The Impact of the Employment Equity Act on Employment Strategies of Firms

In the latter half of 2015 the South African Department of Labour announced its plans to take approximately 1,400 firms to the labour court for failure to comply with the Employment Equity Act of 1998. This announcement linked to the 2014-15 report of the Commission for Employment Equity which found that the pace of transformation of the private sector had remained slow. With threating significant financial fines for non-compliance, the Minister of Labour tries to accelerate the transformation of the South African workforce, a key goal of the post-apartheid government since the mid-90s. While transformation has to be a key objective in South Africa given its history, little is known about the responses of firms to such policies in term of intended and unintended outcomes.

Research done by the AMERU at University of the Witwatersrand unpacks the effect of the Employment Equity Act of 1998 on the employment strategies of South African firms when the Act was first implemented in 1998. This should provide some insights on possible future firm responses when the minister acts on her threats. Given that the Act only applies to firms with 50 or more employees, the research exploits the firm size threshold in order to use a Regression Discontinuity Design. The findings indicate that this threshold policy results in two distinctly different groups of firms once the act was passed with each group treating their labour to capital ratios in a different fashion. A larger group opted to shed employment in order to remain below the threshold for compliance with the Act, and instead embracing higher levels of capital (Figure 1).

In the period of 1996 employment (blue line) showed no noticeable patterns by firm size. However, after the EEA was passed in 1998, the employment by firm size (red line) shows significant clustering below the 50 employee threshold. This suggests that firms have an incentive to remain small in order to dodge labour legislation. Results further suggest that this reduction in the number of workers was accompanied by an increase in the ratio of skilled to unskilled workers. Therefore, the Act itself could be a significant obstacle to the creation of the types of firms that are most likely to hire unskilled labour, the type of workers that are most in danger of facing unemployment and are supposed to be targeted as part of the transformation agenda.

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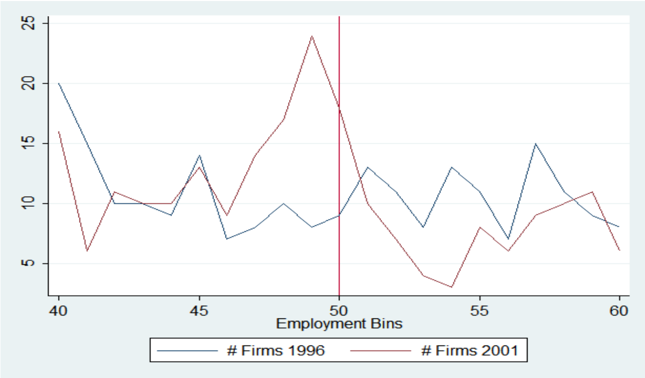
Figure 1: Number of firms per employment bracket in 1996, and 2001



The research results also suggest that the introduction of the Employment Equity Act of 1998 resulted in an inefficient allocation of resources at the firm level, particularly at the small, medium enterprise level, marking the intended effect of the particular Act to increase employment of designated groups as counterproductive. While it is not clear if firms merely shed employment through firing and retrenchment practices or if firms simple allowed for basic attrition of the workforce and instead employed labour brokers to provide indirect labour going forward, it still affected one segment of the workforce most: incentivising firms to push unskilled labour into increasingly precarious employment. With the South African government currently extending labour policy to cover workers in 'precarious employment', primarily part-time and contract workers there should be concern that these amendments strengthen the position of those already in formal jobs at the cost of the very workers that are supposed to benefit from these policies.

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