

SECOND CARNEGIE INQUIRY INTO POVERTY  
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Recruitment and wage determination  
procedures of manufacturing firms  
in the Eastern Cape: Implications  
for unemployment

by

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RECRUITMENT AND WAGE DETERMINATION PROCEDURES OF  
MANUFACTURING FIRMS IN THE EASTERN CAPE:  
IMPLICATIONS FOR UNEMPLOYMENT

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This paper sets out to examine how a recently developed alternative approach to the labour market, in opposition to conventional theory, attempts to explain the existence of barriers to mobility in the labour market, and the consequent failure of these markets to clear. In focusing on the demand side of the market it will be postulated that the recruitment methods and wage determination procedures of a sample of manufacturing firms in the Eastern Cape contribute to the formation of internal labour market structures which contribute to the persistence of low wages, poverty and unemployment.

**Introduction**

In the basic neo-classical theory of the labour market an efficient allocation of resources requires that labour supply decisions on hours, participation and mobility are made on the basis of relative prices by rational, utility - maximizing individuals. Labour demand reflects the outcome of cost-minimizing decisions by firms in response to relative factor prices. An efficient allocation is only achieved if wages equal Marginal Revenue Product and there is no excess supply or demand for labour in any single market, or in the labour market as a whole. A central element of this theory is the assumption that labour markets are sufficiently competitive to incorporate the adjustment mechanisms of prices in the short run and quantities in the long run.

Recent developments in neo-classical theory have attempted to explain sluggish adjustments and the existence of earnings differentials in labour markets. However, as Solow notes, these markets continue to be characterized by high levels of unemployment, discrimination and poverty. The pervasive and long-term nature of these phenomena make it increasingly difficult to treat them as mere aberrations and imperfections. Alternatively, it is perhaps more useful to turn to "an important current in economics that focuses on flaws in the price system, the way that real markets fail because they lack the characteristics that make idealized markets so attractive." (Solow, 1980: 10)

There are many candidate hypotheses that attempt to explain why the labour

market often fails to clear. Some of these fall under the general rubric of labour market segmentation theories which have developed in opposition to the competitive theory of the labour market and contain within them a number of divergent approaches. Before briefly examining some relevant facets of these theories it is firstly important to recognize that most labour markets, and the South African version in particular, display varying levels of segmentation.

In examining the South African labour market it is useful to distinguish between 'pre-market segmentation' and 'in-market segmentation,' since it is upon the relative importance of these two variants that the dispute between the segmentationist and orthodox approaches hinges. The former, which is closely related to social stratification can be defined as "the differentiation of opportunities to enhance one's productive potential through schooling, formal training etc." (Ryan, 1981: 4) Pre-market segmentation invokes the notion of non-competing groups, where the origins of inequality are exogenous to the labour market, and, on the whole, is accepted by economists of differing persuasions. Proponents recognize that labour is not a homogeneous factor of production and that the labour market is segmented in terms of ability, experience and skill. Workers have ties to localities, industries, special job classifications, even individual employers and the fact that competition is rarely direct - in the sense that if X is willing to do Y's job for a lower wage than Y the employer will discharge Y and hire X - certainly allows segmentation to flourish.

In-market segmentation, on the other hand, refers to the subsequent differentiation of opportunities to increase to price of one's rental" (Ryan : 5), and represents the continuation of pre-market inequalities into the labour market itself. The orthodox school argues that "in its competitive formulation, the market does no more than produce at the end of the period a reflection of the circumstances of market participants at the beginning of the period." (Ryan : 6) Thus, the market cannot be blamed for inequality and low pay since it merely replicates the inequality that it inherited, without being, in any way, party to its creation. Internal segmentation theory denies the market such neutrality of status by crediting it with an active role in the generation of inequality, low wages and unemployment.

The major contribution of internal segmentation theory is to examine the effect of internal labour markets. Built upon the notion of labour as a quasi-fixed rather than a variable factor of production (Oi, 1962), the theory attempts to explain how firms insulate themselves from the competitive external labour market by

fostering a set of administrative rules and procedures that govern the pricing and allocation of labour (Doeringer and Piore, 1971). Internal labour markets are said to develop because workers' skills are becoming less general and more firm-specific thereby necessitating a more stable labour force. To this end employers will induce stability by paying workers more than their opportunity wage in the external labour market and by creating employment conditions which contribute to increased job security. The attendant restriction of mobility will diminish the influence of the market on the internal wage structure of the firm which will be increasingly influenced by custom and institutional rules.

According to this theory, such employment conditions will only pertain to sectors and jobs with the required technological characteristics. Those sectors and jobs characterized by labour-intensive technologies and a lack of market power where incentives to stability are less necessary will experience the low wages and insecurity of employment consistent with a competitive, secondary labour market.

This institutional model has been extended by Gordon (1972) and Edwards (1979). They incorporate the ILM approach into a materialist framework by assigning a more central role to the notion of control. Building on the requirements of labour force stability they emphasize the need of capitalists' to control labour as an important determinant of stratification. Accordingly a tripartite model of segmentation is constructed in order to explain the differing forms of control in each segment.

Thus, within this broad framework it is incorrect to assume that all firms are 'price-takers', passively adopting the changing conditions in technology and the labour market. It is rather more useful to see management as an active process continually attempting to re-define its relationship with both the external market and their own labour forces. Central to this process is the pursuance of employment policies which aim to secure and maintain the cooperation of workers.

In applying segmentation theory to the South African labour market it is useful to formulate a model of racial dualism postulating "a 'White' sector and a 'Black' sector which are the results of a historical process of segmentation of the labour market, in which the distribution of individual jobs and income have become dominated by the superficial characteristic of race" (Cassim 1982a: 11) The duality is evidenced by a glaring disparity between whites and blacks in terms of wages, occupational levels, labour force participation and access to training and educational institutions.

One facet of this racial division of labour is clearly indicated in the following table, the outstanding feature of which is the predominance of whites in the managerial and white-collar occupations and the over-representation of Africans at the semi-skilled and skilled levels.

**Table 1 : The Occupational Distribution of Different Racial Groups, 1979**

Occupational Category	Percentage of Race Group			
	African	Asian	Coloured	White
Professional & Technical	23	3,5	10,0	63,5
Managerial & Executive	2	2	1	95
Clerical	14,7	7,5	8,3	69,4
Sales	24,4	8,8	10,6	56
Production Workers	69,8	4	12,1	14,0
Unskilled	85,1	1,2	12,5	0,5

Source: Department of Labour Manpower Survey 1979. (Presented in Cassim, 1982a: 14).

This table alone suggests that South Africa has two distinct labour markets, one for white labour and one for black labour - distinct in the sense that each is regulated by different laws and institutions, "enhanced by barriers in other areas of society such as housing, education and transport which react and affect an individual's labour market position". (Cassim 1982a: 12)

Against this background it is clear that the South African labour market is moulded by a range of forces that have stratified the labour force into two, or perhaps three, differentiated segments. This is neither a recent, nor a startling observation, but a useful point of departure. The crucial question is whether this pre-market segmentation is merely reproduced, as suggested by the orthodox economists, or whether the process of stratification is continued and augmented within the labour market itself.

In an attempt to throw some light on this question this paper will examine the recruitment procedures, internal wage structures and labour management methods of a sample of manufacturing industries in the Eastern Cape. It will be argued that the behaviour and strategies pursued by a majority of larger firms limits the competition espoused by the conventional model of the labour market by producing various levels of closure through the operation of less-than-neutral internal labour markets.

### **Methodology**

The empirical data in this paper is based on an on-going survey of 43 manufacturing firms in the Port Elizabeth and East London metropolitan areas. These firms represent the first batch of a large sample of firms drawn from all sectors of employment in the survey area. Selection was accomplished by stratifying the universe of firms according to size and then selecting on a random basis.

The survey was conducted with the use of a semi-structured questionnaire which was administered to personnel managers by experienced interviewers.

Unfortunately, these 43 firms are not representative of the defined universe. They constitute mainly the large and medium-sized firms in the survey area with smaller firms strongly under-represented. However, this does not impair the results since the employment factors on which the paper focuses are largely consistent with the theoretically predicted behaviour of larger firms. The inclusion of smaller firms is expected to enrich the results by providing a comparative perspective. In addition, it is intended to complete a few case-studies of selected firms once the general sample has been completed.

### **Recruitment Methods**

In the conventional, neo-classical model of the labour market an efficient allocation of resources is, amongst other things, predicated upon adequate channels of information between buyer and seller. The labour market is no exception to this rule in that easy access to information is required if the market is to clear. If information on job vacancies, wage levels and employment conditions is efficiently disseminated the model predicts a reduction in frictional unemployment and the costs of search incurred by the employee, and lower recruitment and screening costs for the employer.

However, if information to employment seekers is limited in any way, thereby introducing a rigidity to the system, the ability of the labour market to clear is likely to be frustrated. This could have severe implications for those seeking employment, since it follows that the more imperfect the knowledge of potential employees regarding the number and nature of vacancies, the more limited will be their access to opportunities in the job market. Thus, it is important to ascertain how information on job vacancies is communicated in the market.

To this end it is useful to divide information networks in the labour market into two groups: formal and informal. The formal networks include state employment agencies, private fee-charging employment agencies and newspaper advertisements. The informal methods include internal notice boards, word-of-mouth recommendations and casual calling. (Rees: 559)

**Table 2 : Recruitment Procedures x Percentage of Firms Surveyed**

	% unskilled	% semi-skilled	% skilled
Labour Bureau	9.3	11.63	2.32
Farm/friend network	79.06	69.77	13.95
Queuing	60.46	41.86	11.63
Word of mouth	74.42	72.1	11.63
Newspaper advertisements	-	20.93	79.06
Private employment agencies	9.3	9.3	25.6

The columns for each occupational category do not add up to 100 since each respondent was allowed to identify 3 recruitment methods per occupational category. In practice not all respondents actually utilize 3 methods per category.

In reference to the survey area the previous table, Table 2, indicates a marked differential use of recruitment methods across occupational levels with a strong emphasis on formal methods at the skilled level. This is largely explained by the relative shortage of skilled labour in the regional economy which often forces firms to recruit beyond the boundaries of the local labour market area. On the other hand, the unskilled and semi-skilled levels are dominated by informal methods of recruitment. (However comparisons between occupational levels should be treated with some caution, since such comparisons are likely to reflect variations in propensity to notify vacancies in the external market. (Jenkins et.al, 1983:263))



One of the most striking features to emerge from this piece of research is the current importance of the internal labour market (ILM) as a recruitment arena. This indicates the fact that firms frequently recruit to jobs from within their own ranks, through the use of internal notice boards etc.

Eighty-eight percent of all firms interviewed indicated that they prefer the ILM as opposed to external methods as a means of filling vacancies. The survey found, as indicated in the following table, that a large proportion of vacancies, especially among the semi-skilled, skilled and supervisory occupations, are actually filled internally.

**Table 3 : Percentage of Vacancies Filled Internally x Occupational Level**

% Vacancies/% Firms	Semi-skilled	Skilled	Supervisor	Clerical	Managerial
0-25	10	24	14	27	37
26-50	14	17	7	32	24
51-74	2	14	19	10	10
75-100	74	45	60	30	29

This is unambiguous evidence that employers are using their internal labour markets more extensively than the accepted formal methods as a primary source of recruits. Unfortunately the firms were unable to quantitatively differentiate between the various ILM procedures used but the evidence in table 3 indicates that word-of-mouth recruitment is very popular. "In as much as word-of-mouth recruitment frequently involves the communication of nominally internal vacancies to the friends and relatives of the existing workforce, it can, perhaps, best be viewed as an extension of the ILM into the wider market". (Jenkins et.al: 263)

Why is there a significant reliance on internal recruitment? Seventy four percent of firms cited low screening costs as a major reason while 84% emphasized the familiarity of existing employees with their job tasks and with the firm's work and personnel procedures. This evidence squares with the contention that the internal market is cheaper than many other channels of recruitment. In addition it helps to promote peaceful industrial relations by recognizing the workers' need for job security.

Despite the plausibility of this quantitative data the interviews reveal deeper underlying reasons for the use of these recruitment strategies (Jenkins et.al : 264) The most important of these is the firms' desire to recruit or retain employees

that, in addition to the appropriate skills, exhibit more 'acceptable' personal characteristics, such as stability and reliability. As one personnel manager put it, "Better the devil you know. The one you don't (know) may have the skill but might also have a disruptive influence on the factory floor." This view is substantiated by well over 50% of the firms that identified 'reliability' and 'obedience' as among the more important criteria in selecting an employee for promotion or training. Most personnel managers agreed that internal candidates, because of the continuous screening process, are much easier to evaluate with respect to 'reliability', 'obedience' and 'suitability'. Some also admitted that the satisfaction of these criteria may often result in competitive pressures being ignored.

The high incidence of word-of-mouth recruitment reveals the strategy of personnel departments to extend this screening process into the external labour market. Besides helping to reduce the uncertainty in the search process this particular channel provides a privileged source of information about potential candidates and, most crucially, involves the existing workforce in the recruitment and screening process. This introduces the second underlying reason for the increased use of informal recruitment methods: the fact that the process partially transfers the responsibility for discipline and control from line management to the workers themselves, thereby coopting them into the managerial process. Thus, informal recruitment procedures operate as a quid pro quo control strategy for management whereby the labour force have a hand in the recruitment process in return for a degree of shop-floor cooperation. More than one personnel manager admitted that this was an explicit managerial strategy which operated with great effectiveness.

The pervasion of such recruitment procedures, as suggested by Jenkins et. al. (266) could have severe implications for some groups of job-seekers especially women, youths and blacks. It is likely that these groups will find themselves increasingly marginalized in a hostile buyer's labour market. In particular, those job-seekers with limited access to the informal information networks of the market and to training and educational institutions will be at an even more acute disadvantage.

#### **Wage Determination and Labour Management Procedures**

Whether in practice the labour market embodies sufficient flexibility to promote pay equalisation is a central issue in the judging of alternative theories of the pay structure. The theory of internal labour markets, briefly outlined in the Introduction, rejects the assumption of competitive labour markets and the import of

individual productivity characteristics. Instead, they shift the focus onto the structural and institutional processes which generate stable pay inequalities and the internalization of wage determination and management procedures.

The survey shows that 93% of firms interviewed reflected either 'very stable' or 'relatively stable' internal wage structures over the past few years. This stability is adequately explained by the large number of firms that only make 'across-the-board' wage changes leading to the long-term stability of wage differentials. The more pronounced the tendency of plant wage structures to move bodily upwards through time the more rigid and inflexible these structures are likely to become. In part, this will reflect the strengthening of equitable comparisons within the plant and the entrenchment of 'notions of fairness' in the whole employment relationship. This trend has obvious implications for conventional theory since it points to the failure of the internal wage structure to respond to external labour market conditions.

Despite the fact the the sample mainly consists of the larger firms in the survey area it is worth noting that this tendency was less evident among those smaller firms interviewed. A number of these firms admitted flexible internal pay structures indicating greater managerial emphasis on individual productivities. This behaviour is to be expected of firms with little product market power leaving them more vulnerable to changes in the external market. It is also worth noting that some of the larger firms, especially those in the low-paying textile and wood products sectors, only reflect stable internal wage structures because their occupational wage levels are so closely tied to Industrial Council minimum wage determinations. In most of these industries internal wage stability is determined by competitive product market conditions and the relative weakness of worker organization rather than by the strength of institutional processes within the firm. The relative strength of these forces means that segmentation is likely to vary across industries.

The survey also shows that 95% of the firms interviewed have a formal policy to re-engage retrenched workers. This policy is often formalized in the form of union agreements, particularly in those firms that have signed recognition agreements with the independent unions. However, when asked to single out the most important reason for pursuing this policy, 47% of the firms identified job-specificity and the cost of retraining new recruits in these specific tasks.

**Table 4 : Transferability of Skills Within Skill Category**

	<u>x Occupational Category</u>			
	Very trans. %	trans. %	Not very trans. %	Not trans. %
Unskilled	42	28	16	14
Semi-skilled	26	33	30	11
Skilled	28	33	16	23
Clerical	40	35	9	11

**Table 5 : Transferability of Skills to Other Firms**

	<u>x Occupational Category</u>				
	Very Useful %	Useful %	Some Use %	Useless %	Very Useless%
Unskilled	28	23	23	26	-
Semi-skilled	23	23	26	28	-
Skilled	51	12	19	19	-
Clerical	56	26	5	5	2

Table 3 and 4 show that a significant proportion of skills are specific to either certain jobs or industries and consequently not easily transferable across occupations or industries. This is largely consistent with the thesis that the manufacturing sector is experiencing a progressive decline in the importance of general skills. This increase in specific skills is reflected in Table 6 which clearly shows that on-the-job training is quite the most important method of imparting production skills. The implication of this form of training is that the more peculiar it is to individual firms and manufacturing sectors the more closely the workers are tied to the firm and the greater the consequent stability of the workforce.

**Table 6 : Preferred Training/Education Methods**

	<u>x Occupational Category</u>		
	Skilled %	Semi-skilled %	Unskilled %
Schooling	7	5	2
On-the-job training	63	91	91
Internal training	12	5	7
External training	19	-	-

However, at the same time as imposing a constraint on worker mobility this increase places a complementary constraint on the ability of employers to seek out the cheapest labour. The lower elasticities of substitution of these skill-specific categories of labour increases their bargaining power since it is more costly for firms to replace these categories. It is the development of such situations of segmentation which lead Edwards, on the one hand, to explain the existence of control mechanisms within the firm and, Doeringer and Piore, on the other, to predict the evolution of customary procedures, and institutional rules which shield the incumbents of the firm from external market forces.

The next step then is to consider the response of worker organisation to the development of internal labour market structures. According to Rubery, the aforementioned alternative approaches to the labour market lack general applicability because of "the almost exclusive attention paid to the actions and motivations of capitalists in developing a structured labour market, and the consequent neglect of the role of worker organisation in the process" (Rubery, 1978: 18) On this basis it is argued that trade unions will respond to changes in the distribution of employment, the nature of skills and the composition of the labour force by organising to protect itself against new competition. This is not necessarily inconsistent with Edwards since he associates the expression of technical control with the subordinate primary market, the fundamental distinguishing criterion of which is the presence of unions (Edwards, 1979 : 171) Correspondingly the logical home of the institutional rules and customary procedures, postulated by Doeringer and Piore, is surely rooted in a system of collective bargaining.

The survey shows that 54% of all firms determine wages and employment conditions by collective bargaining; 33% use managerial discretion only with the remaining 13% using a combination of both methods but leaving the final decision in the hands of the manager.

The table below illustrates the nature of union representation in those firms paying higher-than-average occupational wages. The evidence supports the contention that the independent unions dominate the high-wage manufacturing industries. There are 2 principal reasons for this trend. Firstly, the majority of the high-wage firms comprise the larger firms in the survey area. It is these firms that have the flexibility and market power to accommodate and negotiate with the powerful, well-organized independent unions. Secondly, these firms are characterized by large, principally semi-skilled labour forces which encourage the propagation of collective behaviour.

Table 7 : Worker Organization in high-wage firms

	%
Independent union	63
Liaison/works comm.	23
TUCSA union	10
No representation	4

Over 80% of the firms with independent unions fill considerably more than half their vacancies from within the firm. Only 50% of firms with other forms of worker organization fill half of their vacancies internally. This, too, indicates that those firms with well-organized unions on the shop-floor reflect a relatively higher degree of labour stability than those with weaker worker organizations and less product market power.

Against this backdrop it must be assessed whether trade unions in South Africa, given their primary concern under competition to obtain job security and higher wages, are acting "to the exclusion and possible detriment of those remaining in the unorganized sector", as Rubery (1978: 34) suggests is the case in the UK. There are however crucial differences between the UK and South African union situations.

Firstly, the union movement in the UK has developed out of a different set of historical circumstances, which has seen the development of machine technology increase the proportion of the labour force directly involved in the mechanised production process. This has caused a partial undermining of the skilled unions' basis for organization and control precipitating defensive action of the part of these unions. The independent union movement in South Africa, on the other hand, fledgling in comparison with its UK counterparts, has not emerged out of a system of craft control, but rather out of a system of severe political repression and, has survived primarily because of the close contact of the leadership with rank-and-file membership and the encouragement of democratic processes on the shop-floor.

Secondly, the unemployed and marginalized sectors in the UK are largely catered for by the mechanisms of a developed welfare state. In South Africa the urban unemployed have scant access to any state welfare funds that might help to alleviate their plight. The burden of these provisions is displaced instead onto the shoulders and pay packets of the employed blacks. This assertion is borne out by

the evidence of Gilmour and Roux (1984), whose household survey in the same labour market area as this industrial survey, shows a dependency rate of 1:4. The crucial implication of this dependency rate is that while employed blacks live in close contact with the mass of urban unemployed, they are also the benefactors of their sustenance and welfare. The efficacy of this argument rests on the assumption that at least one member of most African households is gainfully employed in the formal sector. If the assumption holds, and Gilmour and Roux's data seems to bear it out, then a significant proportion of formal sector pay is being redistributed among the unemployed.

Thus, while there is no denying the inevitable tension between wages and employment in a capitalist economy these two aforementioned factors render it difficult to sustain Rubery's argument in present-day South Africa. The unemployment problem certainly does pose problems for organized labour but this potential source of stratification is surely offset by the empirically proven dependency relationship of union members with the mass of unemployed. In addition, the independent union movement is playing a pivotal, organizational role in the campaign for democratic rights and, in order to survive, must be geared to the demands of its members - even if this means more wage and stability demands.

### Conclusion

This article has documented some of the processes in the Eastern Cape labour market which contribute to the failure of markets to clear. It is argued that the increasing use of informal information networks, in particular, the current importance of the internal labour market as a recruitment arena indicate that fewer jobs are coming onto the open market with the result that some firms are becoming less involved in the external market place for labour. The empirical data concerning wage determination shows that the majority of larger firms in the survey area reflect stable internal wage structures over time contributing in turn to the stabilization of labour forces. It is also evident that general production skills are increasingly being replaced by firm - and industry-specific skills reflected by the high incidence of on-the-job training, further promoting labour stabilization. This trend is particularly apparent among those firms with above average product market power, facing well-organized trade unions on the shop-floor.

Taken together, the factors outlined have a number of consequences. Firstly, the increasing incidence of labour stabilization and specific skills seem to provide

suitable working conditions for the generation of institutional rules, customary procedures and control mechanisms which contribute to the partial insulation of the firm from the external labour market. Secondly, as these forces entrench themselves over time the labour market can be expected to display deepening levels of segmentation and more powerful barriers to mobility between the high-wage, capital-intensive sector, the more competitive, low-wage sector and, the unemployed sector. It is likely that the participation of large numbers of potential employees, especially disadvantaged groups comprising blacks, youths and women will be severely curtailed as the relative strengths of competitive and stratifying forces vary across time and place. For many this marginalisation will bring protracted confinement to low-paid, routine, menial jobs and, for others the spectre of enduring unemployment.

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