

L.C.Q. Is MRP an Appropriate Way of Setting Wages in the Public Sector

ANSWER: No, MRP is not appropriate for setting wages in the Public Sector because

- 1) **Physical Output is Not Always Produced:** Many jobs in the public sector are services, so it is difficult to measure output, thus making it difficult to measure Marginal Physical Product (MPP) and consequently MRP.
- 2) **Not Sold in the Market Place:** The goods/services produced within public sector are often not sold on the open market or at market prices. It is therefore difficult to estimate price or marginal revenue.
- 3) **Difficult to Differentiate:** When Capital and labour are used together it is difficult to estimate whether the extra productivity is due to labour or capital e.g. computerisation of government departments in the Civil Service.

Outline an Alternative Method for Determining Wage Levels in the Public Sector.

- 1) **Pay Comparability:** As productivity is difficult to measure then it may be best to compare those workers in the public sector with those workers in the private sector doing similar work / with similar qualifications.
- 2) **Benchmarking:** It was introduced by the government as a method of setting wages in the public sector. The Benchmarking Review Body examines the earnings of similar jobs in the private sector and makes a recommendation on wage increases based on this.

Possible Ways in which the Minister for Finance could Reduce the Public Sector Wage Bill

- 1) **Reduce the Numbers Employed in the Sector:** Do not fill vacancies when they occur / natural wastage. Introduce a voluntary redundancy package e.g. as in the HSE.
- 2) **Reduce Rates of Pay per Employee:** Pay new entrants into the sector lower rates of pay than existing employees. Adjust pension entitlements to reduce the cost of future pensions.
- 3) **Change Terms of Employment:** Defer incremental pay increases. Cap the pay of higher paid civil servants. Ban overtime for state employees/offer career breaks.

- 4) **Change Pension Entitlements:** Reduce the pensions given to current pension holders.
- 5) **Outsource Services:** This will mean that less staff is required in the public sector to provide these services. e.g. IT / Payroll

The Mobility of Labour

Labour Mobility refers to the ease of movement of workers from one job to another (occupational mobility), or from one area to another (geographical mobility).

Occupational Mobility of Labour:: The ability or ease of a worker to move from one job to another

E.g. An art teacher who cannot find work becomes a painter/decorator.

Geographical Mobility of Labour: The ability or ease of a worker to move from one area to another

E.g. a worker moves from Dublin to Limerick in order to take a job.

Such mobility of Labour can reduce the unemployment rate.

Unemployment will fall if workers leave an area where there are no jobs and move to an area where there are jobs. The unemployment rate will also fall if people, who cannot find work in their chosen career, seek an alternative career.

Factors which Determine Labour Mobility

- 1) **Language Differences:** This reduces geographical mobility. There is a tendency among Irish people to be more willing to move half way around the world to Australia to find work rather than move to a country like France or Germany simply due to the language barrier.
- 2) **Cost of Property:** If property is expensive in an area of high employment (Dublin during the Celtic Tiger), geographical mobility will be reduced.
- 3) **An Unwillingness to Move Family:** Many parents are reluctant to move family members from their home area as they are concerned for their happiness or the parents themselves don't want to move as they might wish to be near family. This reduces geography mobility.
- 4) **Lack of Information:** If unemployed workers are not informed of job vacancies, Labour mobility is reduced. This reduces both geographical and occupational mobility. One of the purposes of fás is to inform unemployed workers of job vacancies.

- 5) **Necessary Skills or Training:** The ability to move from one job to another is restricted by the worker to do the work required by the job. This affects occupational mobility. E.g. For a teacher to become a doctor, retraining is necessary.
- 6) **Age:** Younger people tend to be more flexible and mobile than older people when it comes to moving location or switching job. This affects both geographical and occupational mobility.
- 7) **Government Policies:** If the government actively discourages immigration, by reducing work permits etc, Labour mobility into the country is reduced.

GOVERNMENT POLICIES WHICH AFFECT THE MOBILITY OF LABOUR

Geographical Mobility

In order to increase geographical mobility the government could enact the following policies.

- 1) **Housing:** The government could increase the availability of affordable housing in areas of high employment if shortages in housing are prohibiting people moving to such areas.
- 2) **Educational Facilities:** The government could improve the availability of educational facilities to ease concerns of parents, making them more likely to move to areas of high employment.
- 3) **Social Infrastructure:** The government could increase the number and quality of amenities in areas of high employment in order to entice people to move to such areas.
- 4) **Government Support:** The government might provide adequate support so as to aid people to move to areas of high employment. E.g. The government could provide a remuneration scheme that would help people to cover the cost of the move.
- 5) **Information:** The government could set up a web site or other such amenity in order to inform people of all available dwellings and the costs involved in such a move.

Occupational Mobility

In order to increase occupational mobility the government could enact the following policies.

- 1) **Educational Courses:** Provide further education courses in order to educate people so that they are capable of performing a different job and keep the prices of these courses accessible to workers.
- 2) **Training:** Provide training programs in order to skill/retrain workers to perform different at prices accessible to these workers.
- 3) **Government Policies:** Change regulations on work permits etc in order to allow more immigrants access to institutions like fás.
- 4) **Trade Union Barriers:** Reduce barriers to entry into certain occupations. Currently it is very difficult for well educated, highly skilled medical consultants to work in Ireland because the consultants union is so strong. If they reduce entry, they keep their supply low which keeps their wages high.

Employment and Unemployment

Before we discuss employment and unemployment we will first look at a number of definitions.

Full Employment: refers to a situation where everybody who wants a job can find one at existing levels.

The Labour Force: comprises those who are unemployed (seeking work) and those in employment.

The Participation Rate: refers to the proportion of the population of a country that is in the Labour Force.

$$\begin{aligned}
 \text{Participation Rate} &= \frac{\text{Labour Force}}{\text{Population}} \\
 \text{Labour Force} &= \text{Employed} + \text{Unemployed} \\
 \therefore \text{Participation Rate} &= \frac{\text{Employed} + \text{Unemployed}}{\text{Population}}
 \end{aligned}$$

Underemployed: refers to workers whose skills/talents or time is not required or used to their full potential

E.g. A plumber who is willing to work 40 hours a week but is only able to find 20 hours work a week is underemployed. (Job Sharing, Week on/ week off etc)

The Unemployment Rate: is calculated by dividing the number of people unemployed by the Labour Force.

It is generally accepted that unemployment is a bad thing and this is why it is very worrying that nowadays many Irish people are losing their jobs.

Types of Unemployment

Frictional Unemployment: refers to unemployment that results from people who are between jobs and therefore temporarily unemployed and to job seekers that are not located where suitable jobs are available.

E.g. If a construction worker loses his job at the start of January but finds a new one that will start in August, he is frictionally unemployed for those seven months. Another example is where a construction worker is unemployed in Dublin but there is a huge demand for construction workers in Limerick. The Dublin worker is frictionally unemployed.

Structural Unemployment: arises from the change in the structure in an industry brought about by the changing pattern of demand in an economy or increasing mechanisation (technological progress)

E.g. When Dell left Ireland, Pfizer were still hiring. However the Dell workers (computer programmers etc) did not have the necessary skills (pharmaceutical education) to fill those jobs and as such remained unemployed.

Seasonal Unemployment: refers to unemployment that results from a change in the time of year.

E.g. The unemployment levels fall in Brittas Bay during the Summer as there is increased employment in the services sector to cope with the influx of tourists and falls again in the Winter months as the summer tourists leave.

Cyclical Unemployment: refers to unemployment that results from a decline in a trade cycle

E.g. Now with the credit crunch, demand for goods and services has fallen. When there is a decrease in demand there is a decrease in economic growth. People start to spend less. Firms earn less profit and as such make people unemployed in order to survive. This is Cyclical Unemployment (Recession).

Institutional Unemployment: refers to the unemployment that arises due to the obstacles to the mobility of Labour or the removal of incentives to work.

E.g.

- 1) If there are jobs available in Galway and the unemployed in Dublin wish to move to Galway to avail of these jobs but can't due to a lack of housing in Galway.
- 2) If there is high unemployment benefit this removes the incentive to work.
- 3) If there are legal restrictions on foreign Labour taking up employment.

Disguised Unemployment: Refers to those people who do not appear on the live register but are willing and able to work.

E.g. Married Women: If there was an upturn in the economy these people would take up employment, but with the economy in its current state they do not seek employment but do not claim social benefit.

Technological Unemployment: refers to the unemployment caused due to the increased mechanization and advances in technology used in industry.

E.g. The introduction of ATM machines reduced the need for bank clerks resulting in some of them being unemployed.

Wage Drift: When Wage Levels rise above Negotiated Levels

E.g. During times of economic boom, wage levels rise, which in the long run, makes labour less profitable, causing the demand for labour to fall, which results in unemployment.

Why Do Governments try to achieve Full Employment

Unemployment is a waste of scarce economic resources (labour). These resources could be used to generate wealth and as such increase the standard of living of society instead of lying idle. Also the social cost of unemployment is very high such as depression, crime and the consumption of drugs. The government must use scarce resources to combat this, which could be used in other areas, which again costs society.

Problems of Unemployment

- 1) **Decreased Government Revenue:** If people become unemployed they cease to pay income taxes which reduces the revenue of the government. This means that favourable government projects (Transport 21) might have to be put on hold due to lack of funds.
- 2) **Increased Government Expense:** In order to try to ensure that those who are unemployed have at least some standard of living the government pays them social welfare. The more people unemployed the greater the amount of social welfare payments the government must make.
- 3) **Economy is producing at Below Capacity:** This is wasteful of resources but also results in many people emigrating. This is bad because it reduces the Labour force (which reduces the country productive capacity) but also many educated people leave which reduces the amount of human capital in society.
- 4) **Depression and Social Exclusion:** Many people who lose their jobs feel ashamed and lose their sense of self worth. This may lead to depression and drug addiction leading to greater social problems and increased expenditure on crime prevention.
- 5) **Reduced Disposable Income:** The unemployed have very little money available to them to spend. The less money people have to spend the lower the level of demand in the economy. The lower the demand the lower the level of economic growth which causes more unemployment. It is a self perpetuating cycle.

How can the Government Create Employment?

- 1) **Reduce Taxation:** If the government reduced rates of VAT this would remove the divergence between rates of VAT in the Republic and those in Northern Ireland. It would also help reduce prices. This may encourage people to spend, thereby increasing demand and leading to an increased demand for labour.
- 2) **Subsidise Additional Labour Employed:** If the government reduced the rates of PRSI on additional labour hired it would help reduce the cost of labour and may encourage employers to hire additional labour.
- 3) **Reduce Costs for Business:** The government could, through regulation, force those firms supplying utilities to reduce their prices. This could reduce the costs for businesses, which may lead to a reduction in prices. Demand may increase resulting in an increased demand for labour. This may help decrease export prices thereby increasing aggregate demand, resulting in employment.
- 4) **Prudent Management of the Economy:** Many economic commentators suggest that the government needs to restore confidence in the public. If confidence is restored then people will start to spend, resulting in increased aggregate demand and boost employment. Thus prudent economic management of the economy is essential to restore confidence.
- 5) **Infrastructural Development:** Funding of improvements in the capital and social infrastructure directly leads to employment in the construction industry and, through the multiplier effect, leads to increasing spending and growth in employment.
- 6) **Maintain a Low Corporation Profits Tax Base:** The low rate of CPT is seen as an essential element for Ireland to continue to attract mobile foreign direct investment. This can be used as part of the package used to attract companies to Ireland and so increase employment.
- 7) **Investment in Education and Training:** One of the factors which attracts companies to set up in Ireland is the availability of an educated, skilled workforce. To maintain this advantage the government must continue to invest in education and training. Investment will allow workers to up-skill and so acquire those skills in demand currently. Possible availability of EU funding for training and up-skilling workers.

Measuring Unemployment

There are two main methods used to measure the unemployment rate in Ireland.

- 1) The Live Register.
- 2) The Quarterly National Household Survey (QNHS).

Both of which are calculated by the Central Statistics Office.

The Live Register: is a record of all those in receipt of social welfare payment.

Functions of the Live Register

- 1) It measures the current level of unemployment.
- 2) It measures the trends in unemployment over a number of years.

Is the Live Register Accurate

ANSWER: No. The Live Register is not an inaccurate reflection of the level of unemployment in the country because.

- 1) There are many people who are claiming benefit who are not unemployed but have illegal jobs in the Black Economy.
- 2) There are people with legal jobs who receive the dole illegally.
- 3) There are people who are unemployed but do not seek the dole or register themselves as unemployed.
- 4) There are many people who are available for work, for legal reasons, cannot claim benefit such as men and women is full time home duties.
- 5) People who are incapable of working and therefore who are not be in the Labour Force, are on the Live Register.

The Live register is not considered as accurate as the QNHS as it is considered to overstate the unemployment rate.

The Quarterly National Household Survey (QNHS): is a survey of 39,000 households, carried out every three months, and the employment status of those surveyed is used as an indication of the National Unemployment Rate.

The CSO conducts a survey each quarter and places all those surveyed who are over 15 into one of three groups, Employed, Unemployed or not in the Labour Force.

The Quarterly National Household Survey provides a more accurate measurement of Irish unemployment than the Live Register because it excludes

- 1) People 'signing on' who are actually working.
- 2) People who work Part-time (working up to 3 days per week), seasonal workers and casual workers (who are entitled to Unemployment Benefit / Unemployment Assistance if they meet the statutory requirements).
- 3) People who claim Unemployment Allowances or Unemployment Benefits who are not seeking work and/or are not available for work.
- 4) The QNHS includes those people who are unemployed, but for many reasons, may not draw the dole and do not sign on.

Tax Wedge

When discussing pay and rewards in the workplace, we must remember that the employee must pay income tax on his pay. Employers may also have to pay a portion of PRSI (Pay Related Social Insurance, which can be classified as payroll tax) on behalf of the employee also. There is a difference between the cost of Labour to the employer and what the employee brings home. This difference is known as the Tax Wedge.

Tax Wedge: The difference between after tax income received by the employee and the wages (including payroll taxes) paid by the employer.

EXAMPLE:

<u>WAGES</u>	<u>EMPLOYER PRSI</u>	<u>EMPLOYEE PRSI</u>	<u>PAYE</u>	<u>TAKE HOME PAY</u>
40,000	3,000	5,500	8,000	26,500

The Total Cost to the employer from employing the worker is €43,000, but the employee's take home pay was €26,500. Here the tax wedge is €16,500.