and worker skill. Furthermore, unions compel employers to pay higher wages, but the effects are not uniform. Unionization is easier and cheaper in larger than smaller firms because workers may more easily gather together and there are economies of scale in addressing them and collecting dues. In the case of capital-intensive firms, workers have acquired more on the job training than in labour-intensive firms and cannot easily be replaced by scab labour in the event of a strike. Thus the workers have greater power so the union is able to negotiate for higher wage and recruit more members. In the case of firms with highly skilled (and highly paid) management's, the negotiation time of senior management is at a premium. They would probably spend more time attending to wildcat strikes, industrial sabotage and grievances if they did not

permit orderly union negotiations. This is what Moll (1995) calls the "voice" aspect of unions, which tends to increase the efficiency of unionized over non-unionized firms.

The model hypothesizes that there are two rounds of effects. The first round effect of unionization is that in firms characterized by large size, capital intensity and highly skilled management, union membership is likely to be larger and the effect of the unions on the wage rate is larger too. The second round effect of unions occurs when management is faced with longer queues of workers wishing to take the now better paid jobs. Management selects the more motivated and capable workers whose productivity on the job is such that it partially compensates for their higher wages. Management also introduces more capital-intensive production methods to save on the now higher labour costs. Total employment in the union sector falls and the excess workers are initially unemployed but are eventually absorbed into the non-unionized part of the industry where wages fall and in the long run technology becomes more labour intensive. The implications on the labour market of the extensions, within the context of the above model, can be broken down into three types: effects on labour, effects on employers and investment and effects on residual or uncovered sectors (Moll 1995). They are as follows:

a) Effects on labour.

1. Wages of workers in smaller firms will rise, thus making them better off.
2. The wages of those still employed in the relevant industry are more equal.
3. Some of the smaller firms are incapable of paying the minimum wages and go out of business and thus jobs are lost. Other firms in the same range reduce their labour force and, in the long run, adopt more capital-intensive means of production. Thus since the cost of employment and investment has risen, total investment and employment in the industry fall.
4. A second round effect of compulsory centralization is that wage levels in subsequent industrial council negotiations rise.
5. The unions now have stronger grounds for informing workers in non-unionized firms about their rights. They can force non-compliant firms to pay the legal minimum wage and provide the appropriate working conditions by reporting them to the industrial council secretariat. The union's recruiting efforts are thereby facilitated because they can easily demonstrate to workers in non-compliant firms that they (unions) are able to deliver.
6. The model also predicts that if the legislation for extensions to non-parties is made available, the unions and large firms that favour extensions will attempt to see that it is applied to all.

b) Effects on employers and investment.

1. Firms unable to pay the minima will either go out of business or employ fewer workers. The cost of investment rises and the total investment in the industry declines.
2. The minimum wage creates a barrier to entry for small firms. Many of these potential entrants, in the post-apartheid South Africa, are likely to be black owned. In the long run there are fewer black firm owners throughout the size range of firms, because fewer black firms have started up and had the opportunity to grow to a large size. The effect on overall economic growth is negative.
3. Profit rates rise throughout the industry. This is because one element of competition, namely over wages and working conditions, has been eliminated: smaller non-unionized firms are n longer able to undercut larger ones. The profit may be seen as a rent; it is unearned benefit conferred by legislation, not obtained through improvements in efficiency. The increased profit rate is attenuated in the long term because it gives all incumbent employers an incentive to invest more within the industry. It is attenuated further as the unions are enabled to negotiate to capture a portion of the rent.
4. Since one element of competition is eliminated, larger firms are no longer forced to operate as efficiently as before. Some large firms that would be incapable of withstanding competition from small firms are kept in business. This negative effect on dynamic efficiency reduces the growth rate of the economy.

c) Effects on the residual or uncovered sectors.

1. Wages in the rest of the economy fall as the workers dis-employed by the "ergo omnes" rule look for jobs in other industries. If, as in South Africa, most of the non-primary sectors are covered by industrial council minima and/or employer/union agreements, these workers fall on residual sectors such as self-employment, domestic service, gardening, or casual work for small construction concerns.
2. If the wage differential is large it induces search or waiting behaviour by workers. Instead of working in the uncovered sector, it is in the interest of some workers to search, to queue or simply to wait for a covered sector job. The measured number of the unemployed rises.
3. One element of inequality increases namely that between the covered sectors and the residual sectors in terms of wages.

The second model proposed by Moll and Boccara (1996)[1] argues that in the unionized part of the economy workers are able to enjoy above competitive wage levels. This is achieved as long as they are willing to spend part of their benefit on lobbying government for an extension of the union wage

[1] Moll and Boccara (1996), p10

to the non-union sector, and on policing these wage regulations. The regulations in the covered sector depress the wage in the uncovered sector. At the same time, workers have a reservation wage which is undergirded by the prospect of intra-familial distributions arising from, among other things, the social pensions paid to all workers above the age of 60 (women) or 65 (men). Workers whose reservation wage exceeds their actual wage offers decide to "wait" in unemployment until better offers arrive. The more the industrial council regulations depress the wage in the uncovered sector, and the higher the expected benefit, the more unemployment is generated. This model examines the resultant effects on welfare. The advantage of extensions is higher wages for workers in the covered sector. There are three disadvantages: diminished output in the covered sector; the industrial council's cost of policing; and the long-term loss of skills and experience. The only unpredictable factor is that output in the uncovered sector may increase or decrease depending on the magnitudes of investment captured from the covered sector. The implication of this model is that the bargaining councils through their affect on the wage rate increase unemployment and its duration.

Having looked at these models, I now turn to the evidence substantiating these views of the effects of Bargaining Council's on the South African labour market. The model predicts that there will be a substantial wage gap between covered and uncovered sectors. There are large differentials of between 77 percent and 131 percent[2] between the covered and uncovered sectors that create incentives for workers to remain unemployed while waiting, searching or queuing for covered sector jobs. Moreover, since the covered sector accounts for a substantial portion of the urban economy, it is likely that the differentials have induced a considerable movement of labour out of the covered into uncovered sectors. Thus the low uncovered sector wage is partly the result of the many covered-sector employers reducing their labour forces. Moll (1995)[3] argues that unions have been successful from the point of view that they have preserved the covered uncovered wage differentials in spite of low or stagnant economic growth and population influx.

The model predicts that participation is more common in larger firms than in small ones. A sample by du Toit et al (1995)[4] indicates that the average firm had 53 employees, and the average non-party firm had 13 employees. Several commentators have noted that some of the larger firms use the industrial councils to negotiate a lower wage than they would otherwise have to pay, and this provides an incentive from the large firm end of the industry for remaining in the industrial council Moll (1995). Furthermore, larger firms also seek the elimination of "unfair" wage competition from

[2] Moll and Boccara (1996), p21
[3] Moll (1995), p37
[4] Moll and Boccara (1996), quoting du Toit et al. 1995

small firms, as Moll (1995) and Bendix (1995)[5] argue, if the "ergo omnes" rules were done away with the industrial councils would fall away because they would no longer be useful to big business. Moll (1995) found that there was strong support of the compulsory aspect of centralization by the unions, however, small business was opposed to industrial council activity. A sample by du Toit et al. (1995)[6] found that 22 out of 25 (small) firms held that agreements negatively affected their operations. Furthermore 40 percent of the sample stated that the minimum wages set by the councils were a problem for their business, and 12 percent said that labour inflexibility was a problem.

To test the second model Moll and Boccara (1996) examined three questions. Firstly are the industrial council minima binding? Secondly do the industrial council rulings to non-parties reduce employment in the covered sector, i.e. do council ruling raise labour costs? Thirdly does the expectation of a transfer benefit tend to discourage low-wage employment from the demand side, i.e. do transfers increase the length of unemployment spells, or do they decrease the probability of labour market participation. Moll and Boccara (1996) provide evidence that the minima are binding, saying that a substantial proportion of firms pay wages at or only slightly above the minima, so that changes in the minima have real effects on labour costs. Enforcement of industrial council rulings is near universal for firms in the main business districts. However, in the townships where micro-enterprises are common, there is frequently little enforcement, although there is an increasing trend towards effective inspection. He also finds some tentative evidence that intra-familial redistribution of transfers, such as pensions, tend to increase unemployment.

These two models find their basis in neo-classical theory. They provide a useful insight into the effects of the extensions. The first model distinguishes between the cost structures of small and large firms. Small labour intensive firms have lower costs than larger more capital-intensive firms do. This distinction is important when looking at the impact of the extensions in equalizing cost levels across an industry. This equalization has the effect of raising the labour costs as well as administration costs of smaller firms. Meanwhile the larger firms can internalize the administration costs and lower their labour costs (Standing et al. 1996)[7]. This prejudices the operation of the smaller firms. In terms of the behaviour of the parties to the process the model is consistent in its contention that the parties to the agreements are rent seeking. This behaviour is rational in the context of agents attempting to control the environment within which they operate. For example, a firm would create barriers to entry or make it difficult for other firms to compete if it had the means to do so. The means in this case is the bargaining council system. These models suggest that bargaining council agreements should not be extended to non-parties. Rather the bargaining

[5] Moll (1995) quotes Bendix (1995), p492
[6] Moll (1995) quotes du Toit et al. (1995), p59

councils should be made voluntary organizations that facilitate bargaining between firms and unions but do not impose conditions on non-parties.

The structuralist view is in opposition to the above models. This view is contained in the Labour Market Commission Report and the ILO Report. In this view high levels of inflexibility and low levels of security characterize the South African labour market. The structuralists believe that the free market philosophy is flawed in that it does not achieve efficient outcome in the labour market. The idea is that institutional rigidities will never be removed from the labour market and thus intervention is needed to ensure efficient outcomes. An efficient labour market according to them is one in which the needs of flexibility and security are reconciled and a balance is achieved between them. This balance is to be achieved through the bargaining council system where security and flexibility can be bargained for between labour and business.

The structuralists see labour and business as adversaries. Each is attempting to achieve a different goal as regards the other. Labour is looking to increase levels of security while business is seeking increased flexibility. These different objectives are seen as opposing. Flexibility for workers means less security in terms of job and income security. Workers see flexibility as the employer's ability to change working conditions. This introduces a level of uncertainty for workers, as they do not know what the future holds for them as the business environment changes. Firms on the other hand see security as an impediment to their ability to react to changes in the business environment. Firms would like to be able to adapt to these changes as fast as possible. However, if firms cannot alter their labour inputs or costs quickly enough then this may have negative implications for their existence. It is fundamentally this opposition between employer and employee needs that forms the basis for the structuralist viewpoint. The objective of reconciling these needs is in the opinion of the ILO and Labour Market Commission Reports best achieved through 'voice regulation'. The ILO position is summed up as follows:[8]

> *"The competing or conflicting set of concerns for employers and workers both need to be taken into account, as do those of the more marginalised or vulnerable on each side of the spectrum. They cannot be given their due weight if one party or the other is enfeebled or fragmented. This is ultimately why 'voice' mechanisms, or representative institutions, are required even though the neo-liberal supply side advocates of flexibility and 'deregulation' regard institutions and regulations as rigidities and the main source of inflexibility. Those sirens of deregulation are wrong, because unless flexibility is bargained between strong*

[7] Standing et al. (1996), p185
[8] Labour Market Commission Report, p12

negotiators, opportunism would lead to short term gains by one side or the other (usually the large scale powerful employers) that would have long term adverse consequences for dynamic efficiency."

The structuralists believe that the only way to achieve an efficient outcome in the labour market is the reconciliation of these two opposing objectives. They believe that the free market system with no labour market intervention will not achieve this. The intervention that they are calling for falls under the blanket of labour market regulation. The objective of this labour market regulation is a system of regulated flexibility. This system consists of the bargaining council system underpinned by labour market regulation. The bargaining council system is the means by which 'voice regulation' functions, i.e. this is where the employers and employees negotiate the balance between flexibility and security. However, in order to force parties to the bargaining table, the bargaining council system must have legal recourse. This legal recourse is the extension of agreements. The idea is that government set down broad regulations regarding employment conditions and the specific conditions and wage levels be decided in the bargaining council forum. The agreements reached are then extended to the entire industry so that conditions are equalized for all.

The structuralists see the labour market as being highly unequal. This can be observed in the high wage differentials that are reflected in the highly skewed income distribution as well as the skill acquisition of different population groups. (White professionals and managerial personnel accompanied by an over abundance of black unskilled labour). The structuralists conclude that there is an important link between wages and employment. The estimated long run wage elasticity of labour demand is -0.7[9] and this is worrying in the context of high unemployment. The reason is that wage increases impact negatively on employment to the extent that, over the long term, a 10% increase in wages is going to result in a seven-percent drop in relative employment (although this may not be in absolute terms). This suggests that in the long run, employment levels are sensitive to changes in wage levels. The structuralists, however, argue that the key issue for competitiveness of industries is not the wage but the unit labour cost. In saying this they imply that a range of measures is needed to contain increases in unit labour costs. Unit labour costs are the labour costs per unit of output and as such if productivity increases and wages remain the same then unit labour costs will decrease. The Labour Market Commission is saying that measures are needed to address the levels of productivity because there is evidence to suggest that average unit labour costs in South Africa are higher than comparable middle income countries. Thus to bring down the unit labour costs they believe that more effort should be put into increasing the productivity of workers. This is implicitly an efficiency wage argument. From this standpoint they argue that there should not be a decline in

[9] Labour Market Commission Report, p52

wage levels because the impact on average unit labour costs of depressing unskilled wages may be relatively small depending on labour intensity and on the contribution of wages (especially unskilled wages) to total labour costs. They believe that it would be more efficient to increase the levels of productivity rather than decrease wages because of the positive correlation between the two. Thus if there was a decrease in wages then productivity would also decrease. In their view this is undesirable and will impact negatively on growth in the economy.

Increased international competition has placed a strong burden of adjustment on South African firms and as a result labour costs may well be comparatively high relative to production especially for those firms using a high proportion of unskilled workers. Some analysts (essentially proponents of the neo-classical paradigm) have blamed "high unskilled wages" for South Africa's lack of competition and its high level of unemployment. The issue is seen as more complex than common sense orthodoxy assumes, especially accounting for the level of unskilled wages and productivity of unskilled workers. The belief is that the higher skill, higher wage industrial sectors are unlikely to generate large numbers of new jobs and that future formal-sector employment growth is most likely to occur in lower wage more labour intensive sectors such as tourism and clothing. Thus they see it as simplistic to conclude that wages can simply be lowered, or that job growth would automatically follow a reduction in wages. Wage repression in the view of the Labour Market Commission may simply breed resistance and results in increased industrial and social unrest that would discourage both growth and new employment. They argue that to some extent there is a wage-employment trade-off, however, it does not follow that unemployment is simply caused by high wages. They believe that other factors are also responsible such as macroeconomic and industrial policies. For example, contractionary and uncoordinated macroeconomic policies that reward capital intensive investments impact negatively on employment growth independently of the operation of any wage employment trade-off. Also the Labour Market Commission cites anecdotal evidence to suggest that many employers are reluctant to employ large numbers of unskilled workers because of the 'hassle factor', i.e. the time and management energy involved in dealing with a demanding workforce aware of its rights. They recognize that the shortages of skilled labour are a recognizable constraint on economic growth. Labour intensive production also requires skilled employees (essentially managers) and these shortages may act as a bottleneck as much as in the capital intensive sectors.[10]

The structuralist support of the bargaining council system stems from the belief that by reconciling the needs of security (workers) and flexibility (employers) a system will be created where productivity will be increased. The argument is that if workers are content then they will be more productive and by addressing their need for security in the workplace this will be accomplished.

[10] Labour Market Commission Report, p52

The argument is that firms should focus on the long-term instead of the short-term. The structuralists argue that to reduce costs and become more competitive, firms will in the short-term seek to lower the wage rate, however, in the long term it is not feasible to continually lower the wage rate. The structuralists argue that it is in the firm's interests to increase productivity and thus their competitiveness. This can only be achieved in the long-term. The structuralists believe that the bargaining council system will force firms to become active in finding ways to increase labour productivity and thus act in the firms and workers long-term interests. The structuralists argue that this will lead to stability in the wage rate and the workforce will be content. Thus all round stability will be achieved in the labour market.

The structuralist approach is insightful into the motivations of employees and employers. It recognizes that employers and employees have opposing motives. This opposition in the respective motives is seen as the major impediment to the efficient functioning of the labour market. This is entirely plausible given peoples self interest. However, this approach does not go far enough in explaining the behaviour of firms, unions and employees. The crucial aspect that they do not seem to address is the self-interest of union officials. Although the union officials have to work within the constraint of satisfying their members there is still latitude enough for them to pursue their own interests. Thus we have perhaps three players in the labour market, firms, employees and union officials. Furthermore the aspect of a firms motive that is not accounted for is their will to affect the environment in which they operate. If a firm can create an environment that will minimize competition from other firms such as higher costs for other firms or barriers to entry, then it will. The structuralist account does not address the union's use of the system to create a closed shop situation where its workers are protected from the threat of non-union workers and in so doing increase unemployment. The implications of the above is that they could negate the positive effects of negotiation and lead to greater impediments in the labour market.

It is true that the labour market is more complicated than the simple neo-classical model would suggest, however, the effect of the price mechanism in the allocation of labour and levels of employment cannot be neglected. The wage rate sends signals to the agents in the economy and if distorted will lead to inefficient behaviour resulting in unemployment. On the issue of the wage rate the Labour Market commission implicitly hinted at the existence efficiency wages and the link between wage levels and productivity when they discussed the issue of unit labour costs. The efficiency wage models argue that if the level of wages affects the productivity, then it may be in the firm's interest to raise the wage rate above the market clearing level and to refuse to cut wages, despite the resulting unemployment.[11] For example, Shapiro and Stiglitz (1984) show that firms

[11] Azam, p79

have an incentive to increase the wage above the market clearing wage, as a "worker discipline device". The argument is as follows: if there is full employment with the same wage paid to all workers, the incentive for shirking is strong. When caught shirking, the worker is fired at no cost to him since he is bound to immediately find a new job. Thus to improve the productivity of workers, firms must try and offer better wages than do the competitors in order for the workers to face some prospect of loss when they get caught shirking. But by then all the firms pay a wage higher than the market clearing wage and the resulting unemployment is sufficient penalty to deter, at equilibrium. In the case of the labour turnover model (Stiglitz 1974), firms have the incentive to increase the wage above the market clearing rate in order to reduce the turnover costs. In other words firms pay higher wages, with a positive unemployment rate, so as to make the expected outside wage low thus reducing the turnover rate of employees. An extra dimension is that the turnover rate not only depends on the wage paid within industry but also those in other sectors such as the relative rural wage.[12]

The implication of the efficiency wage argument as presented by the Labour Market Commission is that an adjustment of the wage rate downwards, as prescribed by the neo-classical model, will reduce the level of productivity. The reduction of productivity will in turn impact negatively on the level of output and hence GDP. This is in their opinion undesirable if the objective of labour market reform is to foster growth and development.

The explanations of the ILO Report and the Labour Market Commission neglected one aspect of structuralist theory, namely the insider-outsider approach. The insider-outsider approach in contrast with the neo-classical approach recognizes that incumbent workers (insiders) can influence the hiring and firing decisions of the firm. There are two basic elements that drive a wedge between the wage paid to insiders and the reservation wage of the outsiders: firstly, there are various costs for hiring and for firing; second, insiders possess a know-how that outsiders need to acquire and this entails a productivity differential. Azam (1994) notes that this theory can offer an explanation of unemployment, and it has important consequences for macroeconomic dynamics and the effect of nominal shocks on output and unemployment. It implies a ratchet effect or hysteresis effect.[13] For example, if some insiders are fired after an unexpected negative shock and rapidly lose their status (becoming outsiders), then the economy settles at this new equilibrium level with a lower level of employment than in the preshock equilibrium, even after the shock has disappeared.

[12] Azam, p84
[13] Azam, p91

The efficiency wage and insider-outsider models are useful in explaining unemployment without the existence of interventions by the authorities that introduce rigidities (such as minimum wages). This suggests that even if markets are left alone they will not necessarily reach equilibrium. However, the question is in what way are these rigidities introduced into the labour market and the magnitude of this effect. For example the efficiency wage effect may be limited to larger more capital intensive firms that have higher skill requirements than do smaller more labour intense firms. The insider outsider theory in this paper relates to workers covered by extensions and those that work in uncovered sectors. It implies that covered workers will attempt to create barriers against incoming workers that may try to undercut them in terms of wages.

Conclusions

The theories of the South African labour market with reference to bargaining councils all offer useful insight into the dynamics of this market. I believe that you cannot look at one theory exclusively. The main contribution of the neo-classical theory is that it explains the effect of the bargaining councils on employment through the effect of extensions raising the cost structure of smaller firms. This happens because the extensions force smaller firms to pay higher wages than they otherwise would and therefore cannot employ more workers than they presently do or did so in the past. Larger firms on the other hand end up paying lower wages than they would have too without the negotiated agreements. Furthermore, the theory states that the larger firms that attend the negotiation of the agreement actively seek these conditions. Smaller firms that cannot devote the resources to the negotiation and do not participate in them are discriminated against. These actions of the larger firms are seen as the erection of barriers to entry.

The structuralist approach sheds light on the interaction between workers and employers. It highlights the differences between employer motivation and employee motivation. These motivations affect the behaviour of the respective parties. The workers are seeking greater security and the firms are seeking greater flexibility in the labour market. These goals are seen as opposing and result in conflict between workers and firms. The solution suggested by the structuralist orthodoxy is the bringing together of business and labour under the auspices of bargaining councils to negotiate the balance between their respective needs.

A further aspect of the structuralist theory is their opposition to any decrease in wages. In their view a decline in the wage rate will lead to a decline in the level of productivity of workers and result in a decrease in output. The structuralist approach argues that wages should not be decreased, rather the

level of productivity should be increased. This implicitly implies the existence of efficiency wages. Their solution is the imposition of measure that will raise productivity levels.

The fundamental difference between the structuralist and neo-classical view is that the neo-classical model is focused on the demand side and calls for an adjustment in the wage levels while the structuralists focus on the supply side and argue that it is more important to increase productivity levels. The solution according to the neo-classical model is the deregulation of the labour market. This would entail the downgrading or removal of bargaining councils. On the other hand the structuralist approach argues that the bargaining council system is the panacea resolving the problems in the South African labour market. The question of whether the correct solution is increasing or decreasing regulation of the labour market is somewhat complex and beyond the scope of this paper. The scope of this paper is to examine the effects of bargaining councils. The remainder of this paper will be devoted to investigating the degree and effect of these rigidities as well as the types of rigidities that are introduced. The next chapter deals with the development of the bargaining council system. This is crucial to the understanding of the effect of bargaining councils because in effect they are an apartheid structure that is still operating in the new democratic South Africa.

CHAPTER 2

THE DEVELOPMENT OF THE BARGAINING COUNCIL SYSTEM

Introduction

In order to examine the nature and extent of the effects of bargaining councils one must first understand how they came into existence. The purpose of this chapter is to look at the history of the bargaining council system. It was said in the previous chapter that the bargaining councils are in effect the old industrial councils merely renamed. Therefore the nature of the development and objectives of the old industrial council system are important in explaining the functioning of bargaining councils.

It is generally accepted that the industrial council system was formed to promote selectivity and protect the jobs of the white minority. It can be argued that with the changes in the South African labour market the industrial council system evolved from one that discriminated on the grounds of race to one that protects and advances the interests of a specific group of individuals, namely the employed unionized workers and big business.

This chapter looks at this process and examines the reasons for the changes that result in the creation of the current bargaining council system.

The Development of the Bargaining Council System

The evolution of the South African labour market was characterized by initial high flexibility moving over time towards greater rigidity (Standing et. al. 1996). The early legislative and regularity framework was intended to 'free' the labour supply to the mines and commercial firms. In 1924 the Industrial Conciliation Act was passed and sought to protect the unionized white workers (poor whites) from cheap black labour. This was the first substantial move towards regulated labour markets in South Africa. After the election of the national government in 1948 the government attempted to create a system of regulated rigidity through policies such as, pass laws, influx controls, job reservation and regional development policies. These were intended to direct labour mobility and lower the labour cost of black workers while protecting the wages of the whites

(Standing et al 1996). The 1956 Labour Relations Act (LRA) superseded the 1924 Conciliation Act. This Act formed the cornerstone of the apartheid labour market. The LRA stimulated the establishment of "industrial councils" whose role it was to regulate the labour market at the sectoral level for the benefit of the white minority. Under the LRA registered employer organizations and registered trade unions could voluntarily agree to establish an industrial council, the membership of parties was, however, at the discretion of the registrar (section 18). This discretion meant that the registrar could decide on which class of worker was eligible for representation. Black workers were not eligible. The industrial council system was seen as a means of implementing selective rigidity.[14] The ILO Report summarizes the flavour of the system in saying that:[15]

> *"The industrial council system encouraged a selective (racially based) form of regulated corporatism through notions such as "sufficiently representative" - which of course excluded black workers who were not allowed to form recognized trade unions until after 1979 - and reference to "stability", which has been an objective of all hegemonic systems including the welfare state regimes of post-1945 western Europe. The industrial council system was intended to provide labour security for protected white insiders, who thereby could set the conditions they favoured and impose post entry closed shops. The system went so far as to allow the Minister to make "extensions" of Industrial Council agreements to non-parties, i.e. impose so called 'ergo omnes rules on the sector or area covered by the agreement."*

The extensions to non-parties arose out of the concern to protect white labourers from competition from black labourers. The Industrial Councils were empowered to set minimum wages for workers as well as conditions of employment. Once an agreement was reached, employers were bound to provide at least the minimum wage agreed to and the unions were bound not to strike. Strikes could only take place after proper negotiations had taken place. All employers and unions in industries with industrial councils were required to register under the Act, even if they did not participate in the negotiations.

The basis of the government strategy was the regulation of minimum conditions of employment and minimum wages through the use of individual employment contract under common law, statutory law and collective agreement. The complexity of the system created problems resulting from overlapping jurisdictions and this is evident in the multitude of wage determinations, industrial councils, labour orders, apprenticeship regulations, conciliation board agreements and arbitration

[14] Standing et al. (1996), p14
[15] Standing et al. (1996), p14

awards. The LRA amendment of 1981 introduced the concept of a 'labour order', which was more selective in regulatory coverage, to cover areas not covered by the Wage board.

The Wage Act through Wage Boards set minimum wages for all areas except bantustans. Selectivity was promoted by the fact that the Wage Board was dominated by Ministerial discretion as it was the Minister who appointed the board, set its terms of reference and decided to accept or ignore its recommendations in making a wage determination. Exemptions had to be sought directly from the Minister. The Basic Conditions of Employment Act (BCEA) set maxima for hours work and overtime, restrictions on continuous work and provisions relating to duration of meal times, Sunday work, annual leave, sick leave and maternity leave. Under apartheid these regulations were selective, for example the exclusion of agricultural-workers, domestic workers and public service workers, with a myriad of other exclusions and exemptions. Minimum standards did not apply in the same way to all workers that were covered by the act; for example casual workers were treated differently to so-called 'indefinite' employment contracts. The BCEA gave very little employment security: it stipulated two weeks notice of termination of employment for monthly paid workers, one week for weekly paid workers and none for casual workers (section 14). Employers could only obtain exemptions to the various regulations through application to the Minister of Labour and only the Minister was empowered to grant them regarding any provision of the BCEA.[16]

Between the LRA, Wage Act and the BCEA the government created a system of regulation and control in the labour market. The apartheid labour market enabled the white minority to increase its wealth at the expense of the black majority. However, conflicts between the needs for industrialization and the character of selective regulations began to put pressure on the apartheid labour market. This led to the recognizing of black trade unions. The culmination was the Industrial Conciliation Act of 1979 where Africans were permitted to join registered trade unions or form trade unions that would be eligible for registration. This ultimately led to the loss of control of the Industrial Councils by the white unions. The result of this was that the wedge between white and African workers was recycled as a wedge between "insiders" or workers employed in the industries covered by the industrial councils, and "outsiders" or workers who were either unemployed or were employed in industries not covered by the industrial councils.[17]

Standing et al. (1996) argue that the regulatory framework of the apartheid labour market became ineffectual as the conflict between the needs of industrialization and the character of selective regulations sharpened in the 1980's and 1990's. It was the growth and diversification of

[16] Standing et al. (1996), p13 notes that the protection was for the white minority, to protect them from outsiders.
[17] Moll and Boccara (1996), p5

manufacturing, and to a certain extent construction and services, that accelerated the erosion of the old system. Manufacturing needed more skilled workers and needed to incorporate the rapidly growing black urban industrial population. Economic development and industrialization produced untenable tensions in the dominant social relations of production. Pressures on the system of "selective rigidity" came from the concentration of capital and the growing desire to promote industrial development, coupled with growing international hostility to apartheid and the resistance of black urban youths.[18] By the 1990's there were many institutional features inherited from the apartheid era that were gradually being stripped of their former functions and context.

The movement towards a democratic South Africa that culminated in the first democratic elections in 1994 has led to a revision of labour market legislation, the goal being the creation of a system of regulated flexibility as defined by the Labour Market Commission.[19] This is encompassed in the Labour Relations Act, No 66 of September 1995. The Act makes provision for the strengthening of collective bargaining through the preservation of the industrial council system under the new name "Bargaining Councils". The Act provides for the automatic extension of Bargaining Council agreements to non-parties if the majority of the Council requests it and the both unions and employers represent 50 percent or more of the workforce. It strengthens union rights by prohibiting the dismissal of legal strikers, legalizing sympathy strikes, and enabling legal picketing.[20] The Labour Relations Act recognizes that where bargaining strengths are very unequal, the Wage Board will have to protect workers. In promoting institutional mechanisms for collective bargaining, the LRA proposes that at the national level there will be a tripartite Commission for Conciliation, Mediation and Arbitration, which will replace the former conciliation service. There will also be a national Labour Court, whose judges will be appointed by the President in consultation with NEDLAC. The changes to the law are fivefold, namely:[21]

1. Bargaining Councils cover both private and public sector parties;
2. Small-scale employers must have their interests represented;
3. Bargaining Council representativeness of an industry must be reviewed annually;
4. The Minister of Labour retains the power to extend agreements to non-parties;
5. Dispute resolution capacity should be improved through mediation and arbitration procedures;

Reformers were intent on preserving what they perceived as the protective features that tend to give forms of labour security while promoting economic development, dynamic efficiency and

[18] Standing et al. (1996), p15
[19] Standing et al. (1996), p15
[20] Moll and Boccara (1996), p6
[21] Standing et al. (1996), p169

restructuring. They have moved to reform industrial relations through the 1995 Labour Relations Act, which is an attempt at strengthening sectoral collective bargaining and sectoral forms of tripartism. The general direction of these initiatives could actually be described as creating a system of "regulated flexibility" (Standing et. al.). The Labour Market Commission believes that bargaining council agreements between unions and employers can generally lead to realistic and agreed minimum conditions being determined since they include the parties directly affected. In their opinion collective bargaining is the preferred system. The Commission also believes that there is some justification for the judicious use of legal incentives, using mechanisms of the Wage Act and the LRA's provisions allowing the extension of bargaining council agreements.

Notwithstanding the reforms, the bargaining councils are still run by the same bureaucrats that where in charge of the functioning of industrial councils. The union and the employer representatives are the same and have the same motivations and objectives as before. The bargaining councils are in effect the same institutions that operated in the apartheid system. The changes to the labour relations act have served to strengthen the bargaining council system in terms of coverage and ability to extend agreements. In my opinion the bargaining councils have not changed into the institutions that were envisaged in the new Labour Relations Act.

Conclusions

Given the changes to the industrial council system that transformed it into the bargaining council system, it is fair to say that the two systems are essentially the same if not in specifics then in character. The implications for the ideals of the Labour Market Commission Report are that the equality they believed would be delivered through negotiation within this forum will not be realized. The implications of the models in chapter one especially the more neo-classical models by Moll point towards increased unemployment. This, needless to say, has severe consequences for the economy.

In theory I do not see any problem with using the bargaining council system as a mechanism in the labour market, however, the problem is the manipulation of the system in order to serve a select group's interests. In addressing the problems in the South African labour market one should keep in mind that high levels of inflexibility are present.

Thus far I have examined the theoretical and historical perspectives of the bargaining council system. Some bodies such as the bargaining councils themselves and the proponents of the

bargaining council system would argue that relief is given to firms as regards the extensions and this negates any negative effects resulting from the extensions. Proponents would also argue that the coverage of bargaining councils is not extensive and thus the impact of them is relatively small when looking at the entire labour market. In the next chapter I address the issues surrounding the scope and activities of bargaining councils.

CHAPTER 3

THE INSTITUTIONAL STRUCTURE OF THE SOUTH AFRICAN LABOUR MARKET WITH REFERENCE TO BARGAINING COUNCILS

Introduction

This chapter examines the scope and workings of the bargaining councils in the labour market. 'Voice mechanisms' as envisaged by the ILO Report and the Labour Market Commission Report are promoted by the new LRA in the form of Bargaining Councils. The Act strengthened collective bargaining, which is seen as essential in order to achieve the goal of "regulated flexibility" (as envisaged in the ILO and Labour Market Commission Reports) and an equitable labour market. In this forum employers and employees, represented by employer associations and unions respectively, negotiate the balance between flexibility and security.

The practicality is that once a year the parties within an industry meet in order to negotiate agreements regarding minimum wages, conditions of employment and any other related issues. Once the negotiations are completed and the agreement finalized then if the council has been granted the ability to extend the agreements the conditions of the agreements become binding on all firms and workers in that industry. In those industries where extensions do not exist, the agreement is only binding on the parties to the agreement.

The rest of this chapter is devoted to examining the main issues regarding the extension of agreements. These are coverage, extensions and exemptions. I have restricted the scope to these three issues because they are the main issues of debate surrounding the extent and magnitude of the effects of bargaining councils and they are the main points around which the debate about the desirability of bargaining councils revolves.

Bargaining Council Coverage

The reason to examine the coverage of bargaining councils is that it gives an indication of the number of firms and employees that are directly influenced by the bargaining council system. Table

1 shows the number of councils present in each year, the number of wage agreements, the number of employers that were covered by those agreements and the number of affected employees. Moll and Boccara (1996)[22] argue that the coverage measures underestimate the impact of the regulation in question. According to Table 1, the industrial council system's coverage waned from 1.2 million workers in 1981 to 0.5 million in 1990, before expanding again to 0.8 million by 1993 and 1 million by 1994. Moll and Boccara (1996), Fallon and Lucas (1996) believe that the system's coverage rose to 1.3 million by 1995, and that it may rise further to 1.6 million as the Labour Relations Act of 1996 is progressively implemented[23]. One reason for the decline in membership in the eighties as suggested by Standing et al (1996), is that management was increasingly resorting to decentralized, plant level bargaining, even within individual firms. Horwitz and Franklin (1996) corroborated this sentiment in their study of developments in the South African labour markets.

Table 1. Coverage of industrial councils, 1981 - 1995

ear	Number of councils	Number of wage agreements	Employers	Employees
1981	104	99	46,668	1,265,000
1982	104	77	48,309	1,267,222
1983	104	87	40,075	1,171,724
1984	102	94	51,031	1,183,399
1985	100	85	48,329	1,084,278
1986	99	77	47,032	961,302
1987	97	86	45,941	964,881
1988	95	68	44,927	980,00
1989	94	71	41,205	958,150
1990	92	60	31,292	515,082
1991	87	63	49,740	761,332
1992	87	84	51,266	583,472
1993	85	73	65,578	805,133
1994	81	-	54,000	1,000,000
1995	81		-	-

(Source: Moll and Boccara (1996), p.8, from Standing et al. (1996), p. 145, Table 5.1, in turn from the Department of Labour.)

[22] Moll and Boccara (1996), p8

[23] Moll and Boccara (1996), p7 quoting Fallon and Lucas (1996) p18 and 24.

Furthermore, management is also seen as seeking ways around the industrial council rulings by, for instance, using labour contractors to perform tasks such as cleaning and security. Furthermore, employment in some of the largest manufacturing industries declined (Moll 1996).[24]

The scope of coverage varies, for example as of May 1992, nine percent of the councils had a national scope, 43 percent a regional scope (encompassing seven or more magisterial districts), 40 percent a local scope (six or fewer districts), and 8 percent had only a company scope.[25]

Moll and Boccara (1996) argue that the industrial council arrangement is a barrier to entry; it raises labour costs and reduces incentives for investment in the covered sectors. It reduces the number of firms active in the covered industry. As a result the covered ratio - whether the proportion of workers covered or the proportion of firms covered - falls over time, as the industrial council's regulations take hold. The industrial council arrangement in acting as a barrier to entry extends its impact beyond the regional jurisdiction stated in the councils Main Agreements.[26] An investor wishing to take advantage of the lower wage in a region excluded from the ambit of a particular industrial council would have to take into account the likelihood that, once the firm is established an industrial council could be set up in order to regulate this new activity. The intention of legislation is opportunistic: the objective is to regulate the labour process wherever the unions perceive substantial benefit from doing so. Therefore if a large manufacturing plant were established in a small town outside the jurisdiction of the industrial council, and if the union were to become active, before long a bargaining council would be in place and the labour costs would have risen. Coverage is important as it indicates the possible impact of extensions of agreements, i.e. the number of firms and workers affected by them. This is the issue to which I now turn.

Extensions

Extensions, otherwise known as "ergo omnes", occur when an agreement reached within the industrial council forum becomes binding on the entire industry. Therefore, the terms and prescription of the particular agreement bind even non-parties to the negotiation process.

Extensions are made at the Minister of Labour's discretion. The 1995 LRA prescribes that if employers and employees represent more than 50 percent in an industry then the Minister of Labour is bound to extend them. However, if this condition is not met then it is up to the Minister after

[24] Moll and Boccara (1996), p8
[25] Moll and Boccara (1996), p8

careful consideration. The extension of agreements has been widespread, as of April 1994, 69 out of 75 council agreements had been subject to extensions.[27] In some cases, the parties to an agreement have declined gradually as a share of the total. Moll and Boccara (1996)[28] states that in 1981 the largest industrial council (the National Bargaining Council for Iron, Steel, Engineering and Metallurgical Industry) accounted for 42 percent of all firms covered by the agreement. In 1995 the council represented only 28 percent, and the workers employed by party firms in 1981 accounted for 82 percent of all covered workers, but by 1995 they were only 65 percent of the total. This would seem to indicate that extensions have become more prevalent elsewhere in the economy, this is indicated by the decrease in the share of coverage of the National Bargaining Council for Iron, Steel, Engineering and Metallurgical Industry which is the largest.

In 1985, some 64 percent of workers in the manufacturing sector were covered by industrial council agreements (Moll 1993). In the sample of manufacturing firms selected for the Labour Market Flexibility Survey by Standing et al. (1996), fifty percent were covered by industrial councils. However, in the non-manufacturing sectors there exists what might be termed a "voluntary" system of collective bargaining where negotiations occur at the level of the factory, the firm, a group of firms, or the entire industry, without such compulsory aspects as registration with the industrial council or forced compliance with industrial council rulings by non-parties. An example is the cement industry in which there are a small number of large producers that bargain jointly with the unions. The important issue as regards extensions is the contention that they increase wage differentials between covered and uncovered sectors. Although there is debate as to the magnitude of this effect, the fact that there is an effect is cause enough for concern especially in light of the strengthening of the powers of Bargaining Councils by the new LRA.

When confronted with criticisms of extensions, the proponents of this system argue that there are exemptions from agreements and thus there are no negative effects. However, the granting of exemptions is a contentious issue from the point of view that they are at the discretion of the Bargaining Council and the process by which applications are processed is perceived as being inefficient and biased.

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[26] Moll and Boccara (1996), p7 quoting Peter Doyle

[27] Standing et al. (1996), p 143, in turn quoting J Baskin, 1994. Centralised Bargaining and COSATU. Johannesburg: NALEDI., June.

[28] Moll and Boccara (1996), p8

Exemptions

The LRA introduced a system of exemptions at the discretion of the Industrial Council, that could be granted if terms or conditions were not substantially less favourable than those prescribed in the agreement. The Bargaining Council grants exemptions in question and as a general rule they are of limited duration (usually one year) and are given only to a firm less than a certain size in existence for less than four years. Moll and Boccara (1996)[29] states that in the experience of most firms the chance of being exempted is so small that it is not worth applying. In 1994/1995, the industrial councils granted 4,315 complete exemptions and 153 partial exemptions, while turning down 389 applications (Standing et. al., 1996, p144). The total granted were 4,468, this comprises only 8 percent of firms.[30] The system of exemptions has been widely criticized, on six grounds:[31]

1. The parties to an agreement who have vested interest in not granting exemptions decide on exemptions;
2. Exemptions take a long time to process;
3. Exemptions granted are on an arbitrary basis;
4. Representations by applicants are not allowed;
5. Reasons for refusal are not given;
6. Exemption procedures are complex.

The system of exemptions is perceived as not being efficient in addressing the problems created by the extensions. Discussions with Confederation of Employers of Southern Africa (COFESA)[32] revealed that in their experience in representing members in their applications for exemptions, the exemption boards comprise both union representatives and representatives of the firms competitors. The granting of the exemption will mean a loss of income to business, for the employer's organization and the council as well as affiliation fees for the union since only union members may work in these factories. In submitting applications for exemptions firms have to submit private and confidential business information to their competition in businesses that sit on the board. COFESA believes that these boards ignore the fundamental rights of administrative justice, free trade and privacy.

[29] Moll and Boccara (1996), p9
[30] Moll and Boccara (1996), p9
[31] Standing et al. (1996), p143
[32] I had discussions with Mr H van der Walt who is the director if COFESA in March 1997.

Effects and Costs

COFESA[33] assists companies in dealing with industrial council regulation, and has to an extent been involved in the push towards the use of contract labour in order to side-step the bargaining council agreements. In dealing with bargaining councils they have found that the high level of wages for new entrants is unrealistic and inhibits job creation. Some bargaining councils prescribe that the wage of the entrant must increase at the completion of six months of service. In many cases production has not increased and the person is still at the initial phase of the learning curve, costing the company money in terms of training time and wasted materials.

The discussions with COFESA also revealed that bargaining councils have an effect on the costs of labour for firms. The bargaining councils affect the cost structures of firms by increasing administration costs such as pension contributions. In the view of COFESA the councils protect their uneconomical pension schemes, which are not supervised by the Registrar of the Department of Finance. COFESA has found that the councils pretend that they exempt factories who can provide better pension or provident funds, however, in practice it is impossible to prove that another fund is better and the councils are the ultimate judge of eligibility. Firms are forced to match the contributions of workers to the pension funds and this can be a sizable sum thus increasing the costs of labour and the result of this is that firms hire fewer workers. The firms do not receive anything in return for their contributions, however, when firms have a better alternative they are not allowed to exercise it. Furthermore, COFESA believes that the bargaining councils affect the firm's ability to function. This works through the stipulations regarding employment and the conditions of employment. The stipulations result in the firm being inhibited in its ability to alter the size and composition of its labour force. Thus firms would rather hire less permanent labour and when the need arises use casual labour to fill in. This is because in times when demand for the firm's products increase the firms need to hire more labour in order to increase output, however, they do not know how long the increase will last. Now because the firm cannot easily retrench workers it would rather not take on more permanent workers in case the demand for its product decreases and it is burdened with larger labour force that it must now pay. Therefore the firm will employ a smaller permanent labour force. The higher costs and stipulations about employment translate into lower levels of permanent employment. The theories of chapter one did not address this dynamic of the bargaining council system. The neo-classical model focused on the effect of direct labour costs and the structuralist model on the productivity aspects of labour. The implications of this are that there are aspects of the bargaining council system that are not explained by the theory and possibly not yet understood.

[33] I had discussions with Mr H van der Walt who is the director if COFESA in March 1997.

According to COFESA the bargaining councils prosecute more than 4 000 firms per year (approximately 60% white and 40% black) in Gauteng alone for not registering or paying levies to the councils. This is a form of "dirty tricks" in order to induce firms to comply with bargaining council regulations. This jeopardizes the Growth Equity and Redistribution initiative of the Department of Trade and Industry to create 400 000 job opportunities per year.

Conclusions

The debate surrounding industrial councils is focused on the issues of coverage, extensions and exemptions and the differing interpretations as to the impact and effects of these phenomena. The debate begins with the extent of coverage. The opponents have argued that coverage is relatively large and extends beyond the mere number of employees and employers that are covered. However, the issue of coverage is not only confined to those already present in an industry. For example the threat of the formation of industrial councils is enough to deter investment into a particular industry. An important implication is that the new LRA in supporting the bargaining council system will extend the coverage of bargaining councils. This means that coverage will increase and therefore the effects of the bargaining councils will be further exacerbated. It can therefore be expected that the inefficiencies present in the labour market caused by extensions will worsen.

The issue of coverage leads directly into the issue of extensions. The argument of the proponents of extensions is that they introduce stability, predictability and equity into the labour market. Opponents to the system argue that the extensions raise the cost of labour and hence lead to increased unemployment. They also lead to covered-uncovered sector wage differentials. It does seem that the extensions are the case rather than the exception in the bargaining council system. For example in 1994 69 out of 75 agreements were subject to extension. A further implication of the new LRA is that there will be more agreements as other industries are brought into the bargaining council system and most of them will be subject to extensions. This coupled with the increased coverage suggests that the bargaining council system will have a far greater impact on the South African Labour than it did in the past.

In response to the criticisms of the extensions proponents cite the existence of exemptions. Opponents, however, believe that the system of exemptions is inefficient, biased and ineffectual. In relation to the number of employers the number of exemptions granted is small, only eight percent. When looking at the interplay between the three issues, coverage, extensions and exemptions the above analysis suggests that the negative impact of the bargaining council system is going to get worse. In my opinion this implies that there will be an increase in the level of unemployment as

firms find it more difficult to operate. The models in chapter one substantiate this; especially the neo-classical model coupled with the institutional aspects of the system highlighted in chapter two. If the bargaining councils are in any way responsible for any level of unemployment as claimed by Moll and COFESA then the strengthening of their powers will lead to more unemployment.

Discussions with COFESA revealed that the bargaining councils have an effect on the cost structures of firms and the firm's decision-making capacity. However, the effect does not work through the wage setting mechanism, it works through the regulation of employment practices. The regulations increase the costs for firms and constrain the firm's ability to adjust the size of its labour force. The result of this is that firms employ fewer workers than they would if they were not covered by the bargaining council agreements.

The final chapter presents the results from a survey that I conducted for the World Bank in the beginning of 1997. The purpose of the survey was to answer questions related to coverage, exemptions and extensions as well as to establish the degree of compliance with bargaining council regulation. This last point is possibly the most important objective. This will give an indication of whether the bargaining council regulations are binding.

CHAPTER 4

SURVEY OF THE EFFECT OF BARGAINING COUNCILS REGULATIONS: A CASE STUDY OF THE MOTOR INDUSTRY AND THE IRON, STEEL, ENGINEERING AND METALLURGICAL INDUSTRY

Introduction

This chapter will present the results from a survey conducted by the World Bank in March 1997. It has been argued that the regulation of wages and working conditions exercised by Bargaining Councils tends to reduce employment, particularly at the small-firm end, where techniques are more labour intensive and wages are lower. Interviews with some businesses and with business associations have revealed that at least some businesses find the Bargaining Council regulation to be a burden. From various sources (Bargaining Councils, the unions and interviews with some firms) it is clear that compliance is virtually 100 percent among firms with significant union representation. However, there is some debate as to the level of compliance among smaller non-union firms, the fundamental purpose of the survey is to obtain a better understanding of the factors that are associated with compliance.

The survey is for logistic reasons focused on two of the largest manufacturing sub-sectors, namely: The Motor Industry and the Iron, Steel, Engineering and Metallurgical Industry (or the Iron and Steel Industry). The choice of these two sub-sectors relates to the governments wish to expand employment and raise exports. These two have the capacity for both. Also they will provide a contrast in respect of wage levels, one being a high-wage industry (Iron, Steel, Engineering and Metallurgical Industry) and the other a low-wage industry (The Motor Industry). Both sub-sectors have relatively high numbers of workers and employers: they are the two largest Bargaining Councils in terms of the number of employees and number of firms covered.

Method

The survey apart from being limited to the two sub-sectors was also limited to two contrasting regions. This was because there is some regional variation in the minimum wages prescribed by the Bargaining Councils, and there may be differences in the degree of compliance across regions. The

two regions were Witwatersrand (Wits), which is the most heavily populated region and the region that contributes the largest share to GDP; and the Pietersburg, Nelspruit areas. The reason for selecting these is that both the Bargaining Councils have two types of regions with differential wages, and the objective was to choose areas that reflect this contrast. Iron, Steel, Engineering and Metallurgical industry has the "urban" and "rural" category. Wits (including Potchefstroom and Klerksdorp) is considered "urban" while Pietersburg and Nelspruit are considered "rural". The Motor Industry has "A" and "B", Wits is considered "A" while Pietersburg and Nelspruit are considered "B".

The sampling frame was obtained from the membership lists obtained from the Bargaining Councils. The Bargaining Council staff extracted lists of all the firms with no or very low union membership. The cut off percentage of unionization per firm was ten percent, however, due to practical considerations this was revised up to around thirty percent. This sample structure provides the best test of compliance from the point of view that if among non-union and low-union firms it is apparent that compliance is general then we can be relatively confident that the same is true of partially and fully unionized firms as well.

From the lists we obtained from the Bargaining Councils, a random sample was taken and 60 firms chosen from each list, 30 "urban" and 30 "rural". The first problem encountered was that for the Motor Industry there were 36 "rural" firms registered, so the entire list was used. Of the firms approached, 50 returns were obtained from the Iron and Steel and 24 from the motor industry sample. The regional split was roughly even, in the Iron and Steel 54 percent from the Witwatersrand region and in the motor 46 percent from the Pietersburg/Nelspruit region, and from the Motor industry 46 percent from the Witwatersrand and 54 percent from the Pietersburg/Nelspruit region. From of the overall sample, 26 percent of firms were located in central business districts, 57 percent in industrial parks, 16 percent in suburbs and only 1 percent from the townships. The sample is limited to the main business areas in the respective regions. The limited coverage of the townships is not problematic from the bargaining council's point of view as the businesses concerned are very small and are unlikely to be registered. Their impact is seen as minimal. This presents the problem of evasion. Small firms may be evading the bargaining councils by choosing a location where they are unlikely to be discovered. Thus the bargaining councils may be underestimating the number of firms in a particular industry and hence their coverage.

The sample is small and is not intended to provide definitive results as there is the possibility that it may not capture all the relevant information. Notwithstanding this, the results point to some interesting and important findings.

Results

With regards to production, 53 percent of the firms in the sample produced goods that are exported or ultimately end up as a component of an export good. percent produce consumer goods and of the goods aimed at consumers only 17 percent are luxuries. For the Motor industry 70 percent of the urban firms produce for exports whereas only 31 percent of the rural firms produce for export. This tendency is also seen as regards the Iron and Steel industry where 65 percent of "urban firms and only 43 percent of rural firms produce for export. This would indicate that the export industry is more concentrated in the urban areas such as the Witwatersrand.

Employer associations represent employers at the negotiations that take place within the Bargaining Council forum. In the survey firms were asked if they were a member of an employer association. For the Motor industry 67 percent of urban firms and 77 percent of rural firms were members, however, for the Iron and Steel industry 76 percent of urban firms and only 39 percent of rural firms were members. Overall membership in the sample is 65 percent. Thus it appears that in the Motor industry membership of employer associations is equal in terms of regions, however, in the Iron and Steel the rural areas are under represented relative to the urban areas. This can be inferred especially from the rural sample as the sample covered close to 100 percent of registered firms in those areas.

The sample covered 6905 employees, of these 32 percent were rural based. Unionization in the overall sample was 31 percent. The rural areas had 35 percent (Motor) and 36 percent (Iron and Steel) unionization, whereas the urban areas were lower with 29 percent for both industries. This would seem to indicate the presence of unionization differentials of around 6 percent. In these two industries there are separate rates for urban and rural wages.

Firms were asked whether they submitted monthly return's to the Bargaining Council. Of the firms in the motor industry 91 percent submitted returns (83 percent rural and 100 percent urban) and of the firms in the Iron and Steel industry 88 percent (87 percent rural and 89 percent urban) submit returns. These returns contain information as regards wages, medical aid contributions, pension contributions and any other pertinent information about the firm and its relationship with workers. The high level of returns indicates that there is a high level of compliance to Bargaining Council regulations. In discussions with Bargaining Council staff, if a firm does not submit returns then it is automatically inspected and audited for any irregularities, if any are found this would lead to litigation and ultimately cost the firm. Thus it is in the firm's interest to submit returns, however, these returns enable the Bargaining Council to keep watch on the entire industry. It is from these discussions and evidence from the survey that I can infer that regulations are binding.

In terms of policing the respective industry, a question was asked about how many visits the firm had received in the last 24 months. In the sample there were 97 inspections of 74 firms. This may seem somewhat small, an average of less than one visit a year. However, this coupled with the aspect of returns submitted as well as self policing through unions, other employers and employees informing on each other, it appears that the regulations are binding and are relatively universally applied in these two industries. The self-policing aspect arose from discussions with the bargaining councils. The councils said that they needed relatively few inspectors as compared with the number of firms in the respective industries. This is because employers, unions and workers report any firm that they know is not complying with the bargaining council regulations. Thus the bargaining councils see no need for numerous inspections as a result of this self-policing.

Exemptions

Exemptions are obtained from the respective Bargaining Councils on application. The granting of an exemption means for the employer the relaxing of regulations such as minimum wage regulations, working hours, pension/provident fund requirements and any other aspect of the respective agreements. Of the firms in the sample 40 percent (31 percent of Iron and Steel, 61 percent in Motor) applied for exemptions, 58 percent (48 percent of Iron and Steel, 73 percent in Motor) of those were granted fully and 11 percent (9 percent of Iron and Steel, 13 percent in Motor) partially.

In the Motor industry none of the applications were for relief from paying the regulated minimum wage, 54 percent were for the altering of working hours arrangements, 29 percent applied for exemption from the council pension and provident fund arrangements and, 70 percent applied for permission to have their own pension/provident fund. All except one firm still enjoy exemptions. In the Iron and Steel industry 40 percent of the applications were for lower wages, 27 percent were for the alteration of working hours, 33 percent for exemption from pension/provident funds and 25 percent were to have own pension/provident funds. Only 20 percent of these firms still enjoy exemptions.

The firms that had not applied for exemptions were asked why they had not applied. In the Motor industry 86 percent of firms said that the union would not permit it and 78 percent said it would not be worth it. Seventy eight percent said that they did not need one and all respondents said that the wages they were paying is fair and that in paying lower wages they end up with lower quality workers. All the firms also said that they felt that their application would be rejected so there was no

point in applying. In the Iron and Steel industry, 79 percent they did not need it, 96 percent said that the wage they were paying was fair with 85 percent believing that lower wages equals lower quality employees. Seventy percent said that the unions would not permit the granting of exemptions and 78 percent said the effort would not be worth it and 75 percent believed that their application would be rejected.

What is evident from the survey is that the conditions and procedures for exemption and the perceptions of them are vastly different for the respective industries. It seems that in the Motor industry it is easier to obtain an exemption than in the Iron and Steel industry. Considering that the survey was directed at smaller firms and it is these firms that have the greatest chance of obtaining an exemption under the conditions set out by the councils then it would appear that exemptions are likely to be less for the larger firms. Also the issue of the number of exemptions cannot be generalized across industries and different Bargaining Councils, rather one should look at the respective criteria and procedures of each Bargaining Council.

The results suggest that as regards wages, most if not all firms felt that wages were not a hindrance, rather that the wage being paid was fair. Furthermore, it was indicated that firms feel lower wages result in lower quality workers. This seems to indicate that there is a premium on quality and hence skill levels, i.e. they are prepared to pay higher wages for better quality workers. This issue was also raised in interviews with firms and they said that there are queues of people trying to get a job, however, they are unskilled and in order to attract the right level of worker for a particular job, they have to offer a higher wage.

Lastly, it became evident from discussions with firms in the survey that the perception of the Bargaining Councils is not a good one. Firms do not believe that their applications for exemptions will be granted and a reason for this is that firms do not perceive the process of exemptions as fair. They see it as a lottery due to a lack of consistency in the granting of exemptions and thus the time and effort entailed in submitting an application is not worthwhile in terms of time and cost versus benefit once the application has been granted.

Extensions

Firms were asked what they thought would happen to unskilled wage levels if the Bargaining Council agreements were no longer extended to non-parties, 57 percent believed that wages would hold steady, 43 percent thought wages would drop in some or most firms. When asked what would

happen to employment, 81 percent believed that employment would rise if the agreements were no longer extended. In the Motor industry 55 percent of urban firms and 92 percent of rural firms felt that employment will rise if agreements are no longer extended to non-parties, in the Iron and Steel industry 38 percent of urban and 81 percent of rural firms believe that employment will increase. When asked by how much, most firms believed it to be somewhere between 10 and 40 percent. In terms of region, in the Motor industry 69 percent of rural firms believe wages will hold steady and 31 percent believe they will drop, whereas only 50 percent of urban firms believe wages will hold steady with 40 percent believing they will drop. In the Iron and Steel industry 48 percent of rural firms believe that wages will hold steady with 52 percent believing they will drop and 60 percent of urban firms feeling that wages will hold steady with 40 percent backing the fall in wages.

Firms were then asked as to whether they thought output would increase if bargaining council agreements were no longer extended to non-parties? From the Motor industry 82 percent of urban and 80 percent of rural firms believed that output would increase. In the Iron and Steel industry 83 percent of urban and 81 percent of rural firms believed output would increase. For the motor industry 90 percent of firms sampled believed the increase would be between 10 and 40 percent and in the Iron and Steel 74 percent also believed that the increase would be between 10 and 40 percent.

Firms were then asked what they would do if agreements were no longer extended to non-parties? They were given the options of paying lower wages, changing working hours and changing provident/pension funds. In this regard, 94 percent of the Motor industry indicated that they would not lower wages or change working hours, 42 percent said they would change pension/provident funds. In the Iron and Steel industry 90 percent said they would not lower wages, 74 percent said they would not change working hours and only 33 percent would change pension/provident funds.

In order to establish the market for unskilled labour firms were asked if they hire workers on a piece rate. The results in both industries is identical, 87 percent said that they do not us piece rate workers. When asked if the would convert to this if they were allowed to by the Bargaining Council, 76 percent of the Motor industry and 64 percent of the Iron and Steel industry said they would not. In terms of regions, in the Motor industry 89 percent of urban firms and 67 percent rural firms said they would not convert, however, in the Iron and Steel industry 57 percent of urban firms said they would convert while 86 percent of rural firms said they would not. Having established this, firms were asked, if the firm could and it wanted to convert to piece rate would it be able to hire people to work on this rate? In the Motor industry 89 percent of urban firms and only 54 percent of rural firms said that they would be able to hire workers under those conditions. In the Iron and Steel industry 71 percent of urban and 65 percent of rural firms said that they would be

able to. This would seem to indicate that there is a greater supply of labour in the urban areas relative to the rural areas.

Conclusion

Even though the survey is limited to the Iron, Steel, Engineering and Metallurgical Industry and the Motor Industry, it yields some useful insights into the issue of compliance and impact of bargaining councils. From the returns it appears that bargaining council regulations are binding and are followed by the majority of firms in the respective industries. There does seem to be a difference between urban and rural regions. The results of both industries in urban and rural regions are commensurate exhibiting essentially the same trends.

As regards exemptions, the only clear result is that there is not a coherent manner in which they are evaluated and granted. The types of application appear to be relevant for example, none of the firms in the Motor Industry applied for relief from minimum wages whereas in the Iron and Steel Industry 40 percent of the applications were for minimum wage relief. On the other hand seventy five percent of firms in the Motor Industry applied for permission to have their own pension/provident funds whereas only 25 percent of the Iron and Steel Industry had applied for the same. These differences hint at the possible structural differences between the respective industries and the actual functioning of the respective Bargaining Councils. However, there is not sufficient information to ascertain which is the main cause.

An important implication that surfaces when firms refraining from application for exemptions were asked why, almost all of the respondents believed that the wage that they are paying is fair and hence do not need relief. Furthermore, they believed that lower wages yielded lower quality workers. This would suggest the existence of skill differentials and that a premium is paid for skills and greater productivity. This indicates a shortfall in skill levels and an inherent lack of productivity among the unemployed workers as well as the fact that existing workers are inflexible to wage cuts.

Most firms said that they could hire extra workers on a piece rate, however, there appears to be a significant difference between urban and rural replies. More urban employers indicated that they could hire more workers than did rural employers. This would tentatively suggest that there is a greater supply of workers in the urban setting. Notwithstanding this, the fact that most firms said they could hire more labour points to a surplus of labour.

In terms of the halting of extensions of agreements, except for the Iron and Steel Industry in the rural area, the majority of firms believed wages would hold steady if extensions were no longer allowed. The majority of firms also believed that employment and output would increase (mostly in the 10 to 40 percent ranges) if the extensions were no longer in place.
Firms' are consistent in saying that the level of employment would increase if the extensions were dropped but also that wages would hold steady. This alludes to the constraints that firm's face under bargaining council regulations in terms of the amount of labour that they hire. Firms are constrained in their ability to hire and fire workers by the bargaining council regulations, i.e. it is difficult for firms to retrench workers when the firm no longer has the use for them. Thus the firm will hire less workers than it otherwise would in case it falls on hard times and ends up with too big a labour force that it has to pay every month. If the bargaining council agreements no longer existed then the firm would easily be able to adjust to changing conditions and could employ the required number of workers at all times. The implication of this result is that wages do not seem to be the issue in terms of the number of workers employed rather it is the regulation of the conditions of employment as set out in the bargaining council agreements. This is further corroborated when the firms say that the wage they are paying is fair.

Applications by firms for permission to have their own pension/provident funds indicate that the bargaining council pension/provident funds are a problem, especially in the Motor Industry. This seems to substantiate the argument that the bargaining councils raise the administration costs of firms. The reason for their applications is that the council's pension/provident funds are costing the firm too much. Thus if the firms moved to their own pension/provident funds they could cut those costs. This implicitly supports the argument that bargaining councils increase the administrative costs of firms.

In sum, the main implications of this survey are that bargaining council extensions decrease the level of employment and that the regulations are binding and are followed by firms in the industry. Furthermore the results hint at aspects of the bargaining council system that have not been taken into account by the theoretical models. In this regard the neo-classical model seems to be misdirected in focusing mainly on the wage effects. The structuralist model also neglects the above features, although, the efficiency wage argument is pertinent in explaining the level of wages in terms of skills and productivity. This implies that the firms must pay the current level of wages in order to secure the required level of skills and productivity. Thus the level of wages does not impact on the firms decision regarding the number of workers it employs. Rather it is the institutional structure of the bargaining council system that introduces rigidities into the industry that impacts on employment levels.

CHAPTER 5

CONCLUSIONS

The underlying objective of the industrial council system was the promotion of selectivity. Although the kind of selectivity has changed, the underlying objective remains the same. It is the promotion of interests of a select group namely, unions and employers that are party to the negotiation of agreements. The parties' motivations may differ from each other but are entirely consistent with the notion of selectivity. The unions seek to create a closed shop and the employers want to create barriers to entry and reduce competition from other (normally smaller) firms. Given the history of the industrial council system, it would be naïve to think that renaming them and increasing their powers would convert them into a useful labour market institution. It is true that labour markets practically never operate as efficiently as one would like. The point is to get the labour market functioning as efficiently as possible, however, reliance on a system that is grounded in apartheid is in my view incorrect. The bargaining council system that was created by the new Labour Relations Act is not much different from the old system. The same people still hold the same positions and the old biases are still evident. That is to say that the rent seeking behaviour of the negotiating parties is still prevalent. Thus as a mechanism that has the purpose of protecting certain groups such as union employees and big business, the bargaining councils are no different from the old industrial councils.

Moll's first model provides insight into how this works. The contention is that the larger more capital intensive firms have higher costs especially on the labour side, as they need more skilled labour. At present South Africa has a shortage of skilled labour and thus a premium is paid for skills. The smaller firms tend to be more labour intensive and have lower labour costs. Through the negotiations and formalizing of agreements the larger firms are able to affect the cost structure of all firms in the industry. In effect the larger firms create a situation where they pay less wages than they otherwise would have to and the smaller firms pay higher wages than they do. The important aspect of this model is the distinction between the cost structures of large and small firms.

The structuralist view is insightful in analyzing the conflict between labour and firms resulting from their respective needs for security and flexibility. The structuralists believe that there is a trade-off between them, i.e. for workers to have more security means that firms have less flexibility. The

balance between them is achieved through negotiation within the bargaining council forum. However, the structuralist view does not account for the abuse of the bargaining council system that emanates from the old industrial council system. The structuralist approach, in opposition to the neo-classical approach, focuses mainly on the effects of productivity with the argument that it is unit labour costs that are important for the firm and not merely wage rates. This view argues that wages and productivity as positively related and if there is a decrease in the wage level then productivity will decline. The main implication of this view is the existence of efficiency wages. These imply that a premium is being paid for skills and higher levels of productivity. Therefore if bargaining council extensions were no longer enforced the wage levels would remain relatively the same. This is corroborated in the survey when firms said that the wage they are paying is fair and that if the extensions were no longer enforced, they would not lower the wage levels. Furthermore, in discussions with firms in the survey it became evident that they had to pay higher wages in order to attract workers with the required skill levels. Given this it appears that the neo-classical model is incorrect in its contention that the effects of bargaining councils work through wages. However, the neo-classical argument regarding different cost structures and the effect of bargaining councils on the cost structures of smaller firms is correct. The structuralist approach in focusing only on unit labour costs neglects the impacts of other costs and the regulation of the employment environment.

The results of the survey indicate that bargaining council regulations are binding and affect the operations of employers. The results corroborate the argument that bargaining councils affect the firms in two ways, firstly through the increase in administration costs such as cost of sending returns to the council every month and contributions to pension funds. Secondly, through the councils' effect on the decision-making capacity of firms. It is this second point that forms the basis of the rigidity. Firms are bound by the extension of the agreements to follow procedures in the hiring and firing of employees. These procedures make it extremely difficult for firms to alter the size of their labour force. In other words, firms cannot easily reduce the size of their labour force should the conditions within the industry dictate that they should. Knowing that they operate under this constraint firms employ a smaller permanent labour force and use part time labour if the need arises. They do this to avoid the risk that they may find themselves in the situation where they are paying for labour that they do not need. This means that the employment levels are below what they would have been without the extensions. This phenomenon constitutes the rigidity.

Furthermore, administration costs especially for the smaller firm's form a significant part of their overall costs. Thus the level of these costs has a large impact on the firms profitability. These costs can result in the firms employing less labour in order to cut costs and may even cause firms to close down. These effects are greater in the case of the smaller firms as the larger firms find it much

easier to internalize them. The effects of the rigidity are greater for the smaller firms than for the larger firms especially those that take part in the negotiating process. One can infer this because the larger firms that take part in the negotiations would not agree to those conditions if they adversely affected their operations. However, the conditions do adversely effect other firms that were not involved in the negotiations. Therefore the bargaining council system will not achieve equitable or efficient outcomes in the labour market and will result in higher levels of unemployment.

The argument of this paper that bargaining councils do increase unemployment has important implications for the South African labour market. The new LRA strengthens the powers of the bargaining councils and promotes their formation in industries where they do not already exist. Thus it appears that the bargaining council system is here for the foreseeable future. The expansion of the bargaining council system in terms of this paper suggests that unemployment is likely to increase and the goals of equity in the labour market are not likely to be achieved. Furthermore, the system is unlikely to increase the levels of training and education in the labour market while the bargaining council agreements constrict the firm's ability to make decisions about its labour component. South Africa is under pressure from international competition both for domestic and international markets, however, the constraints placed on firms will mean that they become less competitive in the international market place. This in turn has severe negative implications for growth and development, namely that growth will not reach its full potential and in turn this will hamper development. Thus the government's GEAR program will be placed in jeopardy.

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