



Social networks, employment and worker discouragement: Evidence from South Africa

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ABSTRACT

Social networks are increasingly being recognized as having an important influence on labour market outcomes, since they facilitate the exchange of job related information. Access to information about job opportunities as well as perceptions about the buoyancy of the labour market depend critically on the social structures and the social networks to which labour market participants belong. In this paper, we examine the impact of information externalities generated through network membership on labour market status. Using Census data from South Africa, a country characterized by high levels of unemployment and worker discouragement, we adopt an econometric approach that aims to minimise the problems of omitted variable bias that have plagued many previous studies of the impact of social networks. Our results suggest that social networks may enhance employment probabilities by an additional 3–12%, and that failure to adequately control for omitted variables would lead to substantial over-estimates of the network co-efficient. In contrast, the impact of social networks on reducing worker discouragement is much smaller, at between 1 and 2%.

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1. Introduction

Networks matter for economic and social outcomes, since they allow for complex social interactions to take place between individuals, thereby facilitating information spillovers and learning between network members, as well as the transmission of norms and values (Banerjee, 1992; Bikhchandani et al., 1992). While information spillovers have been widely examined by economists, as affecting fertility decisions, education decisions (Coleman et al., 1966), participation in criminal activities, (Besley and Coate, 1992; Borjas, 1995, Case and Katz, 1991), and consumption (Abel, 1990), in this paper we focus primarily on information externalities generated through network membership as they pertain to employment prospects.

Arguably, it is now a stylized fact that individuals rely on friends, family and acquaintances (or “weak ties” in the parlance of Granovetter, 1974¹) to find jobs, and while reliance on these social networks may

vary by location and demographic characteristics², these channels are usually productive (Calvo-Armengol and Jackson, 2004; Blau and Robbins, 1992; Montgomery, 1991). Moreover, reliance on networks to find employment typically results in better matching between the job candidate and the available job, reduces employer uncertainty about worker productivity, and may even enhance job satisfaction and employee loyalty (Datcher, 1983; Devine and Kiefer, 1991; Marsden and Gorman, 2001). Obviously, this is conditional on the “quality” of one’s network. When an individual’s contacts are unemployed, the likelihood of getting information about jobs through contacts is reduced, thereby impeding such network benefits, reducing active search behaviour (Devine and Kiefer, 1991; Kingdon and Knight, 2001) and increasing the duration of unemployment. Thus, heterogeneity in network effects is important since it can explain changes in wages and employment inequality over time. Arrow and Borzekowski (2004) show that networks explain 15% of the unexplained variation in wages and a substantial portion of the disparity between black and white income distributions. This is exacerbated if one allows for the fact that social networks are largely endogenous or self-selected.

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¹ The extent to which networks serve as efficient conduits of information concerning job opportunities depends on the strength of ties amongst individuals in the network—Granovetter (1974, 1995) argues that strong ties are those that link close friends while weak ties are those that link acquaintances, and that weak ties are relatively important in helping individuals find access to employment, since these weak ties bring information about opportunities available outside the individuals immediate circle and locale.

² For example, the empirical evidence to date suggests that network effects are particularly important in poorer communities (Elliot, 1999) and that reliance on networks varies demographically, with, for example, women being less reliant on networks than men. (Ports, 1993; Bradshaw, 1973).

Table 1
Narrow and broad unemployment rates.

	Census 2001
A. Total employed	768,701
B. Total unemployed (official definition)	561,432
C. Total economically active = A + B	1,330,133
D. Narrow unemployment rate = B/C	0.422
E. Total unemployed (broad definition)	689,414
F. Total economically active (broad definition) = E + A	1,458,115
G. Broad unemployment rate = E/F	0.472
H. Not searching/discouraged as fraction of unemployed	0.186

Notes:

Data source: 10% sample of the 2001 South African Census.

Sample is limited to the economically active population, that is, individuals aged 15–65 years; all non-housing units and non-participants (with the exception of discouraged workers) in the labour force are excluded.

An individual is recorded as being employed in the Census if they responded “Yes” to the question “In the 7 days before 10 October, did (the person) do any work for pay (in cash or kind), profit or family gain for 1 hour or more?”. The responses include (a) Yes: formal registered (non-farming) (b) Yes: informal unregistered (non-farming) (c) Yes (farming) (d) Yes, has work but temporarily absent (e) No, did not have work. An individual is recorded as employed if they responded Yes to (a) through (d).

The narrow unemployment rate of 42% based on the 2001 Census is substantially higher than the narrow rate of unemployment of 29.5% estimated by the 2001 September Labour Force Survey (LFS). However, the broad unemployment rates are less divergent, with the 2001 Census estimating a broad unemployment rate of 47% compared to a broad unemployment rate of 41.5%. These differences may be attributed to the fact that the LFS is a far more sophisticated labour market survey instrument than the Census, designed to capture a whole range of employment activities in the informal and subsistence agriculture sectors, particularly among those working only a few hours per week. The labour force survey questionnaire includes many more prompts to identify such people, which is not possible during Census enumeration. This may account for the large differences in the narrow rates of unemployment between the two datasets.

Within the context of very high levels of unemployment and worker discouragement in South Africa (see Table 1) combined with relatively low absorption of the unemployed into the informal sector (Kingdon and Knight, 2001), understanding the effect of networks on employment prospects is arguably critical, especially since job search methods in South Africa are predominantly passive, with most jobs being obtained through word-of-mouth and other informal recruitment methods (Kingdon and Knight, 2001). Using the Special Retrospective Survey of Employment and Unemployment (SRS) dataset, Statistics South Africa (1998) reports that just under 20% of individuals cite high costs as the reason they do not engage in active job search. This decision not to search owing to high costs may be exacerbated for individuals living in areas characterised by high levels of worker discouragement. Such individuals may believe that there is little chance of finding work, even if they spend the necessary money to reach the job market, since this is the experience of others in their community, and so, may rationally decide to not actively search as the opportunity cost of the transport is too high. At the same time, large numbers of firms rely on informal recruitment methods. Standing et al. (1996) use firm level data from South Africa to show that 41.4% of all firms studied relied on friends and relatives of their existing employees to recruit new workers. This reliance on informal methods may be attributable to the poor signaling content of the school-leaving exam qualification, given the continuing discrepancies in educational quality, as well as to the high costs associated with formal recruitment procedures, especially for relatively low skilled jobs.

Yet, until relatively recently, the South African literature on job search and employment has focused on individual job search and work choices in isolation, ignoring the potential influence that social networks, constituted by families, peers and acquaintances, might have on these individual decisions. Networks facilitate the exchange of job related information (Ioannides and Loury, 2004), be it about actual job openings or about the paucity of such opportunities. Thus, access to information about job opportunities as well as one's perceptions about

the buoyancy of the labour market may depend critically on social structures and the social networks to which individuals belong. The work that has been done examining the impact of social networks on employment status in South Africa has mostly defined the network as the number of other household members who are employed. (see Wittenberg and Pearce, 1996; Mlatsheni and Rospabe, 1999; Schoer and Leibbrandt, 2006). Wittenberg and Pearce (1996) find that in South Africa, these networks positively influence access to jobs, while Mlatsheni and Rospabe (1999) find that they significantly increase the probability of youth being in wage employment. Wittenberg's (1999) non-parametric analysis is also suggestive of a household network effect as it indicates clustering of employed and unemployed individuals³. Using a non-representative survey for a specific magisterial district located near Cape Town, Schoer and Leibbrandt (2006) demonstrate that unemployed individuals who report that they have contacts in the labour market are significantly more likely to rely on social networks in searching for a job, and that the difference between relying exclusively on social networks as opposed to more active search methods depends crucially on contact availability. Moreover, they also show that unemployed individuals who report that they rely on social networks to search for jobs are more likely to live in households where at least one household member is employed compared to unemployed individuals who rely on more active search methods, such as place-to-place searches or relying on newspapers. However, all of these studies are plagued by omitted variable bias (which we discuss in more detail below). Specifically, it is difficult to disentangle whether unemployed individuals relying on social networks to find jobs are simply more likely to live with employed individuals who support them while they engage in search behaviour, or whether the presence of an employed individual in the household lowers job search costs for the unemployed and improves access to job market information. Schoer and Leibbrandt (2006) argue that their data suggest that household employment provides access to financial resources which unemployed household members use to pursue active search methods, but that when unemployed individuals are constrained in their ability to engage in active search due to domestic duties, other employed individuals in the household then act as transmitters of information.

Recognising that most studies of network effects suffer from omitted variable bias, Bertrand et al. (2000) devise an estimation strategy to try to minimise these biases in their work examining the impact of social networks on the take up of welfare grants in the USA. They use language groups to proxy for social networks, arguing that information flows more easily between those who speak the same language, and include language fixed effects as well as geographic area fixed effects to minimise problems arising from omitted variable bias. They find that networks may increase the responsiveness of welfare use to policy shocks by an additional 15–27%. Our empirical work draws directly on their approach, but we differ in that we use age–language⁴ cohorts to define the social network, and we focus on the impact of social networks on labour market status. We include age–language cohort fixed effects, as well as geographic area fixed effects in order to minimise potential biases that might arise from omitted variable bias. Our network estimates, while small are not insubstantial, and suggest that social networks alone may enhance employment probabilities by an additional 3–12%. In contrast, the impact of social networks on reducing worker discouragement is much smaller, at between 1 and 2%.

³ Some correlations that are noted in the study based on the non-parametric techniques include: (1) if a spouse is employed then the partner will more likely be employed too, (2) search patterns of parents are transmitted to their children.

⁴ Bertrand et al. (2000) define the network on the basis of language only. We combine age and language, so that individuals who speak language X (e.g. English) and are in a common age cohort Y (e.g. age 15–24 years) are considered to be part of the same social network.

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