

INTRODUCTION

The problem of inequality is garnering increased attention, and for good reason, considering inequality is an intractable problem globally and in South Africa. In the most recent report on poverty and inequality by Statistics South Africa (2017), there appears to have been very little improvement in the levels of inequality in South Africa in the last decade. Inequality in both income and wealth remain stubbornly high, and this has negative consequences on the general populous' access to resources, assets and opportunities.

In 2015, the top 10% of full-time South African employees took home, on average, 82 times more than the bottom 10%, with the average earnings for white workers more than three times higher than for African workers (Isaacs, 2016).

In their recent seminal work, Wilkinson and Pickett (2009) describe unequal societies as "dysfunctional". There is overwhelming evidence to suggest that unequal societies are more violent, slower growing and less content than their more equal counterparts. Indeed, inequality, taking various forms, is likely the most damaging socio-economic problem facing South Africa. There is rampant racial and gender inequality; inequality in wealth, access to services, education and life expectancy; and in the life chances and opportunities of people across the country. This policy brief is concerned with the issue of wage inequality – a particular form of inequality that has very deep historical roots and, arguably, the most drastic economic and social repercussions.

The recent introduction of a national minimum wage in South Africa should be celebrated. It is an important intervention that will improve the lives of millions of low-paid workers in South Africa, and it is a good example of the necessity of well-considered labour market interventions. The focus, however, on the lower-wage section of the labour market should not distract us from examining other areas of the wage distribution and there needs to be a broader discussion about policy options to address inequalities arising from pay dynamics at the upper end of the labour market.

This policy brief focuses on wage inequality, as one of the most important components of income inequality, which, as shown below, is the single largest driver of inequality in South Africa; it begins by outlining the scope of such inequality in South Africa, with a particular focus on executive pay and the relationship between executive pay and low pay – the pay ratio. The policy brief then

goes on to review international approaches to reducing wage inequality through the use of pay ratios or pay caps. These examples are used to propose particular policy options for South Africa mindful of the important social and economic differences that distinguish South Africa. In particular, it focuses on the power of Section 27 of the Employment Equity Act to achieve substantive progress in addressing wage inequality, if it is properly implemented. This constitutes the first in a series of policy briefs, each of which will tackle different approaches to reducing wage inequality.

WAGE INEQUALITY IN SOUTH AFRICA



AN OVERVIEW

Inequality in South Africa is not an exclusively contemporary phenomenon but rather stretches back for decades, and even centuries (Giliomee, 2003). Despite the democratic transition in 1994, South Africa has made little progress in addressing this, even compared to some of its peers, such as Thailand, Malaysia and several countries in South America. According to the OECD (2011), while some developing countries have achieved significant successes in reducing inequality between 1990 to 2010; China, India, Russia and South Africa have all seen widening inequality, despite the fact that these countries experienced periods of strong economic growth over this time.

A number of characteristics of the South African labour market help to explain this. Persistently high levels of unemployment – which have endured throughout the post-apartheid period – play an important role. In 1994, the narrow unemployment rate was 20%, rising to 26.7% in 2000 and falling to 22.5% in 2007 (International Labour Organisation, 2017). The rise in unemployment in the wake of the global financial crisis is shown in Table 1. While there has been some degree of economic recovery, it is clear that unemployment has worsened over this time, from 22.5% in 2008 to 27.7% in 2017. According to the expanded definition, which includes potential workers who have given up looking for work, unemployment has risen from 29.7% in 2008 to 36.4% in 2017.

Table 1: Unemployment in South Africa

Indicator (%)	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Unemployment rate (narrow)	22.50	23.70	24.90	24.80	24.90	24.70	25.10	25.30	26.70	27.70

Source: Stats SA (2016, 2017)

These figures, as dire as they are, obscure a highly skewed employment distribution, which is illuminated in table 2 below.

Table 2: Household indicators 2012 (2012 prices)

	Poor		Non-Poor		All	
	Quintile 1	Quintile 2	Quintile 3	Quintile 4	Quintile 5	Quintile 6
Labour Market Participation						
Employed	15.9%	35.9%	52.5%	65.3%	75.0%	44.4%
Unemployed (strict)	25.1%	17.4%	12.3%	9.0%	2.6%	14.9%
Unemployed (discouraged)	5.5%	4.5%	2.2%	1.7%	1.2%	3.4%
Narrow Unemployment Rate	61.2%	32.7%	10.9%	12.1%	3.3%	25.1%
Broad Unemployment Rate	65.8%	37.9%	21.7%	14.1%	4.8%	29.1%
Wages and Labour Market Linkages						
Average Wage of Employed Persons	R1 017	R1 707	R2 651	R4 751	R13 458	R5 787
% Working Households	36.2%	65.8%	71.1%	85.8%	87.8%	69.3%
Average Monthly Household Income	R1 671	R3 125	R4 169	R7 317	R24 090	R8 018
Average Monthly per capita Income	R323	R773	R1 491	R3 117	R12 509	R3 611

Sources: DPRU (2016).

Note: All figures weighted using calibrated weights.

The implications of this are quite clear: South Africa must address its extremely high levels of unemployment. But this alone is not enough – these data show that the country has a pervasive problem of very low pay, and very high wage and income inequality, and this issue requires urgent policy attention in order to redress these massive disparities between quintiles.

This is illustrated by the fact that while average wages in the economy have increased since the end of apartheid, and in particular since 2000, driven by wage increases amongst higher-income earners, the real median wage (the wage in the mid-point of the wage-earning scale) has seen little growth and remains well below the average wage. Work by Finn (2015) shows that, adjusting for full-time equivalents, the average wage in 2015 was R9,690 compared to a median wage of R3,784.

The data suggest that wage inequality in South Africa has actually deepened over the last 20 years. In his review of earnings trends in South Africa from 1993-2014, Wittenberg (2016) notes: **"when we look at the earning distribution as a whole it turns out that the trends are remarkably clear... the top part of the earnings distribution has moved away from the middle, while the distribution at the bottom has become more compressed."** (Wittenberg, 2016, p.1). When discussing inequality, it is therefore important to assess the gap between low or median earners and high earners, rather than using the average wage as a benchmark.

Wage inequality matters, because, as found by Finn (2015), it is the largest determinant of overall income inequality by a significant margin. As shown in Table 3, wages account for 90.65 percent of total income inequality in South Africa – far in excess of the contribution to inequality from remittances and investment income combined.

Table 3: Components of income inequality in South Africa

	Absolute contribution	Relative contribution
Wages	0.6	90.65%
Government Grants	-0.01	-1.04%
Remittances	0.06	8.5%
Investment	0.01	1.87%
Total	0.66	100%

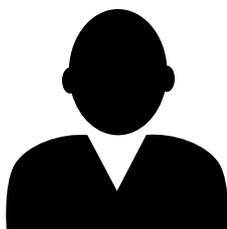
Source: Finn (2015)

The distribution of pay is also highly unequal along gendered lines; the current statistics show very wide discrepancies. Furthermore, the bottom of the income distribution is dominated by low paid precarious work, a disproportionate share of which is done by women. Bosch (2015) finds that the gender pay gap in South Africa is estimated to be between 15 and 17 percent. The gap in this case is defined as the difference in pay for individuals with equivalent skills and experience doing the same job. This difference means that, on average, a woman must work two additional months to earn the same salary that a man with the same skills and experience would earn in one year. Another report (BusinessTech, 2016) found that white male professionals earned up to 42% more than white females according to median earnings. There is only one female CEO in the top 40 companies listed on the JSE (PwC, 2017).

There are also significant racial pay disparities. A 2016 report, surveying 692,704 individuals, found striking differences in the pay. The report (BusinessTech, 2016),

"...found that white male workers in the formal sector earned a median salary of R21,700 per month, compared to R13,331 for white females, R3,612 for black males, and R2,887 for black females."

EXECUTIVE PAY IN SOUTH AFRICA



Given these dynamics, an assessment of pay at the upper end of the pay scale, and the gap between those at the top and bottom, is crucial. This should be viewed in the context of relative pay for executives in South Africa being amongst the highest in the world,

with levels of executive remuneration far exceeding those in comparative developing countries, when adjusted for purchasing power.

Massie, Collier and Crotty (2014) note that the problem of perceived 'excessive' executive pay is endemic in South Africa. They cite work by the Labour Research Services (LRS), surveying 296 executive directors in 83 companies across 14 sectors, which found that in 2012 the average annual remuneration for an executive director was R7.7 million. This means that, in the wages of that year, a low-wage worker would have to work for 267 years to earn what the average CEO was paid in 2012. Furthermore, they note that there is little chance that this problem will correct itself. As Massie et al. (2014) note:

"At the current rate of CEO pay increases and LTIP (long-term incentive payments) grants, there is no chance that, without meaningful intervention, the wage differentials in South Africa will actually decrease. It will take a conscious effort on the part of companies to actually reduce CEO pay packages or at least stop increasing these packages in order for the wage gap to narrow. Symbolic attempts to grant a 2% higher increase to the lowest paid while still raising the pay for the highest paid will not move this country any closer to a system that is fair to all." (Massie et. al, 2014, p.28)

This has been borne out by subsequent reports from PwC which show that executive pay ratios have remained at up to 62:1 by 2017, showing no improvement from 2015 (PwC, 2017).

ASSESSING EXECUTIVE PAY AND PAY GAPS IN SOUTH AFRICA

Executive pay can be compared across companies, sectors or countries in absolute monetary terms. When comparing across countries this can be done at market exchange rates or using a purchasing power parity conversation – as in the example below – which takes into account the difference costs of goods and services in different countries.

One way to assess the relative level of pay, and pay disparities, is via a pay ratio.

A pay ratio is a calculation of the difference between what one employee (or group of employees) and another employee (or group of employees) earns. Pay ratios provide information on how pay is distributed across a workforce.

For example, a CEO to median-employee pay ratio of 20:1 means that the CEO earns twenty times the median-employee's pay. Pay ratio calculations can include or exclude pensions, share incentives, health benefits and other perks. They can also include or exclude interns, part-time workers, temporary workers, contractors and foreign and overseas workers.¹

When one examines pay data and related measures of pay inequality – such as the pay gap – in South Africa, one is confronted with a variety of statistics covering a broad range of measures of inequality, as illustrated in the tables below. A key reason for this is that it is extremely difficult to get company-level information on exact pay figures, both for executives and for other workers, and especially not on a sector-wide or economy-wide basis. While for listed companies, executive pay is disclosed, it is not always done so in a manner that is accessible, as it often comprises a basic salary, long and short-term incentives, and share options, among others. For other workers, individual salaries are of course not disclosed. Therefore, the figures used in this brief are based on a variety of methods.

¹ Some examples include: the ratio between the pay of the highest-paid employee and the lowest-paid employee; the ratio of the top 5% of earners to the bottom 5% of earners; the inter-decile income share ratio, which measures the share of income received by the top 10% divided by the share of income received by the bottom 10%; the 90/10 ratio, which measures the ratio of income of the 90th percentile to that of the 10th percentile. The ratio between different categories of workers could be compared, for example, the ratio of pay between skilled and non-skilled workers or managerial and non-managerial workers; or the ratio between the CEO's total guaranteed package and the average income of the lowest-paid band of workers (PwC, 2013).

EXECUTIVE PAY AND PAY RATIOS IN SOUTH AFRICA

Adjusted for spending power, high-earning workers in South Africa are some of the best-paid employees in the world – a fact somewhat inconsistent with our status as an emerging market economy. According to 2016 research by Bloomberg, South African CEOs were the seventh-best paid executives globally in that year, when adjusted for spending power.

Table 4 provides some comparative figures for pay ratios between 25 countries around the world. Here the pay ratio is calculated by comparing the average CEO income to the average per capita income in the country (adjusted for spending power across countries).² From this table, it is clear that:

South African executives earn fair above the per capita share of national income – an average 541 times more. In India, this figure is 483 times, and in Malaysia – a country comparable with South Africa in many ways – it is 66 times.

Price Waterhouse Coopers calculates the Gini coefficient of income for employed South Africans at 0.43 in 2015, 2016 and 2017 (PwC, 2017). This indicates a very high level of income inequality. However, it is lower than the Gini estimated from survey data which was 0.68 for income inequality in 2015 (including the unemployed) and 0.60 for wage inequality (including only wage-earners) in the same year (Finn, 2015).

What is lacking from the above are trends for intra-firm income inequality. How does executive pay in a given firm compare to the average wage at that firm, or indeed, the lowest paid in the firm? Drawing from publically available financial reports in 2017, the pay ratio between CEOs and the average employee⁵ at the 25 largest companies listed on the JSE is presented in Table 5 below. Using the average wage – calculated by dividing the total disclosed salary bill by the number of employees – is likely to understate the size of the wage gap. This is due to the divergence between average and median salaries, and because these salary bills often exclude wages for outsourced workers, who are among the lowest paid in any company, such as cleaners and security staff.

Nonetheless, the figures are striking. The data presented in Table 5 cover 1.3 million employees in these 25 companies, who together command a total salary bill of R570 billion.

Table 4: The Pay Gap - a global comparison (2015/16)

Rank	Economy	Pay Ratio ³	CEO Pay \$ Million, Latest Filing	GDP p.c. PPP 2015/16
1	South Africa	541.4	\$7.14	\$13 194
2	India	483.06	\$3.10	\$6 423
3	U.S.	298.98	\$16.95	\$56 689
4	U.K.	228.7	\$9.61	\$43 006
5	Canada	202.98	\$9.32	\$45 921
6	Switzerland	179.34	\$10.58	\$59 011
7	Germany	175.65	\$8.36	\$47 582
8	Spain	172.42	\$6.15	\$35 656
9	Netherlands	172.32	\$8.66	\$50 235
10	Israel	11.42	\$4.11	\$34 444
11	South Korea	113.98	\$4.25	\$37 280
12	Australia	113.07	\$5.45	\$48 225
13	Norway	100.99	\$6.96	\$68 944
14	Denmark	82.07	\$3.79	\$46 163
15	Sweden	74.95	\$3.67	\$48 938
16	France	67.65	\$2.84	\$41 930
17	Hong Kong	66.2	\$3.81	\$57 487
18	Malaysia	66.03	\$1.76	\$26 723
19	Singapore	64.89	\$5.60	\$86 232
20	Japan	62.33	\$2.40	\$38 518
21	Finland	61.2	\$2.54	\$41 461
22	Austria	46.57	\$2.21	\$47 421
23	China	43	\$0.64	\$14 882
24	Poland	23.94	\$0.65	\$27 107
25	Thailand	3.94	\$0.06	\$16 483

Source: Bloomberg⁴ and International Monetary Fund

The average salary is R589,850 for the general employee, while the average CEO pay is R55.3 million, roughly 95 times larger than the general employee (BusinessTech, 2017a).

This, however, hides significant variation across some of South Africa's largest companies. For Shoprite, the pay ratio between its average salary and its CEO is 1,332, that is, the CEO of Shoprite earns 1,332 times the average salary of a Shoprite employee. Ten of these 25 companies have a pay ratio larger than 100.

Table 5: The Pay Gap in South Africa (2016/17)

Company	CEO salary	Pay ratio ⁶
Shoprite	R100.1 million	1332
Naspers	R162.4 million*	264
Steinhoff	R88.9 million*	234
British American Tobacco	R126.7 million*	191
Capitec	R35.6 million	183
Mondi	R85.7 million*	172
MTN	R72.2 million	157
Old Mutual	R43.4 million*	150
Anglo American	R70.2 million*	135
Richemont	R122.9 million*	120
AB InBev	R23.4 million*	82
Standard Bank	R44.5 million	79
FirstRand	R42.5 million	78
Nedbank	R36.8 million	77
Sasol	R56.4 million	64
Absa	R29.5 million	58
Glencore	R20.2 million*	55
South32	R43.9 million	54
BidCorp	R26.4 million	54
Vodacom	R35.7 million	50
BHP Billiton	R30.0 million*	43
Mediclinic International	R18.0 million*	28
Aspen Pharmacare	R17.5 million	25
Sanlam	R22.5 million	23
Remgro	R28.0 million	20

Source: Business Tech, 2017a

² This is, however, an imperfect measure as the per capita GDP figure takes the overall national income and divides it equally amongst the population.

³ The pay ratio compares CEO compensation with per-capita gross domestic product adjusted for purchasing power parity, which shows how much income the average person generates.

⁴ The Bloomberg Global CEO Pay Index tracks average CEO compensation at companies that are members of each country's primary equity index, weighted by market capitalisation.

⁵ Calculated as the total salary bill divided by the number of employees.

⁶ CEO to average salary.

On aggregate, Preston (2014) found that across the JSE, the ratio of a company's average CEO compensation to the average wage is 73:1 and in 2016, PwC calculated a pay ratio for a sample⁷ of South African firms between 13 and 66, and for 2017 this was 13 to 62 (PwC, 2017).



These large disparities show no sign of abating, while executive pay has risen in excess of 10% per year since 2009, average wages have risen by less than 8%, thus escalating income inequality (Melin and Lu, 2017).

These large pay ratios are also out of sync with what the general population consider a fair pay disparity. Kiatpongsan and Norton (2014), from Harvard University, recently examined data from forty countries including South Africa, to compare individuals' estimates of current wage disparities to what they believe to be an 'ideal' pay gap. Of the 3305 survey participants in South Africa (a sample representative of the population),

...participants estimated that the pay ratio between a CEO and an unskilled worker in 2009 was 17:1 and believed the ideal ratio to be 8:1.

Across the forty countries studied in the survey, the estimated ratio of CEO pay to an unskilled worker's pay was 10:1, while the ideal was approximately 5:1. Somewhat above this level, the oft-quoted management-guru Peter Drucker asserted that a ratio of 15:1, 20:1 or 25:1 was the maximum optimal ratio (dependent on firm size) to prevent resentment and falling employee morale (Drucker Institute, 2011). Clearly, the ratios highlighted above are far from South Africans' perceptions of the pay gap, or what they consider an ideal ratio, indicating that steps to reduce these ratios would be welcomed by society in an attempt to redress income inequality.

It is important to note that pay inequality is not limited to the individuals who receive executive pay packages. In general, the South African labour market is bifurcated, with very high salaries for mid-level and senior management while the vast majority of workers earn extremely low wages.

Furthermore, given the fact that executives account for a relatively small portion of the workforce, the issue of pay inequality does not always garner the attention it deserves nor should it be limited to a consideration of only those at the very top. While excessive executive pay certainly is a problem, it is itself a symptom of a broken and distorted labour market, one where bargaining power is unequally distributed, to the detriment of low-earners, and to the benefit of a few, extremely highly paid individuals.

PAY RATIOS AT SOUTH AFRICAN STATE-OWNED ENTITIES

As one of the main employers in South Africa, the state has an important role to play in setting wage standards. The government should disclose pay levels and pay ratios within its ranks, actively work to reduce those ratios and ensure that its suppliers and contractors are doing the same. In this regard, it is necessary to look at the pay ratios within the government and within state-owned enterprises (SOEs); some of the latter are shown in Table 6 which highlights pay ratios in 9 SOEs.



It is clear from these figures that the pay gap at South African SOEs is significantly more moderate than in the private sector, with the highest pay gap of 21:1 at Transnet, compared to 1,332:1 at Shoprite. However, these figures almost certainly exclude outsourced workers, such as cleaning and security, and other low-paid contract work. If these are included, the pay ratios would be significantly higher. Calculating pay ratios within government departments themselves is complicated. While national and provincial governments pay according to a salary scale, local governments have more flexibility to set salaries, and thus it is not possible to generate a single set of figures for the government pay ratio.

⁷ Information was sourced from the annual reports of 360 actively trading companies listed on the Johannesburg Securities Exchange which had a total market capitalisation of R14.0 trillion.

Table 6: Pay Ratios at South African SOEs (2015/16)

Company	CEO salary	Average per employee	Pay ratio
Transnet	R7.4 million	R353 570	21
Rand Water	R5.1 million	R344 710	15
Eskom	R8.9 million	R696 170	13
South African Airways	R5.9 million	R543 810	11
SABC	R3.6 million	R726 240	5
Telkom	R2.6 million	R535 860	5
Broadband Infracore	R2.7 million	R677 480	4
SA Post Office	R538 000	R161 280	3
Sentech	R1.2 million	R683 260	2

Source: Business Tech (2017b)

POLICY OPTION 1: DISCLOSING PAY RATIOS

There are many different options for tackling the pay inequality that has been starkly outlined above. This brief focuses on two of these – the disclosure of pay disparities and the setting of (mandatory or voluntary) pay ratios or caps – examining the mechanics, benefits and disadvantages, and practicalities of implementation in South Africa.

In order for appropriate action to be taken regarding wage inequality, it is most important to be armed with appropriate and accurate information regarding pay differentials. While the South African pay ratios highlighted above are striking, they are not a complete picture, as they focus on listed companies. A policy for equitable pay needs to apply to all firms, and thus information on pay differentials is required.

INTERNATIONAL EXPERIENCE

There are only a handful of countries requiring companies, by legislation, to disclose information related to pay ratios. Since 2015, public companies in India have been required to disclose the ratio of the remuneration of each director to that of the median employee's remuneration as well as the average increase in employee remuneration compared to that of key management personnel and explain the difference in this pay gap (InGovern Research Services, 2015). The United Kingdom, similarly, requires companies to compare and disclose the percent change in CEO pay to that of employees of the company (UK Government, 2013b). This calculation does not include equity-based pay and companies are permitted to choose their employee comparator group.

In South Korea, annual reports are required to provide information on average employee pay and the pay of top executives, giving enough information to allow investors to calculate a pay ratio on their own (Shin et al., 2015).

Starting in 2018, public companies in the United States will also be required to publish the ratio of the total annual compensation of the CEO to the median compensation of all the firm's employees (SEC, 2015). Companies may select their own reasonable method for choosing the median employee and calculating that employee's compensation.

CHALLENGES REGARDING DISCLOSING PAY RATIOS

There are three main challenges raised by companies over requiring pay ratio disclosure. However, each of these can be overcome. One argument is that the calculation is an expensive and time-consuming process (Caulkin, 2015). For instance, CEO pay is complex and difficult to compute and a company's employees may be spread out across the globe and be employed by a variety of subsidiaries that encompass a number of different payroll processes. However, publicly-listed companies are already required to compute and disclose the level of CEO pay. Even if such a practice does require some effort, the equity-enhancing benefits for society of such a policy have the potential to outweigh any additional cost to the company in collecting the data.

Another concern is that companies are able to manipulate the pay ratio reported by outsourcing the lowest-paid jobs or turning low-paid workers into contractors or part-time workers. This could be overcome by mandating the inclusion of such workers in pay ratio calculations even if they are outsourced in these ways. This would admittedly add to the expense and complexity of calculating pay ratios, but would provide valuable protection to the most vulnerable workers and ensure companies are not able to manipulate the figures.

A final challenge is that ratios may not be comparable across companies, industries or countries. Similar companies might engage in different calculation processes, resulting in completely different figures. To be meaningful, clear methodological approaches must be defined, for example regarding which employees are to be compared and what parts of their pay must be included. For telling comparisons, all elements of remuneration should be taken into account – not just cash payments. Even if this is done, comparisons between companies should be treated with care, for instance, small companies will likely have lower multiples than large companies. Similarly, pay ratios in a company which has a majority of low-skilled workers, such as domestic cleaning company, will be very different to a company with a highly-skilled workforce, such as a technology development company. Any concerns a company has in this regard can be outlined in explanatory text alongside the pay ratio, while those concerned with pay ratios are surely able to understand any contextual differences when making comparisons.

SOUTH AFRICAN APPLICATION

South Africa already has a legislated mechanism for reporting on pay differentials, in the form of section 27 (s27) of the Employment Equity Act (EEA).

As Massie et. al, (2014) argue, "the strongest possibility for providing say on pay through labour market regulation is contained

...in the EEA provision that requires designated employers to report on 'income differentials' within the organisation.

Designated employers include those who employ 50 or more employees, or who earn above a threshold turnover, and public sector employers such as municipalities and organs of state." (Massie et. al, 2014, p.160). As part of these reporting requirements, these employers must report on remuneration⁸ and benefits received by employees.

The power of the EEA4 form for providing a well-informed basis upon which to tackle the problem of wage inequality can be seen in table 7. This is an example EAA4 form for a company in the manufacturing sector. It lists the number of employees by skill level, race, and gender, and provides an excellent insight into the distribution of pay in the company.

The first thing to note is that the average annual executive pay is R816,649, while the average annual pay for the lowest-paid workers is R42,956, giving a pay ratio of 19:1. But the form allows for an examination of other important pay indicators. At the level of top management, for example, males are paid approximately 45% more than females, while in senior management, white males are paid 2.25 times more than African males. In fact, for all skill levels, whites are paid more than other race groups.

It is clear that the EEA4 forms, through s27 of the EEA, provide an opportunity to build a wage policy based on accurate and complete data. In particular, they allow for an examination of both vertical and horizontal pay wage inequality. Thus the insights these forms offer into the wage distribution in South Africa are unparalleled, and the forms should be used as originally intended. The data from these forms should be made publically available as a step towards ensuring companies comply with the terms of the act where unacceptable pay differentials are identified.

We further recommend that listed companies must, in their annual reports, provide a series of pay ratios based on a common specification, as done in some other countries. These could include, among others, ratio between the CEO and the lowest paid; the CEO and median; CEO and mean; and the ratio between the highest 10% and lowest 10% of workers. While the EEA4 forms exclude outsourced workers, these pay ratios should include them. The publication of these ratios is important in and of itself, but is necessary to ensure that companies are complying with any specified pay ratio.

⁸ 'Remuneration' is defined in the EEA as "any payment in money or in kind, or both in money and in kind, made or owing to any person in return for that person working for any other person, including the State". (Collier and Massie, 2014, p.160)

Table 7: An EEA4 form from the manufacturing sector

	Male				Female				Total
	African	Coloured	Indian	White	African	Coloured	Indian	White	
Top management									
# of employees	-	-	-	3	-	-	-	1	4
Total pay	R0	R0	R0	R2 657 633	R0	R0	R0	R608 962	R3 266 595
Average pay				R885 878				R608 962	R816 649
Senior management									
# of employees	2	-	-	8	-	-	-	-	10
Total pay	R718 547			R6 475 028	R0	R0	R0	R0	R7 193 575
Average pay	R359 274			R809 379					R719 358
Professionally qualified and experienced specialists and mid-management									
# of employees	1	-	-	12	-	-	-	1	14
Total pay	R116 232	R0	R0	R4 495 127	R0	R0	R0	R174 941	R4 786 300
Average pay	R116 232			R374 594				R174 941	R341 879
Skilled technical and academically qualified workers, junior management, supervisors, foremen and superintendents									
# of employees	20	3	-	7	6	1	-	10	47
Total pay	R3 046 533	R528 302	R0	R1 866 793	R395 827	R80 372	R0	R1 346 874	R7 264 701
Average pay	R152 327	R176 101		R266 685	R65 971	R80 372		R134 687	R154 568
Semi-skilled and discretionary decision making									
# of employees	39	4	-	11	7	2	-	-	63
Total pay	R2 082 013	R2 399 905		R623 111	R172 550	R103 847	R0	R0	R5 381 426
Average pay	R53 385	R599 976		R56 646	R24 650	R51 924			R85 419
Unskilled and defined decision making									
# of employees	4	-	-	-	2	1	-	-	7
Total pay	R166 873	R0	R0	R0	R96 967	R36 852		R0	R300 692
Average pay	R41 718				R48 484	R36 852			R42 956
Total permanent									
# of employees	66	7	-	41	15	4	-	12	145
Total pay	R6 130 198	R762 207	R0	R16 117 692	R665 344	R221 071	R0	R2 130 777	R26 027 289
Average pay	R92 882	R108 887		R393 114	R44 356	R55 268		R177 565	R179 499
Temporary employees									
# of employees	-	-	-	-	-	-	-	-	-
Total pay	-	-	-	-	-	-	-	-	-
Average pay	-	-	-	-	-	-	-	-	-
Total									
# of employees	66	7	-	41	15	4	-	12	145
Total pay	R6 130 198	R762 207	R0	R16 117 692	R665 344	R221 071	R0	R2 130 777	R26 027 289
Average pay	R92 882	R108 887		R393 114	R44 356	R55 268		R177 565	R179 499



In addition to requiring the publication of pay ratios, it is possible to require boards to disclose the annual pay increase for each category of employee. Harrop (2014) explains that this would see boards being required to justify why pay growth at the top may be greater than that at the bottom (reasons may simply be that CEOs do more important jobs- giving boards a mandate to disclose why pay changes may incur bias). Given the large number of workers that earn wages below the poverty line in South Africa, companies could also be required to disclose the number of working poor that they employ. Requiring such disclosure alongside executive pay levels and pay ratios could prompt a consideration of how much executive salaries would need to be reduced in order to bring all of a company's workers above the poverty line. Furthermore, companies could be compelled to publish these remuneration data in their annual reports, providing a summary of ratios for executive pay, as well as those for race and gender comparisons. This also points to the related issue of calculating and disclosing executive pay: guidelines must be developed indicating how executive pay must be calculated and disclosed.

POLICY OPTION 2: REGULATING PAY RATIOS OR CAPPING EXECUTIVE PAY

Mandatory disclosure of wage ratios could be accompanied by the stipulation of a target pay ratio, either voluntary or mandatory. If companies fail to achieve these targets over time, the government can enact incentives for achieving these ratios, such as favourable procurement policies or tax incentives. Should companies' voluntary compliance be deemed insufficient, mandatory regulations setting a pay ratio could be instituted. In addition to regulating such pay ratios a firm cap could be set on executive pay. Legislation could require companies to obtain certification proving that they comply with a mandatory remuneration cap.

INTERNATIONAL EXPERIENCE

There are a number of examples of countries capping executive pay or establishing a pay ratio limit. South Korea, Egypt, Israel, France, Venezuela, China and Poland have all established a form of executive pay cap, some based on a pay ratio.

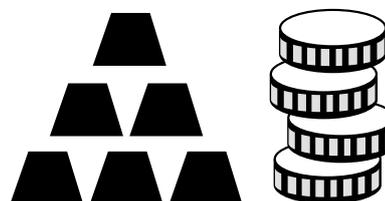
Firms receiving funds under the financial bailout regulations in the United States and Germany had limits placed on their compensation. In South Korea, laws require shareholders to set a pay cap for all executives and directors at publicly-listed companies unless a cap exists under the company's corporate charter. In July 2012, the French government limited salaries at SOEs to €450,000, equivalent to twenty times the average salary of the lowest paid 10% of workers (Ministère De L'Économie et Des Finances, 2012; French Government, 2017). By 2014, the Agence Des Participations De L'État (2014-15) reported that all publicly-owned companies in France complied with the pay-cap decree, demonstrating how a salary cap using a pay ratio can be imposed successfully across many companies as a result of the government leveraging its position as shareholder.

Executive pay in Chinese SOEs is capped at either twelve or thirty times average employee pay for the firm, and plans to cut executive pay in SOEs by 50% were introduced in 2015 (Li et al., 2013; Yuzhe, 2014; Leutert, 2016). Chinese officials stated that these policies were unlikely to result in attrition because executives in China obtain job stability and professional development opportunities they would not get elsewhere. However, Hewitt (2015) reported that several top executives in China's banks had already quit as a result of salaries declining by up to 50%.

In 2016, the Israeli government passed a law that provides that executive compensation greater than 2.5 million NIS (\$650,000 USD) cannot be awarded by a financial company if this compensation is more than 35 times the lowest salary at the corporation, thus relating a pay cap to a wage ratio (Abudy and Shust, 2016). This cap applies to all compensation and requires the pay of contractors and their employees to be included in determining the lowest salary, removing the incentive to terminate or outsource low-paid positions.

Polish legislation caps pay in local government, and in companies where the state holds a majority stake, at six times the average monthly remuneration in the private sector plus a bonus of three times the average monthly remuneration (The European Institute of Public Administration, 2015). The policy also applied to foundations that obtain more than 25% of their annual income from the government. There have, however, been some challenges in implementation, including resignations and the creation of subsidiaries with the sole purpose of gaining more board seats in order to increase their pay beyond the cap, resulting in a huge cost burden to the state which was reportedly more expensive than if the cap had not been imposed at all (Cienski, 2008).

The United States' salary cap on senior executive officers in institutions that received government bailout funds was \$500,000 USD with bonuses of top earners capped at one-third of total compensation. Despite these regulations, Anderson et al. (2009) found that twenty of the United States' financial institutions that received the most bailout dollars paid their top five executives an average of \$32 million each because there was no limit on stock awards.



SOUTH AFRICAN APPLICATION



The intention behind s27 of the Employment Equity Act – given that income differentials are identified as being “disproportionate” – is to compel employers to take remedial action to progressively reduce this differential.

One of the most expeditious approaches to regulating income inequality is to substantively enact s27 of the EEA. But as Massie et. al, (2014) note, the ECC has not been able to obtain the required data analysis on income differential that would allow it to construct useful benchmarks by sector, that would allow for norms and standards of pay to be developed.

“Under the current labour law framework, employees who are unhappy about excessive income differentials have rather limited recourse. When an employer is in contravention of its reporting obligations in terms of section 27 of the EEA an employee or a trade union representative may, in terms of section 34 of the EEA, bring the alleged contravention to the attention of a labour inspector, the Director-General of the Department of Labour, or the CEE. Although the labour inspector is empowered by the EEA to enter the workplace and require the disclosure of information on any matter related to employment law, the power of a labour inspector to obtain an undertaking to comply from a designated employer – or to issue a compliance order – does not apply in the case of an employer’s failure to comply with section 27” (Massie et. al, 2014, pp.167-8).

Furthermore, the Employment Conditions Commission is tasked, by s27(4) of the EEA to research and investigate norms and benchmarks for proportional income differentials, and advise the Minister of Labour on appropriate measures to reduce disproportionate differentials, but to date the ECC has failed to do this (Helm, 2015). It is not possible to pinpoint where the fault for this lies, and it is premature to condemn the ECC for this failing. The Department of Labour must ensure that the ECC is properly capacitated to perform its functions as required by the legislation, and that it receives the necessary political support to do so.

Given the data available in the EEA4 forms, it would be possible to set specific pay ratios for different sectors and adjust these according to the specific needs and characteristics of each sector

In light of this, we propose the institution of a cap on executive remuneration, at a level to be set by the Minister of Labour on recommendation of the ECC, and a mandated pay ratio between the CEO and the lowest-paid, starting at an initial level, for example 50:1, and gradually decreasing on recommendation of the ECC.

There is South African precedent for this. Most notably, PPC Ltd CEO Ketso Gordhan took a R1 million salary cut and convinced a number of managers to agree to a pay freeze in order to reduce pay ratios in the company, achieving a top-to-bottom pay ratio of 40:1 in 2014 (Klein and Masote, 2014; PPC Ltd., 2014). But our recommendation is that a single ratio is specified, one that is set at a level that accommodates a range of sectors.

Given the extent and persistence of excessive executive pay in South Africa, it is important that the pay cap is mandatory, although it could be accompanied by a phase-in period, as with the minimum wage. This policy brief has highlighted not only the extent of excessive executive pay, but its relation to broader problems in the labour market, and this requires decisive action.

In the way of other labour market interventions, such as the National Minimum Wage, a time-specific exemption should be offered to firms that are unable to comply with the wage ratio, provided they provide an implementation plan to achieve the pay ratio over a specified time period. Given the recommendation for a single ratio, it should also be possible for industries as units to apply for this exemption.

⁹On the question of when an income differential is ‘disproportionate’, although the EEA does not define the term, it provides a mechanism for the Minister of Labour to give guidance in this regard.” (Massie et al., 2014, p.166)

CONCLUSION: ADDRESSING WAGE INEQUALITY IN SOUTH AFRICA

It is important to understand that measures to address wage inequality have precedent in South African policy and political processes, and indeed, are reflected in the commitments in the Ekurhuleni Declaration of 2014. The Declaration notes that:

- Wages are the most important component of income for South Africa's working people;
- Income from wages is the main source of ensuring a sustainable livelihood for workers;
- Unemployment and underemployment, including the legacy of low wages, are the biggest causes of poverty and inequality in South Africa; and
- Large pay differentials between executives and low income workers undermine the prospects for cooperative labour relationship and workplace cohesion. (Nedlac, 2014).

This policy brief has demonstrated that pay inequality in South Africa is both pervasive and persistent. While this can partly be explained by widespread low pay in the labour market, the evidence suggests that excessive executive pay is a large and growing problem. Using the pay ratio as a measure to understand income inequality shows that, by some measures, South Africa has among the highest levels of pay inequality in the world, far higher, indeed, than some comparative developing countries.

Given the historical and contemporary socio-political context, the determination of wages cannot be left to the market alone, and indeed there is widespread support for intervention in the labour market, as demonstrated in the wide support base for the implementation of a national minimum wage. There are several policy options available to address the problem of income inequality. Two of the most practicable, explored here, are the disclosure of pay ratios, and the implementation of a pay cap through the prescription of pay ratios or the setting of a wage cap.

It is important to note that in South Africa, the legislative mechanisms to achieve this are already in place. The EEA calls for the disclosure to the Department of Labour of pay differentials by designated employers. This information should be published. In terms of remedial action, again the EEA empowers the Minister of Labour to take appropriate steps to address excessive pay differentials. In the South African context, the prescription of specified pay ratio could be the most efficient to implement, given that there is already supportive legislation in the form of s27 of the EEA, which could prove to be a powerful policy tool. However, to date, there has been no substantive enactment of this provision.

An immediate step that should be taken is the publication of the EEA4 data, which would reveal the extent of income inequality both across and within companies in South Africa. These data could not only be used to implement and enforce a mandatory maximum pay ratio, but would assist unions in collective bargaining, and allow the government to pursue preferential procurement programmes. Furthermore, the ECC must explore the implementation of a mandatory pay cap, in the form either of an absolute cap, or a maximum pay ratio.

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