

Labor Market and Educational System

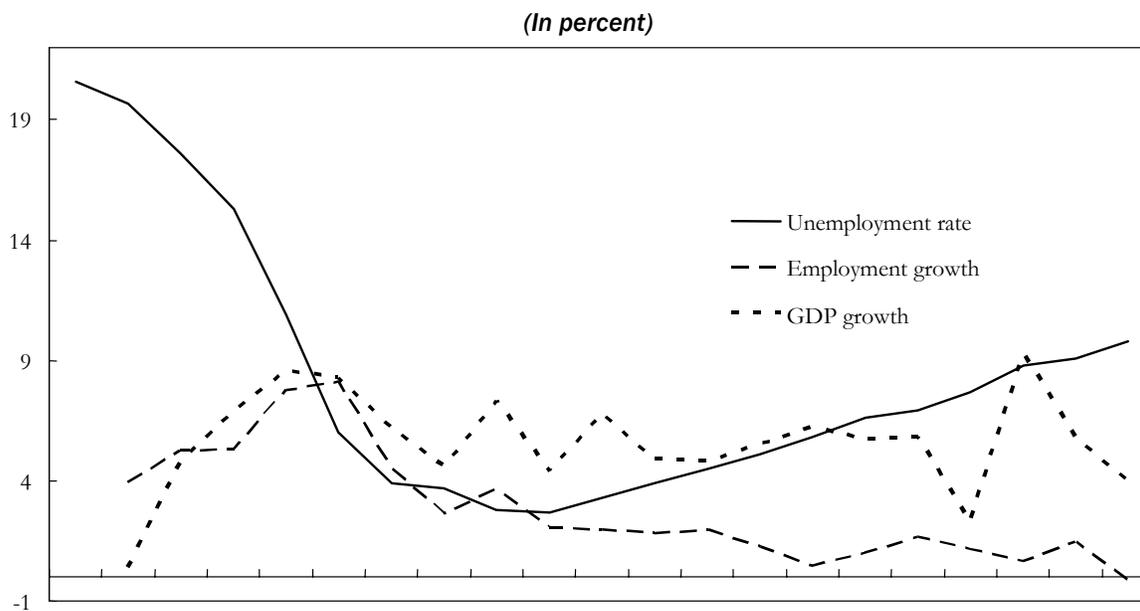
Despite strong economic growth, averaging just below 6 percent per year over the last two decades, a “U”-curve phenomenon of Mauritian unemployment can be observed (Figure 5.1). The unemployment rate plunged from about 21 percent to less than 4 percent from the early 1980s to the early 1990s. Notwithstanding sustained economic growth averaging 5½ percent per year between 1991 and 2002, the declining trend in unemployment was reversed, and the rate steadily increased, reaching approximately 10 percent by end-2002. According to the 2000 census, a majority of the unemployed were young, had never held a job, had failed primary or secondary school education, had no technical or vocational training, and were single and family supported. Despite the rising unemployment rate, two paradoxical facts about the 1990s can be noted: (1) the EPZ was crippled by skilled labor shortages and was compelled to import foreign workers, mainly from China; and (2) the number of unfilled skilled-job vacancies, especially in the financial services sector, increased over the decade.²¹ There is little consensus in Mauritius as to the exact nature and causes of the unemployment problem.²²

The problem of unemployment in Mauritius can be considered to be twofold (Box 5.1). On the demand side, real average compensation has tended to grow

²¹In its 2002 report, the Bank of Mauritius states that “while vacancies advertised have been principally for skilled and management jobs, the vast majority of persons seeking jobs do not have the necessary training, reflecting the mismatch between available labor and skills required.”

²²Mauritian unemployment figures are derived from incomplete data, reflecting, in the main, conditions in “large establishments.” The Mauritian Central Statistics Office is of the view that there is a tendency for people to falsely declare themselves as unemployed. The false responses to questions regarding employment and income might be explained by the respondents’ hopes of receiving some current or potential unemployment benefit. In the case of people engaged in the informal sector, they may not wish to acknowledge their employment and income, because of fear that the questionnaire may be used for tax collection purposes.

Figure 5.1. Real GDP Growth Employment Growth and Unemployment Rate, 1982–2002



1982 1983 1984 1985 1986 1987 1988 1989 1990 1991 1992 1993 1994 1995 1996 1997 1998 1999 2000 2001 2002
 Sources: Central Statistics Office and IMF staff estimates.

faster than labor productivity (Figure 5.2) because of the wage-setting institutions described below, which have had a dampening impact on employment. But on the supply side, there is a serious skills mismatch.

Labor Market Institutions: “One Country, Two Systems”

The Mauritian labor market is tightly regulated and quite rigid. At its core, the present system of wage determination relies on centralized tripartite discussions that are held around April or May and involve the government, trade unions, and representatives of private sector employers. The tripartite system results in an annual minimum wage increase that is mainly determined on the basis of the projected annual inflation rate of the fiscal year ending in June and that applies to all employers, including those not represented in the tripartite discussions, for the following fiscal year starting in July.

Box 5.1. Mauritius: Unemployment and the Labor Market

Against a background of profound structural change and strong growth performance, the unemployment rate in Mauritius has been steadily rising, reaching 9.8 percent in 2002. According to the 2000 census, the majority of the unemployed were young, had never held a job, had failed primary or secondary education, had no technical or vocational training, and were single and family supported. The principal causes of rising unemployment can be found in the characteristics of both the labor supply side and labor demand side of the Mauritian labor market.

Labor market institutions and the educational system

The Mauritian institutional arrangements governing the functioning of the labor market are as follows. (1) A centralized tripartite system involving the government, trade unions, and the private sector, resulting in an annual minimum wage increase based on the projected inflation rate. This system tends to drive up real wages throughout the economy at a faster rate than productivity growth. (2) Quasi-judicial labor review bodies, principally, the National Remuneration Board and the Permanent Arbitration Tribunal for the private sector, and the Pay Research Bureau and the Civil Service Arbitration Tribunal for the public sector. These institutions regulate working time and conditions, and establish minimum wage adjustments that can be above those agreed upon in wage negotiations. Decisions are based on both economic and noneconomic factors. (3) The termination of Contracts of Services Board (TCSB), which settles layoff disputes. The TCSB process is slow, taking typically more than one year to resolve disputes. However, firms in the EPZ are not subject to the jurisdiction of the TCSB.

Demand-side causes of unemployment

The trend of rising unit labor cost has had a dampening impact on job creation and competitiveness and also may have caused some degree of substitution of capital for labor. In addition, the rising minimum wages in the EPZ have constrained domestic labor demand and created labor demand for foreign contract workers, notwithstanding the fact that continuous depreciation of the rupee in recent years has kept unit labor costs in nominal effective exchange rate terms fairly constant. Lengthy and costly layoff procedures appear to hinder firm-level job creation.

Supply-side causes of unemployment

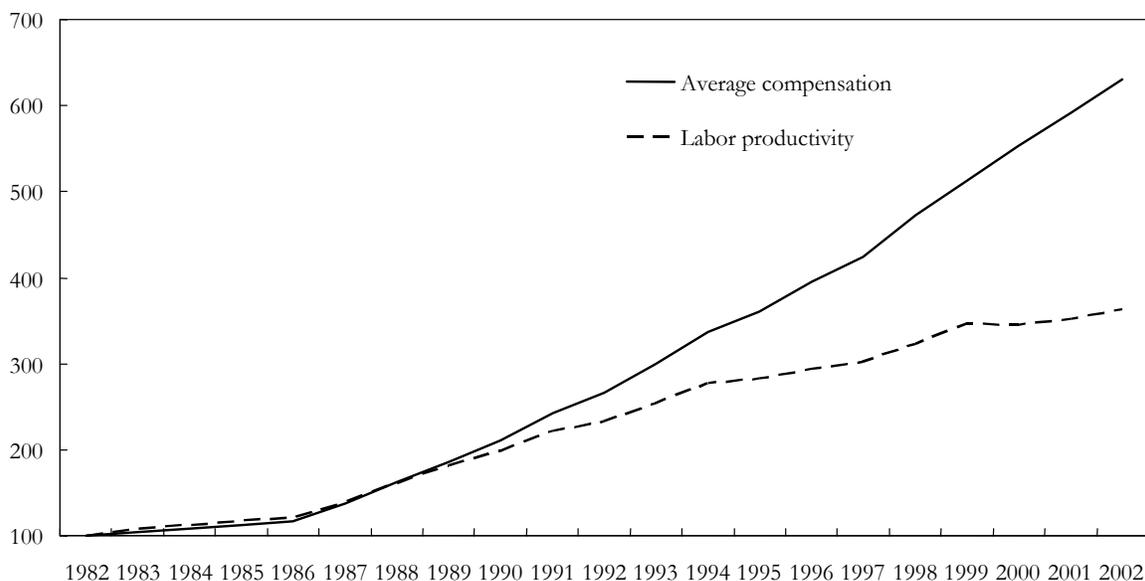
The rapid structural changes during the 1990s have increased demand for skilled workers in the financial services and tourism sectors relative to the low-skilled textile and sugar sectors. However, the Mauritian educational system failed to transform the skills held by the low-skill labor force into the higher skills that were needed by the emerging sectors, resulting in a skill mismatch problem. There is low progression from primary to secondary schools. In particular, of the total number of students enrolled at standard 1 in primary schools, about 35 percent fail to pass the completion of primary education (CPE) examination and drop out of the school system at the age of 11 or 12 years. In addition, 83 percent of those remaining in the system never reach advanced levels in secondary schools, and there is little opportunity for vocational training. At the same time, increasing minimum wages and extensive job protection elsewhere have increased the reservation wages of domestic workers in the EPZ and in other sectors.

Ongoing education reform and future labor market reforms

The Mauritian government has taken bold and comprehensive measures to overhaul the educational system, aiming at increased access, quality, and relevance at all levels, especially for the secondary level. These reforms would alleviate the mismatch on the supply side in the medium term. However, it is equally important to tackle the demand-side shortcomings by improving the present labor market institutions' flexibility.

Figure 5. 2. Average Compensation and Labor Productivity, 1982–2002

(1982 = 100)



Source: Central Statistics Office.

annual minimum wage increase that is mainly determined on the basis of the projected annual inflation rate of the fiscal year ending in June and that applies to all employers, including those not represented in the tripartite discussions, for the following fiscal year starting in July.

Individual employers are, however, free to adjust wages by more than the minimum, and this is often done, especially for the higher pay brackets. The higher percentage increase given to low wages within the tripartite system has nevertheless contributed to a compression of the wage structure and may also have been a source of a drift in the overall wage level.

On top of the tripartite system, a number of institutional bodies specified in the Industrial Relations Act are authorized to address “anomalies” in the wage structure and to settle labor disputes, including those presented by any of the parties. In the private sector, the National Remuneration Board hears such claims and makes recommendations for minimum wages and other conditions of employment by sector and by occupational category. The Pay Research Bureau and the Civil Service Arbitration Tribunal perform similar functions for the public sector. These institutions have only awarded pay increases infrequently, but the awards have been quite large, typically in excess of 10 percent.

There are significant restrictions on the ability of employers to adjust employment levels. Any reduction in the workforce of a private or a parastatal enterprise requires advance notice to the Minister of Labour and Industrial Relations, and many cases end up before the Termination of Contracts of Services Board (TCSB) (see Box 5.1). Until the TCSB reaches a conclusion, layoffs are difficult to carry out and subject to punitive severance allowances. The TCSB process is slow, taking typically more than one year to resolve. It may lead to the layoff being declared unjustified, in which case the employer is required to pay the worker six times the normal allowance or reinstate the worker to his or her former position.

The EPZ stands out by not being subject to many of the rules and regulations that apply to the labor market in the rest of the economy, notably the laws that limit firms' freedom to lay off workers. Also, workers in the EPZ are typically paid on a piecework basis, so that income is more directly tied to productivity than is the case in the rest of the economy. The relatively flexible business environment has meant that the EPZ has been an attractive place to invest. Labor productivity growth has also been strong in the EPZ, and its output growth has been above the economy's average.

While overall employment in the EPZ up to 2002 was broadly stable, there has been a substantial increase in the number of foreign workers, which stands in stark contrast to the rise in unemployment. Hardly present a decade ago, foreign guest workers, almost all of whom are employed in the EPZ, now number some 16,500—about half as many as the increased number of the unemployed over the same period. The foreign workers are predominantly Chinese contract workers in the textile industry. Mostly women, these workers typically come to Mauritius on three-year contracts with a background that includes three years of vocational training and a few years of work experience in the textile industry. A number of factors may explain the surge in the number of foreign workers. First, reportedly, Mauritian workers are increasingly viewing employment in the EPZ sector as unattractive, with little opportunity for advancement and low job security. Consequently, there is little demand for jobs in the EPZ, and firms have difficulties filling vacant positions. Second, the Mauritians who work in the EPZ are seen as less productive than the foreign laborers, who are better educated and more eager to maximize their earnings, for example, by working overtime. Finally, the nature of the fixed-term contracts of foreign workers provides additional flexibility to employers in their efforts to match the workforce to their companies' staffing needs. There is also segmentation between the domestic and foreign labor force in the EPZ, in that legal minimum wages are not applied to foreign contract workers. Therefore, wage increases for domestic EPZ workers do not necessarily lead to increases in the wages of foreign EPZ workers.

However, the tripartite system has adverse consequences for job creation. In particular, the determination of wages by the centralized bargaining system

discourages sector-specific competitive wage setting, resulting in a strong relationship between the wages of the traditional sectors and those of the emerging sectors. While the new sectors create demand for skilled workers and, thus, increase the wages in these sectors, wage increases typically follow in the traditional sectors, leading to a loose relationship between wages and productivity in the traditional sectors. The trend of rising wages in the traditional sectors reduces domestic demand for unskilled workers and tends to increase the unemployment rate of these workers. From the labor supply side, skill premium, expressed by the wage differential between the two sectors, is constrained by this stable relationship, resulting in fewer incentives for the young to invest in education and to supply skilled labor for the new sectors.

Educational System

The educational system plays a key role in supplying skilled labor. Compared with other developing countries, the Mauritian labor force is relatively well educated. The main achievement in Mauritius after independence was universal schooling at the primary level, when other lower-middle-income countries were below 80 percent. Low-income countries (excluding India and China) still averaged only 74 percent in 1992.

Mauritius pushed to open secondary schools to many of its citizens. In addition, Mauritius has been successful in expanding opportunities for overseas higher education for some of its citizens.

However, Mauritius's educational system is lagging behind the economic transformation of the economy. Although Mauritius has a comparatively high level of literacy, it is weak in secondary and postsecondary education, especially in natural sciences, engineering, and vocational subjects. As a result, the output and quality of secondary and postsecondary education and training in Mauritius remain a serious constraint to the development of new high-skilled and high-value-added sectors. Despite an enrollment ratio of almost 100 percent at the primary level, about 35 percent of students fail to pass the Certificate of Primary Education (CPE) examination and drop out of the school system at the age of 11 or 12 years. There are no viable vocational training programs for these youngsters, and they are not allowed to work or become apprentices until age 15, at which time they lack basic education and skills and are thus unsuitable for employment. It is not uncommon for many to succumb at an early age to criminal activities and substance abuse. At the other extreme are students at the so-called star schools, who excel scholastically, often with the help of expensive private lessons. Most of these students complete secondary school, and many obtain university education.

The length and quality of education in Mauritius fall short of that in many countries in East Asia, especially in the areas of science, mathematics, and

computers. The large majority of unemployment is in the categories of semiskilled and unskilled labor. Almost three-fourths of the registered unemployed as of December 2001 have not passed the CPE exam. Consequently, it is almost impossible for many workers, as well as for the unemployed, to acquire high-level skills.

Reforms Under Way

The steady rise in unemployment rates from 1991 until now in Mauritius can be variously attributed to mismatches between labor skills demanded and supplied or between excessive wages and productivity levels, due to the centralized wage-bargaining system. On the demand side, it is clear that reforms in the present institutions governing the labor market can improve its flexibility. For example, the authorities could consider introducing a new national body, representing the three social and economic stakeholders: the government, the employers, and the unions. The body could provide yearly guidelines on general wage increases. However, these guidelines should be nonmandatory at the firm level, in order to allow for flexibility in implementation and for firm-level collective bargaining (see McDonald and Yao, 2003).

On the supply side, education reforms are fundamental. Fortunately, there is a broad national consensus on the importance of reforms aimed at improving the content, quality, efficiency, and equity of access to education and therefore wide support for the government's education reform program. The government realizes that far-reaching education reforms to enhance the skills of the workforce are needed to alleviate the mismatch problem of the labor market and ensure the success of the government's plans to develop a modern information and communications technology (ICT) sector. During the last three years, the Mauritian government has implemented the following educational reforms:

- increase the years of compulsory schooling from nine to eleven years by 2005;
- improve and increase access to primary and secondary schools;
- introduce ICT in primary and secondary schools;
- review the quality and relevance of the curricula; and
- reform the examination system at the primary level.

The government has also invested heavily in school infrastructure. Over the two-year period 2001/02–2002/03, capital expenditure on education reached the

high level of MUR 1.7 billion (1.7 percent of GDP). Government recurrent expenditure on education are estimated at about MUR 4.6 billion for the year 2002/2003, representing 14.8 percent of the government total recurrent expenditure, a ratio similar to that achieved in the previous year.

Capital spending has been used to construct 19 schools and colleges on the island of Mauritius and another three educational establishments on the island of Rodrigues by the end of 2004. Thirty-three additional State Secondary Schools have become operational through new construction, conversion or upgrading, while intake in Form I in public schools has more than doubled to reach 7,700. The introduction of information technology in primary and secondary schools was completed by mid-2003. The abolition of CPE ranking and admission to the secondary level on a regional basis are also facilitating secondary schooling access.

Conclusion

The rapid structural changes during the 1990s have increased demand for skilled workers in the financial services and tourism sectors, relative to the low-skilled textile and sugar sectors. Against this background of profound structural change and strong growth performance, the unemployment rate in Mauritius has been steadily rising. Two main causes for rising unemployment can be identified. First, the highly centralized wage-determination system in Mauritius limits the skill premium, resulting in job destruction in the traditional sector and insufficient job creation in the new technology sector. Second, the Mauritian educational system has been unable to provide to the low-skill labor force the higher skills that are required by the emerging sectors, resulting in a skill mismatch problem.

Both supply-side and demand-side reforms can contribute to higher labor market flexibility, which would reduce the unemployment rate and help maintain the relatively high growth that Mauritius has recorded during the past two decades. On the supply side, the government has taken measures to improve its educational system, as indicated above.

The labor demand is affected by the relatively rigid institutional arrangements regulating the labor market. While these institutions may have played a useful role in the past, all social partners—including workers and employers—are likely to experience welfare losses under the current framework. To preserve some element of the “social contract,” the reforms could seek to introduce a

simplified, two-tier wage-determination system. At the first-tier level, a national body comprising government, employers, and workers could be maintained, but would only establish indicative nonbinding wage guidelines. At the second-tier level, wage-determination would take into account firm- and sector-specific factors, including productivity levels.