POLICY BRIEF

Financial and Fiscal Commission (2022)

Youth unemployment and intergovernmental fiscal relations in South Africa

Executive Summary

The government has, over the years, committed significant resources in terms of policies, legislation and programmes to address the unemployment crisis, especially youth unemployment. South Africa has also set up many publicly funded institutions or agencies to address employment, focusing on youth development and employment initiatives. These institutions include the National Youth Development Agency (NYDA), Sector Education and Training Authority (SETA), Youth Employment Service (YES) programme and, more recently, the Presidential Youth Employment Initiative (PYEI) to promote youth development and employment. These interventions are funded using intergovernmental fiscal instruments such as conditional grants and equitable share allocations to boost employment creation.

To understand the effectiveness of the fiscal framework and relevant public institutions in addressing youth unemployment challenges, the Commission employs a descriptive budget analysis and econometric estimation. The econometric evidence shows that government spending has not resulted in a reduction in unemployment. However, spending on gross fixed capital formation (government investment) has caused unemployment to decrease. In other words, government spending has not effectively addressed unemployment compared to investment. Therefore, the Commission recommends that the proportion of gross fixed capital formation expenditure in the budget composition should progressively increase. The evidence also shows that government labour market interventions have resulted in some economic opportunities at a micro level for young people. Still, these interventions have had no significant impact on reducing the high unemployment rate. Policy needs to break the silo approaches between government departments to promote better efficiencies and synergies.

FINANCIAL AND FISCAL COMMISSION

THE FINANCIAL AND FISCAL COMMISSION

The Financial and Fiscal Commission is a body that makes recommendations and gives advice to organs of state on financial and fiscal matters. As an institution created in the Constitution of the Republic of South Africa, it is an independent juristic person subject only to the Constitution itself, the Financial and Fiscal Commission Act, 1997 (Act No. 99 of 1997) (as amended) and relevant legislative prescripts. It may perform its functions on its own initiative or at the request of an organ of state.

The vision of the Commission is to provide influential advice for equitable, efficient and sustainable intergovernmental fiscal relations between national, provincial and local spheres of government. This relates to the equitable division of government revenue among three spheres of government and to the related service delivery of public services to South Africans.

Through focused research, the Commission aims to provide proactive, expert and independent advice on promoting the intergovernmental fiscal relations system using evidence-based policy analysis to ensure the realisation of constitutional values. The Commission reports directly to both Parliament and the provincial legislatures, who hold government institutions to account. Government must respond to the Commission's recommendations and the extent to which they will be implemented at the tabling of the annual national budget in February each year.

The Commission consists of commissioners appointed by the President: the Chairperson and Deputy Chairperson, three representatives of provinces, two representatives of organised local government and two other persons. The Commission pledges its commitment to the betterment of South Africa and South Africans in the execution of its duties.

Background

The prevailing high levels of unemployment have affected the youth more than other sections of the population. There is a broad consensus that youth unemployment in South Africa is at crisis levels and constitutes a national emergency. The high level of youth unemployment can lead to an increased feeling of exclusion and frustration, resulting in instability. Youth unemployment is estimated at 66.5% for youth aged 15–24 years and 43.8% for youth aged 25–34 using the official definition (excluding discouraged work seekers), compared to 35.3% of national unemployment.

The prevailing high levels of unemployment are not the outcome of a lack of effort from a wide range of sectors and stakeholders in trying to address youth unemployment. A wide range of policies and interventions have focused on addressing the challenge of youth unemployment. Interventions have included using intergovernmental fiscal instruments such as conditional grants and equitable share allocations to boost employment creation. The Employment Tax Incentive (ETI), Expanded Public Works Programme (EPWP) and the recently established Jobs Fund to contribute to the objective of job creation are other interventions. The government has committed significant resources to promote the growth and employment needed to build on recovery following a deep contraction due to COVID-19. For example, the government allocated R24.8 billion for employment programmes[1] for 2022/23. The allocation increased from the estimated expenditure of R21.6 billion in 2021/22. Over the Medium-term Expenditure Framework (MTEF) period (2022/23 to 2024/25), the government plans to spend R76 billion on employment programmes.

Research findings

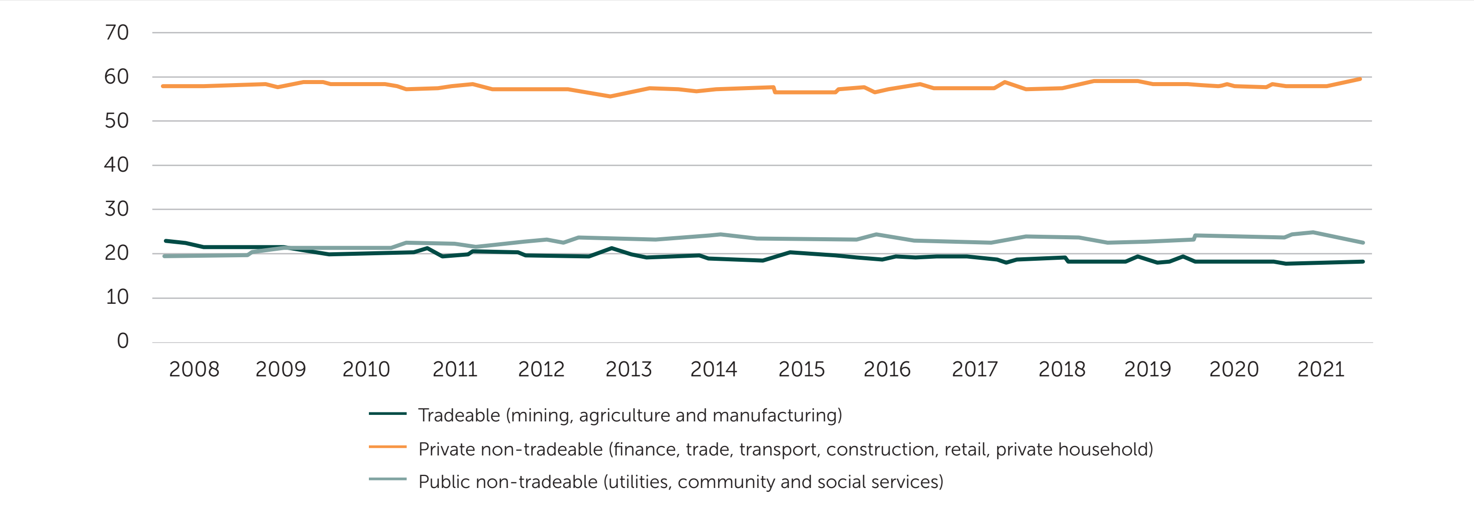
1. Government spending and unemployment

The econometric evidence shows that government spending has not resulted in a reduction in unemployment. However, gross fixed capital formation contributes to the decrease in unemployment. Therefore, capital payments that capture the government's contribution to capital formation and spending on new infrastructure and upgrades, additions, rehabilitation and the refurbishment of existing infrastructure should progressively be increased. The observed effect of government spending on unemployment results from the structural nature of South Africa's unemployment. Structural unemployment results from shifts in the economy, improvements in technology, and workers lacking the job skills required to find employment. Conversely, cyclical unemployment is related to swings in the business cycle and periods of negative growth, such as recessions.

Figure 1 shows the shifts in the percentage of employment by sector. The percentage of employed people in tradeable sectors (mining, agriculture and manufacturing) has declined relative to private non-tradeable sectors. The weakness in export-oriented sectors has denied South Africa growth and employment creation opportunities. The importance of export-oriented sectors is that there is no need for local demand to rise for them to take off. The pattern of structural change is also a key driver of unemployment because tradable activities, especially manufacturing and agriculture, absorb more low-skilled job seekers than services. The ongoing pattern of structural change implies a significant decrease in the relative demand for low-skilled labour because the declining sectors constitute the least skill-intensive parts of the South African economy.

[1] Employment programmes include the Expanded Public Works Programme, the Community Works Programme and the Jobs Fund.

Figure 1: Percentage of total employment by sector



Source: *Commission's calculations based on Statistics South Africa data*

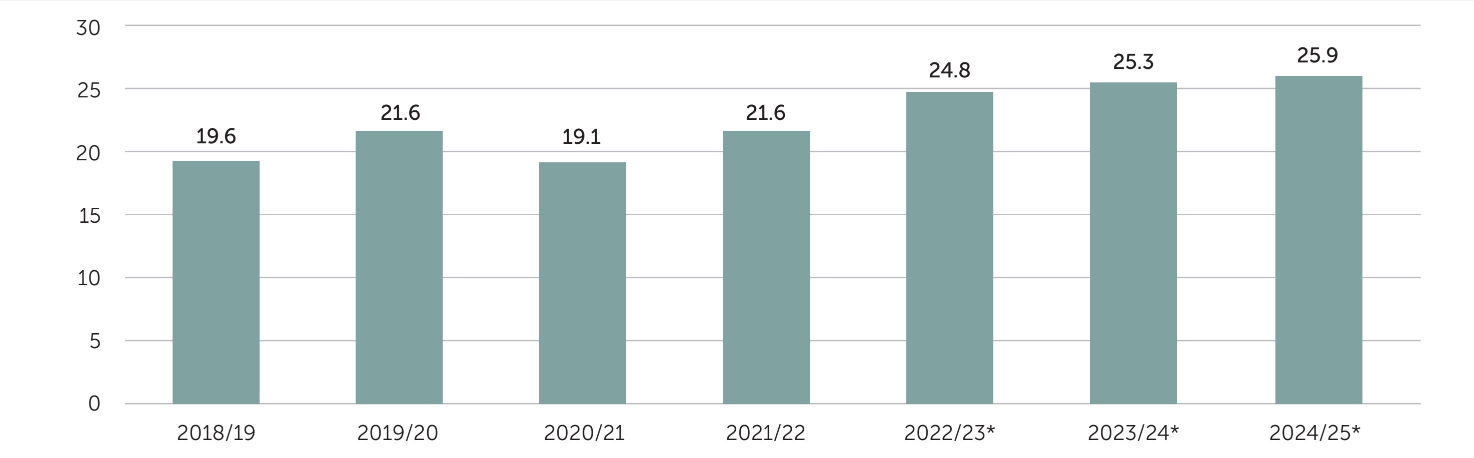
Many young people in South Africa are unskilled or lack the skills required in the labour market. In other words, the limited skills among the youth, coupled with low secondary school completion rates mean that many young people are at a considerable disadvantage in finding employment in an economy biased towards high skills services activities. But the demand for high-skilled workers means that those with high qualifications are more likely to find employment. The challenge of youth unemployment is a structural issue that requires long-term solutions, such as massive structural economic reforms.

2. Labour market programmes and youth unemployment

The government has committed significant resources to promote the growth and employment needed to build on recovery following a deep contraction due to COVID-19. The government aims to stimulate the economy through public employment programmes and tax incentives, while implementing reforms that ease the skills constraint and make it easier to do business. Figure 2 shows that the government allocated R24.8 billion to employment programmes[2] for 2022/23. The allocation increased from the estimated expenditure of R21.6 billion in 2021/22. Over the MTEF period (2022/23 to 2024/25), the government plans to spend R76 billion on employment programmes. Some of this expenditure will be through the Presidential Youth Employment Intervention, which aims to create over 500 000 short-term jobs.

[2] Employment programmes include the Expanded Public Works Programme, the Community Works Programme and the Jobs Fund

Figure 2: Employment programmes R'billion



Source: *National Treasury, 2022*[3]

Short-term jobs play an important role in providing work experience for the youth and first-time entrants, and facilitate entry into the labour market. Short-term employment also plays a vital part in providing income support and mitigating the effects of poverty, and boosting household consumption. Despite the critical role played by short-term work, sustainable long-term work still offers more benefits.
Employment Intervention, which aims to create over 500 000 short-term jobs.

Table 1: Labour Market Programmes

Intervention	Purpose
Employment Tax Incentive	The ETI is a tax incentive that aims to encourage employers to employ the youth. It was implemented with effect from 1 January 2014. It aims to reduce the employer's cost of hiring young people through a cost-sharing mechanism with the government, allowing the employer to reduce the amount of Pay-As-You-Earn (PAYE), while leaving the wage received by the employee unaffected.
Jobs Fund	One of the main objectives of the Jobs Fund is to co-finance projects by public, private and non-governmental organisations that can significantly contribute to the objective of job creation. It involves using public resources to catalyse innovations and investments on behalf of different stakeholders in activities that contribute directly to employment creation in South Africa.
Extended Public Works Programme	The EPWP is a government intervention aimed at contributing to government's priorities of decent work and sustainable livelihoods, education, health, rural development, food security and land reform, and the fight against crime and corruption. The objective is to create work opportunities for poor and unemployed people in South Africa. In this intervention, public bodies from all spheres of government and the non-governmental sector (supported by government incentives) are anticipated to create work opportunities for the unemployed in South Africa through delivering public and community services.
National Youth Development Agency	The NYDA operates in a context of legislative frameworks, such as the National Youth Development Agency Act, the National Youth Policy and the Integrated Youth Development Strategy, as adopted by the Youth Convention of 2006. The institution was established to address youth development issues at the national, provincial and local government levels.
Sector Education and Training Authority	The Sector Education and Training Authority (SETA) is a vocational skills training organisation in South Africa. There are currently 21 SETAs in different sectors in South Africa. Each SETA has the responsibility for managing and creating learnerships, internships, skills programmes and apprenticeships within their jurisdiction.

[3] National Treasury, 2022. Budget Review 2022. Republic of South Africa.

A further review of selected labour market interventions and institutions illustrated in Table 1 shows that government labour market interventions have resulted in some economic opportunities at a micro level for young people, but they have no significant impact on reducing the high unemployment rate. In other words, the success at the micro level has not translated into changing the pattern of high unemployment. The lack of coordination of labour market programmes and the absence of a robust private sector voice contribute to significant inefficiencies. Different departments offer similar programmes for similar target groups or offer potentially complementary programmes without exploiting such complementarities. Some programmes underperform in their potential to support job seekers, and synergies are not used to create comprehensive support for them.

The programmes are not aimed at tackling the structural roots of the unemployment problem, but focus on short-term work opportunities because of the constrained nature of work in some industries where it is most commonly involved (such as once-off maintenance projects). Creating temporary rather than sustained employment (which would be more suitable in the context of South Africa's unemployment challenge) means that they are limited in their ability to address the deeper problem of unemployment in South Africa.

Conclusion and recommendations

The unemployment situation in South Africa has become dire. It has received substantial attention from both policy and research. The policy frameworks and interventions that support youth employment remain uncoordinated, without solid implementation plans and no overall accountability. A more integrated and impactful approach to pathing young people to the labour market is required. This would encompass a significantly improved basic education system with the ultimate result of inclusive economic growth. To address the challenge of unemployment sustainability, which is primarily structural rather than cyclical, the proportion of gross fixed capital expenditure in the composition of the budget profile should be systematically increased. Consumption expenditure should be reduced. There is a need to remove structural and institutional rigidities that impact on private investment in the reduction of unemployment.

Lastly, South Africa requires, among other things, inclusive economic growth. A stable macro economic policy environment, foreign direct investment, an infrastructure base, an education system and regulatory frameworks that facilitate growth and employment are essential. Government should implement growth-enhancing structural reforms that promote economic transformation, support labour-intensive growth and create a globally competitive economy.

The Commission makes the following recommendation:

1. The proportion of gross fixed capital expenditure in the composition of the budget should be systematically increased. Consumption expenditure should be reduced, and there is a need to remove structural and institutional rigidities that impact on private investment in the reduction of unemployment.

2. To better target and increase the impact of the incentive, the Commission recommends revising the employee eligibility age from 18 to 29 years old. The age group 24–34 years has a relatively high rate of individuals not in education, employment or training (NEET) compared to 15- to 24-year-olds. National Treasury can also consider deepening the ETI to encourage hiring young women whose NEET rate is relatively higher than that of their male counterparts for both youth categories.

3. The Department of Employment and Labour, the Department of Higher Education and Training, and the Department of Women, Youth and Persons with Disabilities should coordinate all labour markets and skills programmes. The Department of Women, Youth and Persons with Disabilities has a mandate of enabling the empowerment and socio-economic upliftment of the youth and women. Well-coordinated labour market interventions could bolster the impact of existing labour market programmes through more significant integration and leveraging of initiatives.

Enquiries:

Siyanda Jonas
Siyanda.Jonas@ffc.co.za

Financial and Fiscal Commission
Montrose Place (2nd Floor), Bekker Street
Waterfall Park, Vorna Valley, Midrand

Private Bag X69, Halfway House, 1685

www.ffc.co.za

Midrand Office Telephone: +27 (0) 11 207 2300
Cape Town Office Telephone: +27 (0) 21 487 3780