

Is there a case for a

MAXIMUM SALARY?

How much is enough? Is it time to cap high salaries to reduce South Africa's infamous wage gap? SIKONATHI MANTSHANTSHA puts out feelers.



SOUTH AFRICAN TRADE UNION Solidarity released a report in July 2006 showing that CEOs of SA companies listed on the JSE earned on average up to 53 times more than their lowest paid employees in the financial year 2005/6 (Figure 1 and 2). A similar report by consulting firm Towers Perrin of the United States of America in 2000 showed that South Africa ranked fourth (out of 26 most unequal economies) with CEO compensation at 51 times the salary of the average employee – after the US itself at a dizzy 531 times, followed by Brazil and Venezuela at 57 and 54 times, respectively (Table 1).

Curiously, in South Africa's case the income inequality gap (as measured by the Gini coefficient, Table 2) has been growing since 1996, when the effects of transformation would have started to feed through. But, importantly, the Gini coefficient is highest for the Black/African population at 0,72 in 2001, according to a study published by the Human Sciences Research Council in 2004 (*Fact Sheet: Poverty in South Africa*).

In its study, Solidarity used the same principles used in the Towers Perrin research, although the trade union became aware of the existence of this research only three months after publishing its own results. That then shows the income gap is growing, as does the Gini coefficient compiled by *Global Insight Southern Africa* in 2005.

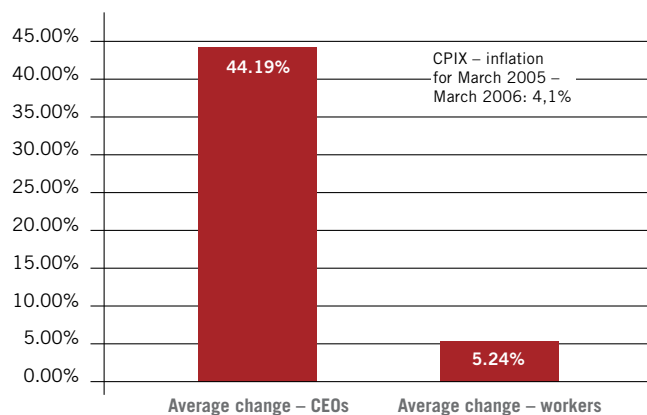
Explaining the Solidarity study, chief economist at the trade union Lullu Krugel said the union studied companies listed on the JSE for six months in 2005 and compared the remuneration of their chief

executives to those of the lowest paid employees. The result was that in some sectors – like retail – chief executives earned up to 223 times the salary of the average worker.

But Krugel says Solidarity is not opposed in principle to high executive remuneration, but wants chief executives to be rewarded for performance and workers to be rewarded likewise. "If a company has performed well, we accept that the leaders should be compensated, but so should the workers," says Krugel.

That is the exact opposite of reality in corporate South Africa. In the 2005/6 financial year most chief executives of listed companies received total remuneration increments in excess of 40%, while some employees had to go on strike to get an 8% increase. By way of an example, workers at Shoprite Holdings, one of the country's leading retailers, settled for an 8,54% increase – after a protracted three-month

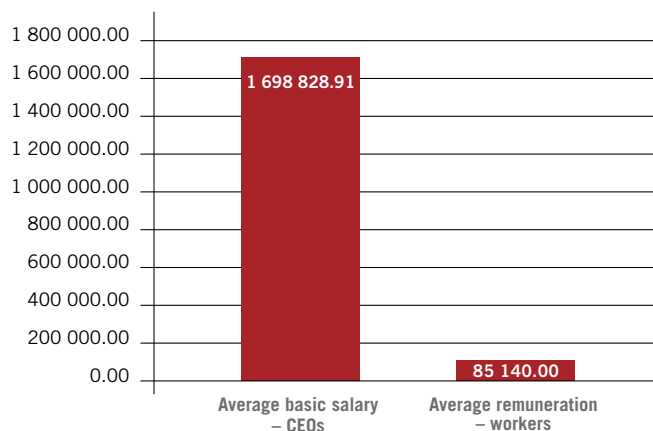
Figure 1: Average change in total emoluments of CEOs of companies listed on the JSE compared to the average change in remuneration of workers, March 2005 – March 2006



This means: The average increase in the total remuneration of CEOs equalled 44,19%, while the average increase in the total remuneration of workers was equal to 5,24% for the period under consideration.

Source: Solidarity Research Institute, July 2006

Figure 2: The average basic salary (in rand) of a CEO of a company listed on the JSE compared to the average basic salary of workers, March 2005 – March 2006



This means: The ratio shows that the average CEO's basic salary is 20 times more than the remuneration of an average worker. The average basic salary of a CEO was calculated for the whole database. All available values were included.

Source: Solidarity Research Institute, July 2006

strike, bringing the salary of the average full-time worker to less than R3 600 a month. In contrast, chief executive Whitey Basson accepted a 30% increase to take his basic annual salary to R9,9m.

“We understand there should be salary differentials; it would be stupid to think that chief executives shouldn’t be paid more [than employees]. But the question is: how much is enough?” says Krugel. “The problem is that the income gap is growing and the poor are getting poorer.”

Global Insight Southern Africa published a study in September 2005 in which it said that the number of people living on less than a dollar a day (at constant prices) had more than doubled between 1996 and 2004 – from 1,9 million to 4,3 million.

Krugel says that the growing income gaps between the highest and lowest paid employees are one of the major causes of strike action among workers, who feel they are not getting fair recognition for their hard work. “The gap shouldn’t be growing. That is our position.”

Krugel acknowledges it is not only corporate greed that can be blamed for the high income gap in the country. She points to skills as one of the major problems which cause inequality. Krugel says the skills base needs to be expanded to allow more people to land jobs that would allow them to increase their income. She also points at economies that have a high skills base like Japan and Australia and says their income gaps are narrower than South Africa’s.

Japan, which has one of the very highly skilled populations in the world, has the lowest gap in income disparity when it comes to chief executive-employee remuneration (Table 1). While Krugel would like to see the gap narrowing significantly, she does not think there is a case for imposing a maximum salary, but reckons more education and training is a way out of the status quo.

“I would be opposed to capping executive salaries as that leaves you open to too many variables,” says Daniel Malan of KPMG, who is a part-time lecturer in Business Ethics and Corporate Governance at the University of Stellenbosch Business School. “In principle I’m opposed

to high remuneration that is not linked to performance.”

From an ethical point of view, says Malan, companies have to disclose income gaps between their highly paid executives and employees at the lowest end of the scale, as that would place a moral imperative to narrow the income gap. “Ethical values and good governance demand openness. Disclosure is of utmost importance.”

“I am totally opposed to imposing a maximum salary,” Malan continues. “Entrepreneurs and CEOs take the risk, and there should be justification for this risk, and reward for the value they add. CEOs will always earn substantially more than employees; that is the reality of the free market economy.” Malan adds that CEOs of South African companies are in demand globally and can work anywhere in the world. Capping their salaries would incentivise them to pack their bags and head for greener pastures.

Barney Jordaan, professor extraordinaire and lecturer in Employment Law and Negotiation at the University of Stellenbosch Business School, is also opposed to maximum salaries. He says only market forces can regulate salaries fairly. However, Prof Jordaan says serious efforts must be made to narrow remuneration gaps. “Major upskilling is required to allow workers to be more competitive and therefore earn better salaries.”

While there’s a good dose of corporate greed, says Jordaan, there is also a major lack of skills at the lower end of the pay scale. “It’s a matter of supply and demand. Capping upper salaries will not solve the wage-gap issue; it won’t benefit anybody. The answer does not lie in capping the salaries, but in skilling the broader population,” says Jordaan.

“There is no need to tamper with market systems; let the market solve its own problems.” Jordaan echoes Malan’s sentiments and says an unintended consequence of a maximum salary would be that senior executives will run to other economies, which would make the problem even worse as the few remaining ones would be even more expensive. >

Table 1: The Global Pay Gap, 1 April 2000

Country	CEO compensation as a multiple of average employee compensation
US	531
Brazil	57
Venezuela	54
South Africa	51
Britain	25
Canada	21
China (Shanghai)	21
Sweden	14
Germany	11
South Korea	11
Switzerland	11
Japan	10

This means: In 2000 nobody beat the US when it came to the difference in pay between CEOs and the average worker. (Average employees were assumed to be working in industrial companies with about \$500 million in annual sales. In 2000, on average, CEOs at 365 of the largest publicly traded US companies earned \$13.1 million, or 531 times what the typical hourly employee took home. In 2000 a CEO earned more in one workday (there are 260 in a year) than the average worker earned in 52 weeks. In 1965, by contrast, it took a CEO two weeks to earn a worker's annual pay.) Around the rest of the world, Latin America and South Africa were the leaders in pay disparity, though not close to the US. At the other end of the spectrum, Japan had the smallest gap between CEO and average-worker pay.

Source: Calculations based on estimates by Towers Perrin, 1 April 2000 (a selection)



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Table 2: The growing South African income gap, 1995 – 2005

Year	Gini coefficient
1995	0.60
1996	0.61
1997	0.62
1998	0.62
1999	0.63
2000	0.63
2001	0.64
2002	0.64
2003	0.64
2004	0.64
2005	0.65

This means: South African income inequality has increased steadily from 1995 to 2005, as measured by the Gini coefficient.

Source: *Global Insight Southern Africa, Regional Economic Focus 2005*

The remuneration issue is a matter of supply and demand and that determines levels of pay at both ends. “Clearly the demand for chief executives far outstrips their supply,” says director of the Institute for Futures Research, Prof André Roux. “At the lower end there is an excess supply of unskilled workers. The long-term solution to that is

to upskill both levels.” Roux says the country clearly needs to produce more chief executives so as to force down their pay levels, while at the same time reducing the numbers of unskilled workers by encouraging more training.

Roux says it is not only through university education that the upskilling can be achieved. Attributes like a willingness to take risks are necessary. “The question is: how many people are willing to be chief executives in this country? How many people are willing to be entrepreneurs?”

People must be taught how to take risks, says Roux, and to start their own small businesses. That could be achieved by teaching subjects like entrepreneurship from the first year of schooling. In such a scenario, the unemployed in the labour pool would be reduced as more people would either become self-employed or work for small and medium enterprises, and the result would be narrower gaps of income. But that is a long-term outcome and, according to Roux, there can be no quick-fix solution to this issue. □