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STRATEGY FOR A PUBLIC SECTOR WAGE POLICY IN KENYA

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STRATEGY FOR A PUBLIC SECTOR WAGE POLICY IN KENYA

1. The purpose of this memorandum is to view the issue of wages and salaries in the public sector from the perspective of the national economy. The level and structure of wages and salaries in the public sector have several important consequences for the economy. It is, therefore, important that the decisions on changes in public sector wages and salaries should be taken in the light of their effect on national economic and social objectives.

PUBLIC SECTOR WAGES IN THE NATIONAL ECONOMY

2. The above consideration is particularly relevant in a country such as Kenya where the public sector plays an important role in the economy. An indication of this role is given by the fact that in 1966 the public sector accounted for £51.7m. or 21% of the estimated monetary gross domestic product for the year. In terms of employment, the public sector, including E.A.C.S.C., accounted for 30% of the total recorded employment, or about 178,000 out of a total of 594,000 in 1965. Likewise, the public sector contributed over 31% of the total gross fixed capital formation carried out in 1965. These figures underline the major contribution made by the public sector to the generation and future growth of national income in Kenya through provision of administrative social and economic services and through investment activities.

3. The importance of the level and the structure of wages and salaries in the public sector derives from various factors. In the first place, the Central Government and the local government authorities, with which the Commission is primarily concerned, between them offer employment to over 145,000 persons. The wages and salaries policy of the Government, therefore, has a direct and immediate impact on the economic welfare of a large number of persons. In its capacity as an employer, the Government, like any enlightened employer, is intimately concerned to promote the welfare of its employees by offering adequate remuneration and conditions of service. Indeed its obligations as an employer go beyond those of private employers, since it provides, and is expected to provide, leadership in employee/employer relations to other employers in the country.

Furthermore, the efficiency of Government operations is vitally affected by the level of wages. Unreasonably low levels of remuneration for civil servants can have disastrous effects on the quality of public services by generating instability and discontent, and by encouraging corruption. Similarly, adequate differentials and increments may be necessary to attract and retain scarce skills and to provide continuing incentives for improvement.

But unlike private employers, the government also has obligations to the general public to provide certain vital services and to accelerate the economic development of the country. It is for this reason that no government can afford to neglect the wider economic repercussions of its wages and salaries policy.

4. It may be useful to list some of these repercussions of public wages and salaries policy. In recent years, remuneration of employees has tended to absorb over 40% of the Central Government's recurrent expenditure: this proportion is considerably higher for local authorities. On the other hand, about three-quarters of the recurrent revenue of the Central Government is derived from taxation. These figures show the close relationship between the remuneration of employees and the burden of taxation. Thus for a given quantity and quality of public services, any changes in the wages and salaries of civil servants will lead to corresponding changes in the tax burden. The latter in turn will affect the distribution and growth of national income.

Alternatively, with a given amount of public revenue, and hence the degree of tax burden, the general level of remuneration will directly affect the quantity of public services provided. A general increase in wages and salaries, with a given amount of public revenue, will reduce the quantity of public services by increasing its price per unit. In a period of expanding public services, it will limit the rate of growth of public services.

5. Secondly, an important repercussion of the government's wages and salaries policy is its effect on the private sector. If the public sector were a relatively small one, the effect of its wages policy would be no

different from that of any other employer. It will be faced with a given level and structure of wages. But in view of the importance of the government as an employer, its wages policy has a marked influence on wages in other sectors of the economy. It is no exaggeration to say that the private sector takes the government wages as a norm and relates its own wages as far as possible to those obtaining in the government. This gives the government considerable power to influence the whole spectrum of wages in the economy. At the same time, it imposes an additional constraint on the determination of an appropriate wage and salary structure for the civil service.

6. Thirdly, the wages and salaries policy of the Government will have a crucial influence on the volume of total employment in the country. This is obvious in the case of the public sector. Assuming a given amount of revenue for the Central Government and local authorities, employment and wage levels are inversely related: higher average wage rates imply lower employment and vice versa. In a growing economy, with rising revenues, wage levels will determine the rate of growth of employment.

In the private sector, there may not appear such an obvious relationship between wage rates and employment. But even here there would appear to be some inverse relationship between wage rates and employment, especially in the export sector. Since, as we have seen, wages in the private sector are influenced by those in the public sector, the government wages policy will also affect the volume of employment in the private sector.

7. Finally, and perhaps most importantly, the level of remuneration in the public sector affects the volume of public investment, and hence in the long run, the share of public sector in the economy. The most important sources of funds for public investment are foreign loans and grants, domestic loans and surplus on the current budget. The general level of wages has an important influence on the size of the surplus that might be achieved on the current budget.

Furthermore, even when the necessary finance for a capital project is forthcoming, its implementation may be held back by the inability of the Central Government or of the local authorities to meet the resultant recurrent expenditure.

... 4.

This argument is particularly relevant to the local authorities in Kenya which are faced with inelastic tax revenues. Again the inability of the government to raise adequate finance from domestic sources may result in the loss of a much larger amount of investment either because of the foreign donors insistence on government participation in the project or because of the limitation of foreign contribution to the foreign exchange costs of the project. Thus the lack of adequate domestic finance available to the government could be an important constraint on the growth of the economy.

Some Recent Economic Trends in Kenya

8. In order to see the relevance to Kenya of the arguments set out above, it may be helpful to describe briefly recent trends in certain key economic variables. Immediately prior to independence, during the period 1960-62, the Kenya economy suffered a serious set-back. This was reflected in marked slowing down of the growth of the economy, in falling employment and investment, and in stagnant revenue and exports. The period 1963-66, however, has seen a strong recovery of the economy and all the indications point to a continued strength and growth of the economy over the next few years.

9. For our purposes, it is especially useful to analyse recent trends in Central Government expenditure and revenue, African recorded employment and wages, and cost of living indices. These statistics are presented in Tables 1 to IV. It will be seen that the growth rates of both recurrent and development expenditure show considerable annual variation. Between 1958/59 and 1965/66, the recurrent expenditure has increased at a cumulative rate of about 7.7% per annum; between 1959/60 and 1965/66 at a rate of 9% p.a. Evidence will be presented below to support the view that in future there may be a tendency for recurrent expenditure to increase at an even faster rate.

Table II traces the growth of recurrent revenue and receipts from taxation. Recurrent revenue increased by 6.6% p.a. between 1958/59 and 1965/66, while tax receipts, which are a more meaningful index, increased at a cumulative growth rate of about 5.8% p.a. Table III assembles some data on changes in recorded African employment, estimated annual wage bill and average earnings. The most significant fact that emerges from this table is that whereas between 1960 and 1965, recorded employment declined by over 10%, average African earnings increased by about 87%. Part of the decline in recorded employment is apparent rather than real: for instance, decline in agricultural employment due to the shrinkage of the large farm sector is recorded, while increased employment on small African farms is not fully reflected in the official employment statistics. But even when an allowance is made for this, the fact remains that employment has been extremely sluggish in the face of a substantial increase in production. The total decline would have been even greater but for an increase of about 10% in the public sector employment over the period. The employment situation contrasts sharply with the average earnings for Africans, which have increased at a cumulative rate of about 13.3% per annum between 1960 and 1965. The rise in the public sector has been nearer 14.2% p.a. These figures cannot be taken as an accurate index of increase in wage rates because they are influenced by the progressive Africanization of better paid jobs. But even when an allowance is made for this factor, it appears that wage rates have increased at a very rapid rate in recent years, probably in the region of 10% p.a.

Although the level and growth of employment is determined by a variety of complex factors, there is now general agreement that the rapid rise in wage rates in recent years has contributed, in an important way, to the stagnation in employment.

11. Finally, the available information on cost of living indices is brought together in Table IV. It will be seen that between 1960 and 1966 the low income index and the higher income index increased by about 14% and 18% respectively. The middle Income Index was started in July, 1964: it rose by 6% in two and a half years. It will, therefore, be seen that even when allowance is made for cost of living changes, there has been a very definite increase in the real income of African employees. This would appear to be particularly the case with employees in lower income groups where the wage earners index has increased at an annual average rate of 2.3%, most of the increase occurring in 1965 - 1966.

... 6.

WAGE POLICY IN THE PUBLIC SECTOR

12. The burden of the arguments presented in the preceding sections has been that the policy towards wages and salaries in the public sector must be formulated in the light of its impact on the national economy and of the recent economic trends in the country. The main objectives of the government's wages and salaries policy may be stated in general terms as follows:

(a) to promote efficiency and stability in civil service by means of an appropriate level and structure of wages and salaries.

(b) to reduce progressively wide disparities in the emoluments of different groups of civil servants and

(c) to facilitate the achievement of national economic goals such as rapid growth of the economy, expanding employment and increased share of the public sector in the economy.

It is clear that to some extent there will be a conflict among the objectives outlined above e.g. between (a) and (b), (b) and (c), and within (c). It then becomes necessary in the formulation of a wages policy for the public sector to weight these objectives in accordance with the national priorities. The recommendations set out below reflect these priorities as stated in various government policy documents.

13. It would appear from an evaluation of the recent economic trends in Kenya in the light of the general arguments presented earlier that it would be contrary to the national economic interest to recommend a general increase in civil service wage and salary rates. The arguments supporting this conclusion are reviewed below. This conclusion does not, of course, imply that there should be no changes in wage and salary scales. For one thing, there are various anomalies in the existing salary structure, which it would be desirable to remove. Secondly, certain changes will be required by the need to encourage the increased supply of certain skills which are in short supply but are vital for the economic growth of the country. Thirdly, considerations of social justice should influence the recommendations of the Commission in respect of the lowest paid group of civil servants.

14. The conclusion that it would be unwise at this juncture to recommend a general increase in civil service wage and salary scales is supported by a number of arguments. One of the most important of these relate to the effect on recurrent expenditure of any such recommendation. Some of the studies recently carried out show that even in the absence of any revision of wage and salary scales, the Central Government recurrent expenditure is likely to increase at a rate substantially in excess of that projected in the Development Plan. It was seen earlier that recurrent expenditure has increased at a cumulative rate of 9% p.a. between 1959/60 and 1965/66. This rate is already above the official government ceiling rate of 7% p.a. What is more, there are strong reasons to believe that it may prove difficult in future to keep the growth of recurrent expenditure below even the 9% rate achieved in recent years.

Recurrent expenditure is affected by five main factors:

(a) the implementation of public development projects.

(b) expansion of recurrent services involving no capital outlay:

(c) upward creep in emoluments due to the incremental salary scales, caused by the age distribution of civil servants

(d) the progressive filling up of vacancies

(e) debt servicing.

All these factors are expected to impart a strong upward trend to the recurrent expenditure of the Central Government as well as of the local authorities in the coming years.

Although no comprehensive projections of the Central Government recurrent expenditure are available, projections of certain key ministries bear out the explosive potential of growth in recurrent expenditure. One of the studies shows that in the absence of any salary increase and on the basis of fairly conservative assumptions about the rate of expansion of primary school enrolments and of a modest upgrading of the quality of primary school teachers, recurrent expenditure on all education is expected to grow by 55% between 1966 and 1970, or at a little less than a cumulative rate of 12% p.a.

It seems likely that popular pressures for more primary and secondary education will lead to higher enrolments than those assumed in the study, raising the growth rate nearer to 14%. This is twice as high as the 7% ceiling put down in the Development Plan. The growth of recurrent expenditure on agriculture is likely to be equally rapid. Thus a general increase in salary scales will further intensify the strong upward trend in recurrent expenditure.

15. If the growth of expenditure is seriously out of line with the growth of revenue, either the size of the public sector development effort must be scaled down, or the tax burden must be greatly increased; neither of these alternatives are likely to be conducive to maximum growth. If the former alternative is adopted, it could slow down the growth rate of the economy as well as reduce the redistributive effect of public social and economic services. Likewise the latter alternative may lower growth rate by affecting adversely the incentives to work, to save and to take risks.

It will also become more difficult to achieve a surplus on the current budget, thus limiting public investment both directly and indirectly by reducing the inflow of foreign private and public capital in the manner indicated above.

16. Finally, a general increase in civil servants' remuneration will limit the ability of the public sector to generate additional employment. The consequences may be especially serious for the local authorities whose revenue tends to be inelastic. Already several local authorities are finding it difficult to meet their employees' wage and salary bill. Any increase in this bill will lead to a further loss in employment by the local authorities.

Similarly, through its influence on private sector wages, a rise in public sector remuneration will have an effect on the total employment in the economy. In particular, some of the agricultural export industries which are not in a position to pass increased wage costs to consumers through higher prices will be hit hard by increase in wage rates. After several years of decline, recorded employment increased in 1964. It is important that the public sector wages policy should not contribute to a reversal of the upward trend of the last three years.

17. All these arguments constitute a strong case for wage restraint in the public sector. It may, therefore, be useful to evaluate some of the arguments generally advanced in support of pay rise for different groups of civil servants. As far as high level civil servants are concerned, a justification for higher salaries is sought in the current scarcity of high level manpower and the alleged loss of civil servants to the private sector. As for the latter argument, it remains to be shown that the existing salary scales, except for some technical and professional posts, are inadequate to attract and retain suitably qualified persons. A prima facie evidence on this is the fact that an overwhelming proportion of skilled African manpower is currently employed in the public sector. Nor is there enough evidence of the drift of experienced civil servants to the private sector. There seems to be just as much evidence of the contrary trend.

It is true that there is a continuing tightness in the market for skilled labour. But even here the position varies a good deal with respect to different types of skills. Furthermore, even in a situation of general scarcity, it does not follow, for a number of reasons, that raising salaries would be the appropriate solution. In the very short run, the stock of domestic high level manpower is given, and an increase in salaries is unlikely to increase its supply. Even in the longer run, the main constraint on the supply side is provided by the capacity of the training institutions. Under the existing system in Kenya, the costs of acquiring high level qualifications are insignificant to the individual since they are largely borne by the state, while the salaries of skilled labour are relatively so high that there already exists a powerful financial incentive to acquire such skills. The raising of salaries in a situation of this sort will only have a marginal effect on the supply of skilled labour.

It may, however, lead to a reallocation of the existing labour from one industry or sector to another. In the situation under consideration, the public sector will only be successful to the extent that the private sector does not follow suit by raising salaries in turn. Changes in salary scales can play some role in influencing the pattern of skills supplied. Thus it would be desirable to adjust the A scale to offer greater incentive to acquisition of certain technical and professional qualifications. But even here it would appear that other methods such as differential bursary rates, improved dessimination of information on labour markets etc., may be more desirable in influencing the flow of manpower into different occupations.

18. Furthermore, the manpower supply situation is changing rapidly in Kenya, as indeed in most African countries. In view of the relative rigidity of wages and salaries in the public sector, it would be a short-sighted policy to base recommendations solely on the existing scarcity of high level manpower.

Finally, an increase in the salary scales for higher level civil servants would go against the policy of reducing income differentials in the country and may generate social and political discontent.

19. The same sort of arguments also apply to the demand for higher salaries by middle level civil servants with the important difference that there is no generalized shortage of labour here. Once again there are specific shortages e.g. of stenographers and accountants, but no overall shortage of qualified personnel to man the middle-level posts.

The main problem here is the elimination of anomalies in the current salary structure. These anomalies derive from various sources. Firstly, in certain cases there are unnecessarily wide differentials for similar jobs; these differentials merely reflect the fact that certain posts were reserved predominantly for members of one race or another during the colonial period. Secondly, some of the anomalies have arisen from the fact that certain salary scales were linked to qualifications from particular institutions. Although the quality and length of training may not be too dissimilar at two different institutions, the salary scales applicable to graduates of these institutions differ a good deal. The third type of anomaly consists of unjustifiably wide differentials in salaries attached to comparable posts in different occupations. The identification and elimination of such anomalies will make considerable contribution to increased efficiency and equity in the civil service.

20. There are similar pressing economic arguments against a rise in the wages of the lower ranks of civil servants. The employment argument is particularly relevant here, especially for the local authorities. But it appears that on balance there is a strong equity case for a modest increase in the wages of the lowest paid workers in the public services, particularly in view of the recent sharp rise in the wage earners Index.

CONCLUSION

21. The basic theme of this memorandum has been the need for restraint in fixing wages and salaries for the employees of the Central Government and the local authorities. Increases should only be granted where these are justified by the need to bring forth the needed skills, to eliminate anomalies and to improve the living standards of the lowest paid workers. The Kenya economy is now poised for rapid sustained growth; the government's wage and salary policy must be carefully devised to accelerate this growth and distribute its fruits as equitably as possible.