

FINANCIAL AND FISCAL COMMISSION
POLICY BRIEF

7/2013

Moderating Provincial Wage Bill Growth and Enhancing Productivity

EXECUTIVE SUMMARY



Expenditure on the public sector wage bill continues to rise, especially in provincial departments, yet these increases do not translate into improved productivity, which is inconsistent with the international literature. Reasons for this increase are varied and include the annual cost of living adjustments, the increase in government employee headcount, vacancies for critical skills not being filled (leading to the appointment of contract workers and appointments being made without proper planning and budgeting), and the influence of trade unions on the outcome of wage bargaining agreements. The analysis focused on provincial health and education departments, which have proportionately larger personnel budgets than other departments. It found that personnel expenditure does not affect short-term economic growth, implying that personnel expenditure could be reduced without compromising economic growth. However, productivity increases are also critical and could be achieved through a more appropriate skills mix and an efficient balance of spending on personnel, capital, and goods and services. Government departments should develop norms for frontline versus administrative staff and establish the necessary controls to monitor employee compensation expenditure against those norms. Methods for improving productivity should also be considered, such as streamlining workflow.

BACKGROUND

The public sector wage bill has been at the centre of controversy and conflict, not only in South Africa but also internationally. While payment of reasonable wages is vital for the integrity and motivation of public officials, issues such as sustainability, productivity and affordability cannot be ignored. The public sector wage bill is inherently complex, as many stakeholders are involved, each with different interests (i.e. government, trade unions and political groups) and has consistently constituted the largest component of government's current expenditure. Despite additions to Medium Term Expenditure baselines to cover personnel costs, over-expenditure on the public sector wage bill persists, especially in provincial departments. Legislation and policy are in place for managing the public sector wage bill, but in general their implementation by the respective departments has been very weak, particularly at provincial level. The Financial and Fiscal Commission's research examines the underlying drivers of the growth of the provincial wage bill and its effect on economic growth.¹

FINDINGS

A descriptive analysis of trends and modelling were used to examine the public sector wage bill data and to assess the key drivers that explain the upward spiral of total personnel costs. The assessment looked at the status quo, cost drivers (employment headcount, staff mix – between frontline delivery and support staff – and salary notches), and the effect of social spending on economic growth. The focus was on provincial departments of education and health, which have proportionately larger personnel budgets compared to other departments. Health and education are labour-intensive in nature, so any adjustments related to personnel will have a far greater effect than in other sectors.

The rising provincial public sector wage bill in South Africa is a complex issue. Reasons for the upwardly spiralling wage bill are varied and include: the annual cost of living adjustments coupled with promotion and job re-grading; the increase in government employees; the introduction of the occupation specific dispensation (OSD),² poor internal controls (poor management of the antiquated personal salary (PERSAL) system); vacancies for critical skills not being filled (leading to the appointment of contract workers and appointments being made without proper planning and budgeting); poor organisational designs (strategic plans not aligned with organogram); policies initiated at national level with little regard to the enormous financial implications on provincial administrations; the equalisation of service conditions (salary increases provided for low-income earners); and the influence of trade unions on the outcome of wage bargaining agreements. This last reason may explain the research finding that increases in the wage bill do not translate into an increase in productivity, which is inconsistent with the international literature. Other factors that could play a role include poor supervision and management of frontline staff.

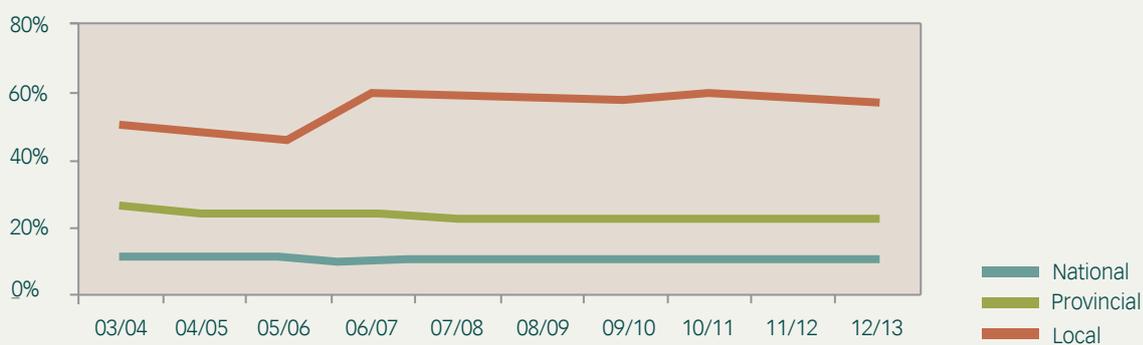
Of the three government spheres, provinces spent by far the most on personnel costs and as a proportion of total expenditure, increasing from 50 to 58 per cent between 2003/04 and 2012/13. In contrast,

¹ For the full study, see Madubula, N and Dawood, G. 2013. Managing the provincial wage bill to contain fiscal stress and build a capable State, Chapter 4 in Financial and Fiscal Commission (2013). 2014/15 Submission for the Division of Revenue Technical Report, Midrand, South Africa.

² The OSD emanated from the resolution taken in 2007 by the Public Service Coordinating Bargaining Council, introducing a new dispensation of revised salary structures that are unique to specific skilled occupations such as educators, health professionals and certain categories of professionals. The aim of the OSD was to improve Government's ability to attract and retain skilled employees through improved remuneration.

as Figure 1 illustrates, the national and local spheres marginally reduced the ratio of personnel expenditure to total expenditure during the period 2006/07–2012/13. The functions assigned to each sphere determine to a large extent the personnel expenditure to total expenditure ratio. For example, national government is not directly involved in service delivery implementation and would not be expected to spend the same proportion of its budget on salaries as provincial and local government. In contrast, functions assigned to provincial government include education and health, which are traditionally labour-intensive. Nevertheless, despite being assigned these labour-intensive functions, the point to consider is whether provincial government is spending more of its total budget on personnel expenditure than it should be. Personnel expenditure by provincial government has increased alarmingly since 2003/04, which is not sustainable, especially if current fiscal conditions worsen.

Figure 1: Personnel Share of Total Expenditure by Sphere



Source: National Treasury, The Commission's calculations

Rising employee headcount is one of the reasons for the increase in personnel expenditure by provinces. As Table 1 shows, in 2011 the total headcount was nearly half a million in the education departments and 329 253 in the health departments. Between 2004/05 and 2011/12 the total number of posts increased by an annual average of five per cent for education and six per cent for health. In 2011/12 permanent staff made up almost 90 per cent of the total staff complement, but contract and abnormal appointments have increased substantially since 2004/05³. Contract employees increased by an average annual growth of 50 per cent for education and 38 per cent for health. A similarly dramatic average annual increase was seen in abnormal appointments for education (96.5 per cent) and, to a lesser extent, health (23 per cent).

The substantial increase in contract and abnormal staff suggests that the education and health departments are adopting a strategy to expand the skill-set of its workforce in the short to medium term, by using the flexibility and less onerous labour provisions that govern these positions. There has been a significant increase in the number of additional posts filled between 2003/04 and 2011/12, with the growth for education being more pronounced. These unfunded additional posts are a drain on the fiscal resources of departments because resources have not been allocated as part of established organogram structures. Departments establish these posts for operational reasons, when additional functions or support are needed, but they are not aligned with the organogram.

³ Abnormal appointments are positions that are filled but are not part of the approved organisational organogram.

Table 1: Total Posts Filled by Main Provincial Sector (2004/05–2011/12)

	2004/05		2011/2012		Annual Growth	
	Education	Health	Education	Health	Education	Health
Headcount						
Permanent	340 544	215 533	440 467	284 867	4.19%	5%
Contract	2 843	7 864	13 021	28 794	51.14%	38%
Abnormal	3873	5 063	30 053	13 288	96.57%	23%
Other	21 280	3 223	14 266	2 304	-4.71%	-4%
Total	368 540	231 683	497 807	329 253	5.01%	6%
Percentage of Total						
Permanent	92%	93%	88%	87%		
Contract	1%	3%	3%	9%		
Abnormal	1%	2%	6%	4%		
Other	6%	1%	3%	1%		

Source: Department of Public Service and Administration (2012). Human Resources Oversight Persal. provincial data; The Commission's calculations

Staff mix has been identified as a cost driver, but Government does not have an agreed way of clearly demarcating administrative versus frontline staff. Typically frontline staff are directly involved in activities or processes related to the beneficiaries of public goods or services, whereas administrative (or back office) staff support services that help frontline staff and ensure the organisation operates seamlessly. The combination of frontline and administrative employees may vary from sector to sector. Although rarely directly involved in service delivery, managers are not considered back office staff, as they are supposed to play a strategic function. Table 2 shows the staff mix for provincial education departments. Employees falling into employment levels 1–5 are defined as lower, levels 6–12 as middle and 13–16 as senior level staff.

Table 2: Staff Mix of Provincial Education Departments (2003/04–2011/12)

EDUCATION Provinces	2003/04			2011/12		
	Low: Middle	Low: Senior	Middle: Senior	Low: Middle	Low: Senior	Middle: Senior
Eastern Cape	0.16	161.48	995.00	0.20	242.95	1 237.13
Free State	0.27	231.04	851.30	0.27	155.34	573.50
Gauteng	0.20	187.47	921.00	0.29	176.84	618.09
KZN	0.22	184.17	828.40	0.26	300.45	1 163.68
Limpopo	0.08	124.62	1 529.10	0.07	56.66	854.44
Mpumalanga	0.16	206.10	1 257.20	no info.	no info.	no info.
Northern Cape	0.34	155.27	454.70	0.28	79.79	285.03
North West	0.20	209.71	1 053.90	0.14	88.88	657.27
Western Cape	0.19	140.49	734.50	0.20	150.73	630.73
Average	0.20	177.82	958.30	0.20	156.45	752.48

Note: No information on staff mix was available for the Mpumalanga Department of Education in 2011/12.

Source: Department of Public Service and Administration (2012). Human Resources Oversight Persal. provincial data; The Commission's calculations

Between 2003/04 and 2011/12 the ratio of middle to senior management declined, from 958 to 752 middle employees per one senior manager. This implies that overall senior management is growing faster than middle employees, although the picture varies from province to province. However, definite conclusions are difficult to draw because no benchmark exists, and other factors can affect these ratios, such as the specific delivery model being employed by the respective provincial departments.

The South African government has committed to moderating the growth in the public sector wage bill, and so the effect of provincial personnel expenditure on economic growth is an important consideration. The econometric analysis found that expenditure on employee compensation at provincial level has no statistically significant effect on short-term economic growth, while non-compensation expenditure is the largest contributor to provincial economic growth. This implies that personnel expenditure could be reduced as part of fiscal consolidation without compromising economic growth. However, this has to be balanced against the fact that provinces typically spend in areas such as health and education, which contributes to long-term growth and broader social development. Therefore, productivity increases within the existing personnel budget is also critical (e.g. by achieving more appropriate skills mix), as is an efficient balance of spending on personnel, capital, and goods and services (for example, to avoid having teachers but no learner support materials, or medical personnel but no medicines).



CONCLUSION

The public sector wage bill is a complex issue. The research found that a number of cost drivers, such as employee headcount and staff mix, explain the upward spiral of total personnel costs. The focus was on provincial departments of education and health, which have proportionately larger personnel budgets compared to other departments. The analysis found that personnel expenditure does not affect short-term provincial growth. However, as spending on health and education contributes to long-term growth and broader social development, the emphasis should be on productivity increases, which would require policy adjustments beyond personnel management and performance-based measures.

With respect to the **provincial public sector wage bill**, the Commission recommends that:

- A transition over the medium to long term is required, towards a more appropriate balance between the wage and non-wage components of provincial budgets for social spending (starting with education and health). This should be in the form of national sector departments setting a norm or ratio of frontline versus administrative staff to total expenditure per sector and/or by specific occupational categories, and developing accurate and up-to-date management information systems to monitor employee compensation expenditure against those norms.
- When human resources functions have been delegated to them, accounting officers are required to adhere to agreed staff establishment norms when filling posts. This requirement must be enforced through existing regulations and performance agreements. Furthermore, each accounting officer must be held accountable for establishing effective personnel spending controls, ensuring up-to-date and credible personnel information to act as an early warning, and for taking prompt corrective action when necessary.
- The capability of human resource functions within provincial line departments – to cost and budget for staff establishments, establish the necessary control systems, respond to Auditor-General queries, and manage financial and non-financial information – is enhanced. Provincial treasuries and Offices of the Premier should enhance their capacity to monitor, support and supervise management of employee compensation.
- Methods to improve productivity of health and education sectors are considered, such as computerisation of certain processes, reorganising and streamlining workflow, and organisational design. The non-wage components of provincial budgets should include adequate provision for health technologies and technologies for e-education (ICT) and support organisational innovations in order to enhance productivity in the social sector.

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