Abstract

The present paper aims at ascertaining the validity of the recurrent argument that wage moderation is necessary to secure jobs and economic growth in Mozambique. The hypothesis is empirically tested through an OLS regression of an aggregate labour demand model, relying upon time-series data covering a span of 28 years (1992-2019).

The paper found that the wage moderation strategy that has been pursued (which kept real wage growth at an average of 0.04%), is consistent with the profit-led growth regime of the economy and although it hasn’t led to reductions in unemployment, it has been effective at preserving a stable [albeit low] level of employment, considering the context of a consistently high labour force participation ratio.

Therefore, as the cost-of-living crisis heightens the pressure for higher wages, the evidence from this study consubstantiates the arguments for continued wage moderation, as it proves that wage hikes above inflation-adjusting will be ineffective at addressing the cost-of-living crisis and if anything, they will only lead to a higher inflation, a worsening current account deficit and ultimately a further deterioration of unemployment levels. Thus, the study goes on to recommend a priority focus of policy-makers towards higher levels of employment, through reforms aimed at enhancing the productivity and competitiveness of the economy, starting from stanching its porosity and stimulating the productive reinvestment of profits within the country.

Key-words: wage moderation; labour demand

Resumo

O presente artigo visa apurar a validade do recorrente argumento de que a moderação salarial é necessária para garantir o emprego e o crescimento econômico em Moçambique. A hipótese é testada empiricamente por meio de uma regressão pelo método dos MQOs, de um modelo de procura agregada por trabalho, com base em dados em séries temporais cobrindo um período de 28 anos (1992-2019).

Este estudo constatou que a estratégia de moderação salarial que vem sendo seguida (a qual manteve o crescimento real dos salários em uma média de 0,04%), é consistente com uma economia cujo regime de crescimento está ancorado aos lucros e, embora ela não tenha levado à uma redução do desemprego, esta estratégia tem sido capaz de assegurar a preservação de um nível de emprego estável [embora baixo], considerando o contexto de uma taxa de participação da força de trabalho consistentemente alta.

Assim, na actual conjuntura em que a crise do custo de vida aumenta a pressão por salários mais altos, as evidências deste estudo fundamentam o argumento em favor da moderação salarial, demonstrando que aumentos salariais acima do ajustamento inflacionário, não poderão resolver o problema do custo de vida e antes pelo contrário, poderão gerar uma inflação mais elevada, um agravamento do défice da conta corrente e, em última instância, deteriorar ainda mais os níveis de desemprego. Assim, o estudo recomenda um enfoque prioritário dos decisores políticos na promoção de níveis mais elevados de emprego, através de reformas que visem reforçar a produtividade e competitividade da economia, começando por estancar a sua porosidade e estimular o reinvestimento produtivo dos lucros dentro do país.

Palavras-chave: moderação salarial; procura por trabalho
1. Introduction

Following the end of the civil war in 1992, the Mozambican economy experienced a rapid expansion, with real GDP growth rates averaging 7.2% until 2019, well above the 3.7% average for the Sub-Saharan African region. In the meantime though, real wages almost stagnated, having grown at a yearly average rate of roughly 0.04%, which suggests that wage adjustments throughout this period were just enough to compensate for inflation and thereby brought no significant improvements to workers’ real balances and living standards. In line with the real wage stagnation trend, GDP by factor income, show that the share of wages has remained at a relatively low average of 25%, whilst profits have consistently accounted for 65% in average.

Business and policymakers have argued that a moderate real wage growth is a sacrifice that has to be endured in order secure the existing jobs and enable the investment on the productive capacity that will, in the medium to long run, create the much-needed new jobs. But, the idea that a drop in real wages will in the end be necessarily accompanied by an increase in employment is rooted in a set of neoclassic self-equilibrating market properties that aren’t always consistent with the workings of a modern capitalist economy (McCombie, 1986). Thus, as unemployment rates in Mozambique have persistently hovered above 20%, it begs questioning if the strategy of wage moderation will ever bear the fruits that have been promised.

Therefore, the objective of this paper is to ascertain through empirical verification whether wage moderation may lead to increases in labour demand (i.e., reduction in unemployment rates). The point is that if real wages are stagnated, one would assume that aggregate demand management is [implicitly] anchored on a profit-led growth strategy. But if we can prove that stagnant wages will not necessarily lead to less unemployment, then the inherent inability of the profit-led strategy to spur aggregate demand and sustainable growth will have been put to bare. Such a conclusion would prop up the case for sweeping wage rises, which seems to have recently gained momentum in the current context of soaring inflation and pay reforms in the public sector. On the other hand though, if the current real wage path is proved consistent with greater economic capacity utilization (including higher levels of employment), then, this paper will crucially beef up the case for continued wage moderation.

In both cases, the far-reaching implications of the present analysis for economic policy prioritization cannot be understated as the country grapples with a simultaneous and dilemma cost-of-living and unemployment crisis in the aftermath of the successive shocks of the Covid-19 pandemic and the ongoing Russian-Ukrainian war.
2. Literature Review

2.1. Theoretical and Empirical Literature

Economic literature has extensively explored the bi-directional nature of the relationship between unemployment and real wages. A classic positive causality, which lies outside the focus of this paper, runs from unemployment to real wages and assumes that a high unemployment rate (i.e., surplus labour) weakens unions’ bargaining power and hence lowers wages (Wakeford, 2003). A post-Keynesian tradition of thought explores the reversal of that causality holding that, real wages do determine the level of unemployment in so far as, profit-maximizing capitalist firms will, by means of factor substitution, adjust their demand and costs on labour, for as much as necessary to preserve its required levels of profits (Bhaduri and Marglin, 1990).

To justify the reversal of the classic causality between real wages and employment, Keynes contended that aggregate demand and employment are co-determined by the propensity to consume [which is a function of income, wages included] and by the rate of new investment [which is a function of expected profits or the marginal efficiency of capital] (Hagemann, 2019). The underlying implication of this formulation is that the factor income distribution between employers and workers holds a significant relevance in determining the levels of aggregate demand and employment.

With that being the case, a higher income share for workers (i.e., a real wage rise), would stimulate consumption but on the flip side, the corresponding squeeze in the income share for capitalists (the profits), would act as disincentive to investment. That means that the net [aggregate] effect on GDP and employment of any change in the income distribution, becomes an empirical matter since it will specifically depend on the relative magnitude of the resulting reactions on each of the above referred components of aggregate demand [i.e., consumption, investment and net exports the latter of which due to expected exchange rate movements in response to domestic price/wage changes] (Bhaduri and Marglin, 1990; Onaran and Galanis, 2012).

Fortunately, the comprehensive cross-country evidence already available (Janssen, 2008; Blecker, 2016; Onaran and Galanis, 2012; Oyvat et al., 2020; De Oliveira and Souza, 2021), draws a pattern of robust empirical regularities that has allowed for the establishment of some key 'stylized facts'1:

i. In countries that are characterized by a larger wage share of income relative to the profit share and low wage inequality, for any given change in real wages, consumption will typically react much more strongly and quickly than investment (i.e., the income elasticity of consumption is greater than the profit elasticity of investment). For these group of countries, in which the most advanced mass-consumption economies are comprised, growth is said to be wage-led and therefore a wage moderation strategy is most likely to seriously depress consumption at such

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1 Given the very poor coverage of the studies on developing countries and particularly on Sub-Saharan Africa (South Africa excluded), the actual behaviour of some these economies might diverge (to a lesser or greater degree) from the ‘stylized’ mean because the underpinning models probably did not fully account for the structural specificities of this region, the most critical of which being the nature and scale (relative to recipient economies) of Foreign Direct Investment (FDI).
a magnitude that will not be offset by the expected increase in investment so that the end result will be a rise in unemployment levels.

ii. In countries that are characterized by a lower wage share of income relative to the profit share, a high level of economic openness, a large private credit-to-GDP ratio and a significant income inequality, any given change in the income distribution is likely to trigger a much stronger and quicker response on investment rather than on consumption (i.e., the profit elasticity of investment outweighs the income elasticity of consumption). For this group of countries that comprises mostly emerging and developing small open economies, growth is said to be profit-led and hence, wage moderation is expected to have a positive effect on capital accumulation, which will in turn expand capacity utilization and ultimately lead to higher levels employment.

For this latter group of countries, most of which had undergone profound structural transformations in the course of the post-1980s’ neoliberal reforms, wage moderation has become a *sine qua non* condition for growth. Wage moderation consists in restraining the growth in average wages below growth in productivity (Disoska and Trpcevska, 2016). In practical terms, wage moderation is the policy of keeping workers' wages at a slow pace of growth, sometimes just slightly above the pace of inflation (Hartman, 2017).

However, whilst the predominantly profit-led growth regime of developing economies is quite an established fact, empirical research on the subject has been so scant (if any) for this group of countries, that our research could not find any specific estimation of the quantitative parameters of the wage-employment relationship for these economies, let alone for Sub-Saharan Africa.

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2 For the Euro Zone, it is estimated that a simultaneous decline of 1% point in the wage share in all countries would lead to a decline of EU GDP by 0.30%. A different study estimated that the decline in EU GDP could actually be of 0.36% (Disoska and Trpcevska, 2016).
2.2. Trends in Productivity, Wages and Employment in Mozambique

For the most part of the past 3 decades, Mozambique was one of the fastest growing economies in Africa, as its real GDP rose by an average rate of 7.2% a year. Yet, despite the increase in average productivity (output per worker) which jumped from MZN 10 955 in 1992 to MZN 37 305 in 2019 (at constant 2014 prices), real wages almost froze as the nominal adjustments grappled to keep up with inflation. In the end, real wages rose annually by a mere 0.04% in average. This widening wedge between the average wage and the average output per worker is largely a reflection of the increasingly capital-intensive growth pattern, driven by an extractive sector with poor linkages with the rest of the economy.

Graph 1: Real wage-productivity gap (in MZN)

Graph 2: Real wage growth-Inflation differential (in %)

The fact that the somewhat steep path of the average productivity curve was largely sustained by the dynamism of a few ‘outlier sectors’ (extractive/mining industry and services) rather than broadly distributed improvements in productivity (Jones and Tarp, 2015; Lachler and Walker, 2018), may explain why the average real wage curve has nonetheless threaded relatively flat throughout the period, as shown on graph 1.

However, perspectives on why the performance of the more traditional sectors of the economy has lagged behind are not quite corroborating. Lachler and Walker (2018) argue that productivity gaps in agriculture and manufacturing (i.e., non-extractive industry) result from a low and declining marginal productivity of new workers caused by an ever-shrinking capital-labour ratio in the face of shortages of investments. But Jones (2006) and Garzarelli and Liman (2019), hold that the problem lies somewhere else. After decomposing the GDP growth rates into its driving sources using the growth accounting approach, they concluded that the labour factor (L) adjusted to human capital, consistently accounted for less than 20% of the growth rates throughout different post-war sub-periods, whereas physical capital accumulation (K) and efficiency gains in the form of Total Factor Productivity (TFP) were the main determinants of growth in Mozambique.
This latter view, which suggests that the ever-slowing performance of the economy may be linked to poor labour productivity, has by and large prevailed and it has provided (to both employers and policymakers) with an understandably convenient rationale for the wage moderation stand. Wage moderation combined with a remarkably generous fiscal treatment towards the largest and most profitable businesses operating in the country (the FDI-funded ‘megaprojects’), were instrumental in shaping the pro-capital distributional pattern of the economy under which, profits have consistently accounted for over a third (65%) of the national income, whereas the wages’ share is stuck at just 25%, according to INE figures.

However, whilst the country’s GDP accounts to such a substantial level of profit income (a large of part of which generated by the FDI projects), only a much smaller fraction gets actually retained and reinvested within the country because the economy being highly porous, a large share of profits is lost to capital repatriation and illicit capital flight (Castel-Branco, 2015). Consequently, as the GDP consistently grew, the high porosity held back de economy from absorbing an important share of its internally produced surplus, ultimately undermining its ability to proportionally expand the capacity utilization. It is the no wonder then, that unemployment levels have not been responsive to the robust post-war GDP growth, as clearly depicted in graph 3.

Graph 3: Unemployment- GDP growth

Source: Author with data from INE.

It is nonetheless worth making a caveat to note that this relative rigidity of unemployment levels also raises the possibility that some of the post-war job expansion may have been offset by the increased Labour force participation rates which peaked at 86% in 2003 and consistently remained above 80% in average throughout the period, according to ILO and World Bank figures.

Now, in spite of its negligible contribution to employment, FDI\(^3\) has been such an important driver of the growth performance. Largely by account of the magnitude of its dependency on FDI, the growth pattern of the Mozambican economy, in line with the majority of similar developing small open economies, falls within the 'stylized' description of a profit-led regime.

\(^3\) Annual inflows of FDI amounted to the equivalent of 28% of GDP in average from 2000 up to 2019, the timespan for which data is available [Banco de Moçambique, Annual Balance of Payments Reports].
So one key takeaway from the analysis of growth dynamics in Mozambique, is that the failure of the economy to reduce the unemployment levels even in the context of robust GDP growth, has had more to do with institutional frailties rather than an inherent inadequacy of the profit-led growth regime.

3. Data and Empirical Methodology

The purpose of this paper is to test the hypothesis that, stagnant real wages may lead to an increased labour demand in the economy. The aim is to ascertain the validity of the recurrent argument that wage moderation is necessary to secure jobs and growth in Mozambique. The study relies upon time-series data covering a span of 28 years (1992-2019), sourced from official INE, World Bank and IMF databases, to estimate the wage elasticity of demand for labour (i.e., the sensitivity of employment to changes in the wage rates) using the standard Ordinary Least Squares (OLS) method.

As per the methodological proposal by Nguyen (2016), the specification of our aggregate Labour Demand model departs from a constant returns to scale Cobb-Douglas aggregate production function \[ Y = Z L^\alpha K^{1-\alpha} \], where:

\[
\begin{align*}
Y &= \text{Output (at current prices);} \\
K &= \text{capital stock;} \\
L &= \text{units of labour employed;} \\
z &= \text{level of technology or total factor productivity (TFP);} \\
\alpha \text{ and } 1 - \alpha &= \text{denote the factor share coefficients of } L \text{ and } K \text{ respectively.}
\end{align*}
\]

Under a Cobb-Douglas technology, competitive firms will optimize the utilization of labour and capital at such levels that the marginal product of labour equals the wage \((w)\) and the marginal product of capital equals its rent cost \((r)\). With \(w\) being the partial derivative of \(Y\) with respect \(L\) and \(r\) being the partial derivative of \(Y\) with respect to \(K\), a system of equations is formed and solved for a \(K\) solution through the simultaneous procedure. Once the \(K\) solution is used to replace \(K\) in the initial aggregate production function, a single equation [expressed in terms of output \((Y)\)] is obtained. Then follows an algebraic manoeuvring aimed isolating \(L\) on the left-hand side of the equation. Finally, the resulting labour demand equation is deliberately manipulated into the following double-log functional form (Nguyen, 2016):

\[
\ln L = \varphi_0 + \varphi_1 \ln w + \varphi_2 \ln Y + \varphi_3 \ln r
\]  
\hspace{1cm} \text{(Equation 1)}

where \(\varphi_1, \varphi_2\) and \(\varphi_3\) are defined as wage elasticity of labour demand, output elasticity of labour demand, and rent elasticity of labour demand respectively.

But this specification is not yet entirely satisfactory because the nominal output variable \((Y)\), blends together two important demand factors – the changes in physical output quantities (i.e., real output) and the changes in output prices. As a result, the variable that ought to reflect changes in output prices is still [at least explicitly] missing from the model. We obviously cannot do without expliciting this critical variable in the model because we know that changes in output prices are a powerful determinant of shifts in firms’ labour demand curve in so far as\(^4\):

\[ \text{https://web.mnstate.edu/stutes/Econ416/StudyGuide/Study08/ReviewS&D.htm} \]
– An increase in the price of the product raises the value of the marginal product of labour and therefore increases the demand for labour.
– A decrease in the price of the product lowers the value of the marginal product of labour and therefore decreases the demand for labour.

In order to address this critical issue and allow the model to reflect both changes in real output and changes in output prices as independent variables, we deflate the nominal output \((Y)\) using the GDP deflator. Thus, assuming that the output \((Y)\) in the Cobb-Douglas production function is expressed at current/nominal prices and bearing in mind that:

\[
\text{nominal output} = \text{real output} \times \text{GDP deflator} \iff Y_{cp} = Q \times P
\]

Then, we can proceed to rewriting equation (2) according to the product rule of logarithms, as follows:

\[
\ln L = \varphi_0 + \varphi_1 \ln w + \varphi_2 \ln (Q \times P) + \varphi_3 \ln r
\]

\[
\ln L = \varphi_0 + \varphi_1 \ln w + \varphi_2 [\ln Q + \ln P] + \varphi_3 \ln r
\]

\[
\ln L_t = \varphi_0 + \varphi_1 \ln w_t + \varphi_2 \ln Q_t + \varphi_3 \ln P_t + \varphi_4 \ln r_t + u_t \quad \text{(Equation 2)}
\]

where:
- \(L\) is the labour demand (measured by the total number of employed)
- \(w\) is the real wage (measured by average wage per worker at constant 2014 Meticais);
- \(Q\) is the real output (measured by GDP at constant 2014 Meticais);
- \(P\) is output price (expressed by the GDP price index also known as GDP deflator);
- \(r\) is the rent on capital (measured by capital expenditure at constant 2014 Meticais)\(^5\);
- \(\varphi_1\) is the wage elasticity of labour demand;
- \(\varphi_2\) is real output elasticity of labour demand;
- \(\varphi_3\) is the price elasticity of labour demand;
- \(\varphi_4\) is the rent elasticity of labour demand, and;
- \(u\) is the error term.

Equation (2) is the final specification of our model. Considering that we are working on an aggregate (rather than firm-level) labour demand model, the incorporation of the GDP deflator as a measure of output prices is fit for purpose because it allows our model to respond to movements in the prices in all goods and services produced in the country (including the export prices).

<table>
<thead>
<tr>
<th>Variables</th>
<th>Mean</th>
<th>Std. Deviat.</th>
<th>Minimum</th>
<th>Maximum</th>
</tr>
</thead>
<tbody>
<tr>
<td>labour demand (units number of employed)</td>
<td>14 024 818</td>
<td>2 475 461</td>
<td>9 555 577</td>
<td>18 114 254</td>
</tr>
<tr>
<td>average real wage per worker (unit Meticais 2014=1)</td>
<td>5 783</td>
<td>2 362</td>
<td>2 739</td>
<td>9 734</td>
</tr>
<tr>
<td>real output (million Meticais 2014=1)</td>
<td>344 246</td>
<td>187 420</td>
<td>104 680</td>
<td>675 762</td>
</tr>
<tr>
<td>output price (index 2014=1, base value=1)</td>
<td>.7023914</td>
<td>.3884761</td>
<td>.0634667</td>
<td>1.424496</td>
</tr>
<tr>
<td>rent on capital/capex (million Meticais 2014=1)</td>
<td>25 779</td>
<td>13 976</td>
<td>7 851</td>
<td>50 384</td>
</tr>
</tbody>
</table>

\(^5\) Unlike the wage bill, which is readily available as the share of labour in the GDP by factor income series, capex (capital expenditure) figures had to be estimated as 10% of gross profits, as per a general rule-of-thumb commonly used for purposes of estimation and forecasting.
4. Estimation Results and Discussion

Before regressing the model in equation (2), we test the time properties of its variables using the Augmented Dickey-Fuller (ADF) procedure. The results displayed on Table 1 indicate that, at a significance level of 5%, all the variables are stationary in their first differences [i.e., integrated of order one or I(1)].

Table 2: Outputs for Unit Root tests

<table>
<thead>
<tr>
<th>Variables</th>
<th>Dickey-Fuller statistic</th>
<th>Mackinnon p-value</th>
<th>Dickey-Fuller statistic</th>
<th>Mackinnon p-value</th>
</tr>
</thead>
<tbody>
<tr>
<td>lnL</td>
<td>-3.596</td>
<td>0.4628</td>
<td>-3.600</td>
<td>0.0229*</td>
</tr>
<tr>
<td>lnw</td>
<td>-3.596</td>
<td>0.4037</td>
<td>-3.600</td>
<td>0.0330*</td>
</tr>
<tr>
<td>lnQ</td>
<td>-3.596</td>
<td>1.0000</td>
<td>-3.600</td>
<td>0.0182*</td>
</tr>
<tr>
<td>lnP</td>
<td>-3.596</td>
<td>0.3760</td>
<td>-3.600</td>
<td>0.0075*</td>
</tr>
<tr>
<td>lnr</td>
<td>-3.596</td>
<td>1.0000</td>
<td>-3.600</td>
<td>0.0108*</td>
</tr>
</tbody>
</table>

Note: The unit root tests were ran with the inclusion of a trend. The asterisk * denotes the rejection of the null hypothesis for non-stationarity.

Then, we proceed to test for cointegration using the Engle-Granger method in order to determine the presence of a long-run equilibrium among the five I(1) variables. In the case the variables are found to be cointegrated, then they can be safely regressed to each other without the risk of generating a spurious result (Wooldridge, 2015).

Table 3: Output for Cointegration test

<table>
<thead>
<tr>
<th>Mackinnon critical values</th>
<th>egranger statistic</th>
<th>Decision*</th>
</tr>
</thead>
<tbody>
<tr>
<td>α = 1%</td>
<td>-5.830</td>
<td>non-cointegrated</td>
</tr>
<tr>
<td>α = 5%</td>
<td>-4.952</td>
<td></td>
</tr>
<tr>
<td>α = 10%</td>
<td>-4.535</td>
<td></td>
</tr>
</tbody>
</table>

* Decision Criterion: Null hypothesis of non-cointegration is rejected if the absolute value of the egranger statistic is greater than the absolute values of each of the Mackinnon critical values.

These results indicate that, under the current specification of equation (2), a linear regression of these variables is inviable. Now, given that all the variables turned out to be I(1), one single differencing will eliminate both the unit roots and the serial correlation whilst turning the variables stationary (Gujarati & Porter, 2011; Wooldridge, 2015), under the following transformation (with $\Delta$ being the difference operator):

$$
\Delta \ln L = \varphi_0 + \varphi_1 \Delta \ln w + \varphi_2 \Delta \ln Q + \varphi_3 \Delta \ln P + \varphi_4 \Delta \ln r + u_t
$$

(Equation 3)

Once we finally run this definitive specification at a 95% confidence interval, the following results are obtained:

Table 4: Output for Regression test

<table>
<thead>
<tr>
<th>Variables</th>
<th>Coefficient</th>
<th>Standard Error</th>
<th>t-statistic</th>
<th>p-values for t stats</th>
</tr>
</thead>
<tbody>
<tr>
<td>lnw</td>
<td>-5.239043</td>
<td>.1378923</td>
<td>-3.80</td>
<td>0.001</td>
</tr>
<tr>
<td>lnQ</td>
<td>1.549922</td>
<td>.5950534</td>
<td>2.60</td>
<td>0.018</td>
</tr>
<tr>
<td>lnP</td>
<td>-.8202028</td>
<td>.3099092</td>
<td>-2.65</td>
<td>0.016</td>
</tr>
<tr>
<td>lnr</td>
<td>-1.147077</td>
<td>.2981914</td>
<td>-3.85</td>
<td>0.001</td>
</tr>
<tr>
<td>constant</td>
<td>8.985713</td>
<td>3.178902</td>
<td>2.83</td>
<td>0.011</td>
</tr>
</tbody>
</table>

Number of Obs=28 $R^2 = 0.7088$ SSR=.880666275 F prob= 0.0001
The results of the regression test show that the estimated model for aggregate labour demand is robust and offers a substantial explanatory power in so far as it is capable of explaining 71% of fluctuations in employment/unemployment levels. All the estimated coefficients are statistically significant and the respective signals are consistent with economic theory.

With respect to the independent variable of interest \( w \), the regression output indicates that a 1% increase in real wages will *ceteris paribus*, lead to a rise in unemployment by half a percent (0.5%). Whilst the negative correlation between wages and labour demand was indeed expectable, it may seem somewhat startling to find the labour demand to be *inelastic* with respect to changes in the wage rate (i.e., a rise in wages leads to a smaller contraction in employment levels), given the rampant precarity of job contracts in Mozambique. The inelasticity of labour demand to with respect to wages suggests, somewhat obviously that, in order to deflect the burden of a wage hike, firms do not solely respond through job-cuts – part of the burden passed-through to output/consumer prices.

The signal of the price coefficient, is one particularly salient feature of our regression. In theory, either signal would fit on the price coefficient but each for different reasons and with different implications:

- A positive correlation between output prices and labour demand would mean that the impulse for the output price movements is mainly triggered by changes in demand, to which firms would respond by hiring more staff (if demand and prices increased) or laying-off staff (if demand and prices fell);

- A negative correlation between output prices and labour demand would mean that output price movements are mainly driven by shifts in the production costs incurred by the firms. In this case, as output prices rise, demand does not necessarily adjust (at least not at the same pace and magnitude) and as result, firms are forced to lay-off staff.

The latter is indeed our case because, due to the large import dependence of the economy, variations in domestic prices in Mozambique are known to be widely associated with changes in ‘production’ costs mostly in the form of imported final and intermediate goods. Our regression results show that when output prices are prompted to rise by 1% (reflecting a passthrough of higher production costs), aggregate labour demand contracts by 0.8%. Therefore, the passthrough from higher wages to prices carries significant policy implications because it definitively confirms the inefficacy of wage rises for tackling both the cost-of-living crisis and the unemployment crisis – if wages (being a production cost) rise, output prices will necessarily follow suit and unemployment will worsen. In the end, the much-aspired wage rise proves elusive and sour.

Now, all else being equal [i.e., assuming that, production costs (wages and capital rent) and prices, do not change], an increase by 1% in quantities of output demanded will

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6 In a study by Chongo (2017), using a Vector Autoregressive (VAR) model, the Mozambican inflation was proved to be (in the long-run) more sensitive to changes in exchange rates than to domestic factors such as money supply. A 1% increase in exchange rates (i.e., a depreciation), *ceteris paribus*, increases the prices by 0.64% whereas a 1% increase in money supply pushes up prices by only 0.33%. 

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lead to the greatest ramp up in firms’ demand for labour, prompting a reduction of unemployment by 1.55%. The magnitude of the real output elasticity being the largest in our regression, conveys a stark, unavoidable and policy-relevant message: the most significant determinant of permanent changes in labour demand will clearly come from an increase in marketed physical quantities of output. Since the physical quantities of output that an individual firm or an entire economy can trade in the markets (both domestic and external), are crucially dependent upon productivity and competitiveness, we can reasonably assert that these are the ultimate determinants of permanent changes in employment levels in Mozambique.

5. Concluding Remarks

The present paper intended to empirically test the validity of the argument that wage moderation is necessary to secure jobs and economic growth in Mozambique.

Having analysed data spanning the past 3 decades, the paper found that the economy follows a profit-led growth regime, largely driven by FDI. Consistent with this growth regime, the country has pursued a wage moderation strategy which has kept real wages stagnant. This paper reckons that, considering the context of a consistently high labour force participation ratio, although the wage moderation strategy hasn’t led to reductions in unemployment, it has been effective at preserving a stable [albeit low] level of employment.

Rather than a reflection of an inherent inadequacy of the profit-led growth regime, the failure of the economy to reduce unemployment despite an environment of wage moderation and robust growth, is largely due to the high porosity of economy which held back de economy from absorbing an important share of its internally produced surplus, ultimately undermining its ability to proportionally expand the capacity utilization.

As the cost-of-living crisis heightens the pressure for higher wages, the evidence from this study suggests that wage hikes above inflation-adjusting will be ineffective at addressing the cost-of-living crisis and if anything, they will only lead to a higher inflation, a worsening current account deficit and ultimately a further deterioration of unemployment levels. Thus, the study goes on to recommend a priority focus of policymakers towards promoting higher levels of employment because it is actually the high ratio of adult dependency (mostly due to unemployment) that is exacerbating the negative social effects of the cost-of-living crisis for families.

The ability of the profit-led growth regime to spur higher levels of employment can be bolstered through appropriate reforms aimed at enhancing the productivity and competitiveness of the economy, starting from stopping the porosity of the economy and stimulating the productive reinvestment of profits within the country.
6. References


