

## opinion

By Johan Fourie



### MINIMUM WAGE

# Rebel with a cause

Anyone who questions the implementation of a minimum wage in South Africa will be met with fierce opposition. But the merits (and demerits) of such legislation require broader debate. Even if this is an unpopular notion.

In the 1990s, Paul Krugman, who later won the Nobel prize for his work on trade, wrote: "There is nothing that plays worse in our culture than seeming to be the stodgy defender of old ideas, no matter how true those ideas may be. Luckily, at this point the orthodoxy of the academic economists is very much a minority position among intellectuals in general; one can seem to be a courageous maverick, boldly challenging the powers that be, by reciting the contents of a standard textbook."

Krugman wrote to explain comparative advantage: the idea that trade between two countries raises the incomes of both. It's a simple and powerful idea, first proposed by David Ricardo, and was responsible for the massive expansion in global trade in the second half of the 19th century. Yet, it's surprisingly unpopular. Why? Because it is intellectually unfashionable. Says Krugman: "Free trade ... has some sort of iconic status among economists; so, in a culture that always prizes the avant-garde, attacking that icon is seen as a way to seem daring and unconventional."

How valid this statement is about the SA labour market.

Every economics student is taught supply and demand. Equilibrium price and quantity is where the supply and demand curves intersect. Workers demand jobs while firms supply jobs. The equilibrium price is the wage. A government-sanctioned regulation that fixes the wage – like a minimum wage – above the market equilibrium means that demand will exceed supply, creating a job shortage – in other words: unemployment.

This is standard first-year economics. Yet the belief that a minimum wage will have no effect on SA's already record-high unemployment rate is deeply entrenched by both Krugman's avant-garde intellectuals and opportunistic politicians and labour union leaders. Any attempt at debate is dead-batted. Proponents happily circulate articles that show a weak or even zero correlation between minimum wages and unemployment, disregarding the fact that these are often about workers in Seattle rather than Soweto.

They argue that higher wages will result in higher levels of spending in the economy, boosting growth, but ignore the fact that higher wages must be paid by someone else, reducing spending by the same amount. When they run out of credible arguments, they play the man, not the ball, labelling those hoping to debate the merits and demerits of minimum wages "apartheid apologists".

This is a tragic state of affairs, for two reasons. First, there are credible reasons to have minimum wage legislation, and good research to back up the claim that not all minimum wages inevitably result in higher unemployment. But this requires the details of each case.

As economist Tim Gindling writes on minimum wage legislation in developing countries: Minimum wages can either increase or decrease unemployment depending on the characteristics of the labour market. Minimum wages target formal sector workers, but in most developing countries formal sector workers are the minority and, importantly, not the poorest. How minimum wages affect the poorest depends on things like the size of the informal labour market, distribution of income and available social safety nets.

Secondly, the impact of the new National Minimum Wage (NMW) Act, implemented from 1 January, has almost entirely escaped discussion in the run-up to national elections. The Act set a NMW across sectors at R20/hour per worker with two exceptions: agricultural workers had a lower rate of R18/hour and domestic workers and gardeners R15/hour.

It's clearly too early to know whether the Act did increase unemployment, but let's turn to research about the impact of earlier such legislation. In some sectors, like agriculture and textiles, higher minimum wages seem to have had large negative effects on employment. This may be because these sectors had limited labour productivity growth in the past two decades. Higher minimum wages simply pushed the equilibrium wage above what employers could afford.

This comes as no surprise: Treasury officials and most academic economists predicted that minimum wages will cause job losses – the same prediction they have made for the most recent legislation as well. But minimum wages did not lead to higher unemployment in all sectors, largely because employers assumed that the legislation wouldn't be enforced. They have therefore continued to pay their workers below minimum wage, which meant they could retain most jobs. Even the SA government shirks the minimum wage: Workers employed on one of its expanded public works programmes are entitled to a minimum wage of R11/hour.

Minimum wages can only do so much to lift the incomes of the poorest. If it rises too quickly, without keeping track of labour productivity, employers will find alternatives – either by substituting capital for labour or by shifting production to countries with cheaper wages or higher labour productivity. Both will deepen the unemployment crisis.

Instead of minimum wage legislation, which ultimately has limited power to affect radical economic transformation of society, we desperately need innovative economic policies that boost labour productivity. Perhaps it's time for a courageous maverick to boldly challenge the powers that be. Weapon of choice? A standard economics textbook. ■

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Workers participate in a strike called by the South African Federation of Trade Unions (Safu), in April 2018, after it said workers were not consulted in the setting of what was then still a proposed minimum wage.