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THE IMPACTS OF **SOCIAL AND ECONOMIC INEQUALITY** ON ECONOMIC DEVELOPMENT IN SOUTH AFRICA

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## Figures

Figure 1	Private investment has decoupled from corporate profits .....	25
Figure 2	Index of agricultural production per capita, 1961 to 2011 (2004 to 2006 = 100)...	27
Figure 3	Fixed capital formation in agriculture forestry and fisheries, 1980 to 2010 (SA Rand. ....)	27
Figure 4	Ratio of rural population to employment in agriculture: a global comparison ...	28
Figure 5	Wage share of GDP in South Africa 2011 .....	34
Figure 6	Unemployment per municipality .....	36
Figure 7	Proximity of RDP housing to major economic centres .....	39
Figure 8	Academic achievement by socio-economic status and age .....	42
Figure 9	Drivers of deprivation among the population .....	43
Figure 10	Distribution of Grade 4 numeracy achievement by historical education department (Data: NSES 20017/8/9) .....	43
Figure 11	Distribution of Grade 6 reading performance by school wealth quintile (Data: SACMEQ III 2007) .....	43
Figure 12	Percentage of individuals going hungry .....	44
Figure 13	Pen's Parade of income, 2006 .....	47
Figure 14	Average annual household income by population group of household head (2012) – in Rands .....	47
Figure 15	Income components by deciles, 2011 .....	48
Figure 16	Labour force status of working age population, 1994-2013, in millions .....	49
Figure 17	Employment in post-apartheid labour markets by race .....	50
Figure 18	Age distribution of unemployment rates in South Africa: 1995-2005 .....	50
Figure 19	Real earnings of wage-workers by gender .....	51
Figure 20	Mean real earnings in post-apartheid labour markets Wage workers by sector Part 1 .....	51
Figure 21	Mean real earnings in pos-apartheid labour markets: Wage workers by sector Part 2 .....	52
Figure 22	Growth Incidence Curves for black Africans: 1995-2005 .....	53
Figure 23	Employment protection legislation is relatively liberal .....	54
Figure 24	Returns to schooling: Black African and white men age 25-59; South Africa OHS/LFS .....	55
Figure 25	Growth Incidence Curves for South Africa, 1995-2005 .....	56

## Tables

Table 1	Structure of the economy (gross value added) 1994 and 2012 .....	30
Table 2	Unemployment by race and gender .....	49
Table 3	Gini coefficients decomposed by decile, showing deciles 1-4 with and without social grants .....	56

# Contents

	Executive summary .....	6
1	Introduction .....	11
2	Inequality, growth and economic development: Review of the theory .....	15
3	Inequality and the structure of the economy in south africa .....	21
	3.1 The inherited legacies of inequality in South Africa .....	21
	3.2 Ownership structures, asset inequality and trends in capital investment .....	23
	3.2.1 Ownership and concentration .....	23
	3.2.2 Patterns of private investment and financialization .....	25
	3.2.3 The land question .....	27
	3.3 Sectoral composition of the economy and employment .....	30
	3.4 The distribution of gains between capital and labour .....	34
4	Spatial inequality .....	35
	4.1 Spatial inequality in the rural context .....	36
	4.2 Spatial inequality in the urban context .....	37
5	Inequality in opportunities and human development outcomes .....	41
	5.1 The rights framework .....	41
	5.2 Drivers of deprivation and disadvantage .....	42
	5.3 Inequality of opportunity in education .....	42
	5.4 Health and inequality .....	44
	5.5 Inequality of opportunity and institutions .....	45
6	Income inequality in South Africa .....	47
	6.1 The big picture .....	47
	6.2 Income inequality and the role of the labour market .....	48
	6.2.1 Key labour market trends .....	48
	6.2.2 Unemployment as a driver of earnings inequality .....	49
	6.2.3 The role of wage inequality in overall inequality .....	50
	6.2.4 Dynamics in the middle of the distribution .....	52
	6.2.5 Labour market flexibility and inequality .....	53
	6.2.6 The role of education in labour market inequality .....	55
	6.3 Social grants, social protection and the social wage .....	56
	6.3.1 The impact of social grants on inequality .....	56
	6.3.2 South Africa's social protection gap .....	58
7	How social and economic inequality impact on economic development in South Africa ...	61
8	Priorities for public policy: dilemmas and trade-offs .....	65
9	Conclusions .....	71
10	References .....	72

# Executive summary

TWENTY YEARS AFTER the end of apartheid South Africa is a different place. It has a well-institutionalized democracy. Significant gains have been made in social equity and in reducing extreme poverty. Yet poverty, unemployment and inequality remain South Africa's most pressing problems. Social change and enhanced access to rights have not translated into comparable economic shifts – unemployment has risen and inequality remains extreme.

In policy debate in South Africa, the question often asked is, in the face of continued poverty, why focus on inequality – when poverty has the more immediate impact on people's lives? There is no dispute about that. But poverty, unemployment and inequality interact in complex ways, with evidence that high levels of social and economic inequality can constrain the scope for growth – and in particular, for the kinds of inclusive growth necessary to create jobs and reduce poverty. In contexts of high inequality, growth often reproduces existing patterns of distribution.

If high levels of inequality constrain growth, and limit its pro-poor impacts, then reducing inequality may be a prior and necessary condition for a sustainable decrease in poverty. Going for growth as a means of addressing poverty in the absence of policies to address inequality or the underlying factors through which inequality is reproduced may yield limited returns. Instead, reducing inequality may be a necessary condition for the kinds of growth required for optimal impacts on poverty. This has important implications for policy, casting into doubt the received wisdom of a trade-off between redistributive policies and growth.

In South Africa, public policy has had a significant redistributive content. Close to 60 percent of government spending is allocated to the social wage, and such expenditure has more than doubled in real terms in the past decade. Per capita health spending has doubled in the same period, free basic education was provided to the poorest 60 percent of learners, and levels of self-reported hunger have dropped by half. Sixteen million people are on social assistance, gross primary enrolment is at around 98 percent, and almost three million houses and housing units have been constructed as potential assets for poor people. Access to basic services such as piped water, sanitation, electricity and refuse removal have all improved, all contributing to a decline in both absolute and relative poverty, and to improving equality of opportunity. In a focus on fiscal policy and redistribution in the World Bank's 2014 Economic Update, they find that in 2010, the combined impact of taxes and transfers shifted South Africa's Gini coefficient from 0.77 to 0.59. Before taxes and social spending, the income of the richest 10 percent was more than 1000



Close to 60 percent of government spending is allocated to the **social wage**

## levels of **unemployment** have remained above 20 percent for the last 20 years

times larger than the poorest 10 percent; after taxes and social spending, this gap falls so that the richest 10 percent earn 66 percent more than the poorest 10 percent (World Bank 2014).

This illustrates the hugely important role of public policy in ensuring that the levels of inequality generated by the economy are mediated at the level of society. Yet within this picture, the World Bank acknowledges some caveats. While the targeted impact of cash-based transfers is easy to measure, the calculations of social spending on areas such as health, education and basic services assumes an equal per capita benefit from spending. Yet in practice, in all these areas, high levels of inequality of outcomes persist, particularly in relation to race, gender and location, and continue to have a strong inter-generational dimension. In a context in which the policy intent is clearly to promote equity, why is this the case? And why does the economy continue to generate such high levels of inequality before taxes and transfers?

Many of the answers are deeply rooted in the inherited legacies of apartheid policies. It is no coincidence, for example, that the former bantustan areas continue to be associated with high levels of disadvantage. They score the worst on every dimension of the multiple deprivation index for unemployment, nutrition, health outcomes, school outcomes, access to services, clean water, energy, sanitation and decent housing, and face severe institutional challenges also. Yet twenty years after the end of apartheid, the question is why post-apartheid policies have not had greater impacts in eroding such inherited legacies.

Despite the importance of policies that enhance equality of opportunity, the impacts of this on people's lives are predicated on there being opportunities. In particular, in South Africa, this means addressing levels of unemployment that have remained above twenty percent for the last twenty years. Unemployment is the single most important factor contributing to income inequality; yet at the same time, inequality plays a role in constraining the scope for employment creation and inclusive growth, in a negatively self-reinforcing cycle. How to break this cycle?



The paper starts with a brief review of the literature to explore the main trajectories through which inequality impacts on economic development and growth. This includes consideration of the crucial roles of public policy and institutions, as well as the roles of asset inequality, income inequality, and inequality in access to opportunities.

The paper then attempts to grapple with the multi-dimensional nature of inequality in South Africa and how social and economic inequality impact on the scope for economic development. It does so in relation to the following themes:

- The structure of the economy
- Spatial inequality
- Inequality in opportunities and human development outcomes
- Income inequality.

In considering the structure of the economy, the paper looks at the roots of inequality: at the double dispossession of land and of mineral rights under colonialism and apartheid, and at the closely linked process of creating a black working class. It then assesses developments following the transition to democracy post-1994. This uses the earlier theoretical discussion on the trajectories through which inequality impacts on inclusive growth to focus on the following themes:

- Structures of ownership and asset inequality
- The relative gains from growth accruing to capital and labour
- The ability of the economy to generate employment – and the terms of that employment.

Spatial inequality is then explored in both its rural and urban dimensions, and the impacts of these on the costs of labour and therefore the costs of production in the economy, before focusing on inequality of opportunities and human development outcomes. Under apartheid, denying black people political rights went hand in hand with limiting their scope for ownership of assets or participation in enterprise activity and prescribed a subordinate economic role in society. This in turn was compounded by social inequalities, in relation to rights and opportunities across the spectrum from access to basic services and amenities, to education and health. While apartheid ended 20 years ago, the first generation of born frees is only now entering higher education and the labour market; for most people of working-age and above, the apartheid years are still part of their living memory, and still affect their lives and the opportunities to which they have access today. The section on inequality in access to opportunities explores the gains made in this area since 1994, and the remaining challenges in ensuring equity of opportunity.

The paper then looks at income inequality in South Africa today. Decompositions of income inequality highlight the critical role of labour market outcomes, the role of unemployment and of wage disparities, and debates over the role of labour market policy. Important as the latter is, the paper argues that debates on addressing inequality in South Africa have given too much primacy to labour market policy; because while labor market outcomes are a critical determinant of income inequality, the main factors that determine the characteristics of both the demand and supply of labour fall outside the scope of such policy.

The role of social grants as a direct income source within the context of income inequality, and its impacts on inequality are then considered. While at an aggregate level, the impact of social grants on the Gini coefficient is relatively modest, the paper argues that from a sociological perspective, a more disaggregated view is necessary; because while big picture inequality certainly casts a long shadow over society as a whole, people's day-to-day lives are also affected by changes in their own communities, that affect their neighbours and

their families. The evidence shows that social grants significantly reduce inequality within the lowest four deciles, with their main effect being to lift the incomes of the poorest. Within poor communities, inequality has therefore been significantly lowered, and in the right direction. It is argued that more work is needed to understand the impacts of this on social cohesion and well-being at this level – without in any way diminishing the importance or impact of overall inequality. Dynamics in the middle deciles are also sociologically important.

Despite the gains from social grants, a critical gap remains in South Africa's social protection coverage that has direct implications for inequality. Most unemployed people are not covered by any form of social protection targeted at them as unemployed people. In addition, most unemployed people are from poor communities, which carry most of the social and economic costs of unemployment. This skewed allocation of the costs of unemployment in society makes poor households poorer, and has a disqualifying effect at an overall level.

The paper then draws together the arguments for how the structure of the economy, spatial inequality, inequality of opportunities and income inequality interact to reproduce South Africa's high levels of inequality, impacting in turn on economic development and the scope for inclusive growth, concluding with reflections on the implications of this analysis for a focus on policy.

The central argument is that if high levels of inequality are constraining inclusive growth, then policies cannot rely on growth to reduce inequality; instead, strategies to address inequality are a prior and necessary condition to unlock growth. While equality of opportunity certainly matters, it relies on the existence of opportunities to achieve changes in outcomes: unlocking such opportunities requires the underlying structural factors that shape such opportunities to be addressed – the structures of asset ownership, the structure of the economy, and the spatial issues. This requires strategies that shift the current patterns of growth onto a more labour-absorptive path. While many existing South African policies aim to achieve this outcome,

● Most unemployed people are not covered by any form of social protection targeted at them as unemployed people



institutional constraints and political economy issues need to be addressed to achieve the desired results.

Even under the best of circumstances, such results will take time to impact at the scale required. It is in this context that the role of redistributive public policy comes back into play. Given the role of unemployment in income inequality and the lack of social protection targeted at unemployed people, it is argued that closing South Africa's social protection gap in relation to unemployed people is vital. While priority should be given to the further expansion of public employment programmes in this regard, because of how participation in work contributes to social inclusion and to building productive capabilities, and because of the scope to use public employment to promote community development, the sheer scale of unemployment in South Africa means not all unemployed people can necessarily be absorbed in this way. Complementary forms of support need to be considered.

Despite the fiscal challenges this will create, it is an investment with both social and economic returns. Quite apart from its intrinsic value, it may also be a necessary condition for the social stability required to achieve long-term structural change in the economy, in a context in which the political economy of doing so will be a critical factor.

● Despite the gains from social grants, a critical gap remains in South Africa's social protection coverage that has direct implications for inequality

**Poverty and inequality – both exacerbated by unemployment – are South Africa’s most significant challenges**



IN MAY 2014, as the queues formed once more at voting stations, South Africans were reminded that only 20 years ago their country was a very different place, marked and marred by a history of institutionalized racism used to justify the concentration of wealth and power in minority hands. The first democratic election in 1994 ended the system of apartheid and realized the political rights of all South Africans, with these rights embedded in a Constitution that promises equality of status. South African society has changed fundamentally since then but the legacy of apartheid means the country remains scarred. Absolute poverty has been significantly reduced. Yet political and social change has not, as yet, translated into reducing South Africa's high levels of inequality. With a Gini coefficient for income inequality of 0.69, South Africa has earned the dubious distinction of being the most unequal country in the world – of those countries where inequality is measured.

Poverty and inequality – both exacerbated by unemployment – are South Africa's most significant challenges. The urgency of addressing them is recognized in South Africa's National Development Plan, adopted in 2013.

To eliminate poverty and reduce inequality, the economy must become more inclusive and grow faster. These are twin imperatives...The crisp question is how. The economy needs to meet a different set of objectives, beginning with job creation. It needs to become more nimble, responding quickly to opportunities and circumventing risks. Furthermore, patterns of ownership and control have to change. This will not be easy. It requires carefully sequenced actions that transform the economy without destroying its capacities (RSA, 2011).

Inequality in South Africa is deeply rooted in history; in colonial conquest and associated land dispossession; in the discovery of gold and diamonds and the wars fought to secure rights over them; in the need for cheap labour to get these minerals out of the ground; in the racial and spatial divisions that apartheid institutionalised; and in the concentrations of wealth this system enabled.

These historical legacies underpinned the distributional landscape that South Africa's new democracy inherited in 1994 and continue to be felt in economic outcomes and opportunities in the present. Inequality has remained deeply embedded, in:

- The structure of the economy
- Spatial inequality
- Inequality in opportunities and human development outcomes
- The structure of labour markets.

The nature of inequality has not remained static since 1994. Social change has brought changes in opportunity, market processes have impacted on patterns of distribution, as have global processes and crises, and public policy has of course impacted on outcomes. The question remains: how and why does inequality continue to be reproduced rather than being significantly eroded in the post-apartheid period?

While poverty levels remain high, public policy has had a significant redistributive content, and has achieved real impacts. According to the Millennium Development Goals Country Report 2013 (Stats SA, 2013), close to 60 percent of government spending

is allocated to the social wage, and such expenditure has more than doubled in real terms in the past decade. Per capita health spending has doubled in the same period, free basic education was provided to the poorest 60 percent of learners, and levels of self-reported hunger have dropped by half.

The Twenty Year Review: South Africa 1994-2014 (RSA, 2014) presses South Africa's good story further: 16 million people are on social assistance, gross primary enrolment is at around 98 percent, and almost three million houses and housing units have been constructed as potential assets for poor people. Access to basic services such as to piped water and to sanitation, electricity and refuse removal have all improved, all contributing to a decline in both absolute and relative poverty.

Yet poverty and inequality persist, and continue to have an inter-generational dimension. In a context in which poverty directly affects impacts on people's lives and well-being, the question is often posed: why focus on inequality? Certainly, an outcome in which inequality declines but poverty rises is no victory for development. A focus on inequality matters both for its own sake, as well as because of how it impacts on the scope to achieve poverty reduction and inclusive growth.

Inequality matters in its own right because of the ways it limits people's access to human rights, to opportunities, and on people's ability to reach their full potential. All of these impact in turn on who is most likely to be poor – and on the types of barriers they face in exiting from poverty.

Inequality of opportunity often informs inequality of outcomes. While at one level, this may simply be a function of poverty, its causes often include forms of social disadvantage based on gender, race, ethnicity, religion, or other forms of discrimination. These in turn often manifest in forms of exclusion and disempowerment that increase the likelihood of affected groups being poor, with the distribution of wealth often closely correlated to social stratification and power relations.

Building on Amartya Sen's work, the United Nations has developed the Human Development Index. This multi-dimensional measure of poverty looks beyond income and includes social outcomes such as nutrition status, access to water, sanitation and energy, and to education and health. More recently, the World Bank has developed the Human Opportunities Index focused on equity of access across a similar spectrum of issues, in order to provide a more multi-dimensional approach to the question of equity in society that also goes beyond a narrow focus on income inequality alone.

The Human Opportunities Index measures the coverage rate of basic services, adjusted by how equitably such services are distributed among groups differentiated by circumstances such as gender, race, family background and location. If these factors determine unequal access within a given coverage rate, this reflects an unjust source of exclusion (World Bank, 2012).

Many of these forms of inequality of opportunity fall within the ambit of social policy, but their impacts on human development have direct knock-on effects on people's ability to realize their productive potential in the economy also. This is a critical trajectory through which social inequality impacts on the economy and in turn on the scope for inclusive growth.



the number of  
**houses and  
housing units**  
constructed by 2014

Twenty Year Review: South Africa 1994-2014  
RSA, 2014

Inequality affects growth and poverty in other ways. While the interrelationships between them are the subject of extensive economic debate, evidence suggests that in certain contexts, high levels of inequality not only constrain growth but also limit the likelihood of growth being pro-poor.

If high levels of inequality act as a constraint on growth, and limit its pro-poor impacts, then reducing inequality may be a prior and necessary condition not only for growth but also for sustainable reductions in poverty. Going for growth in the absence of policies to address inequality or the underlying factors through which it is reproduced may be a fruitless exercise.

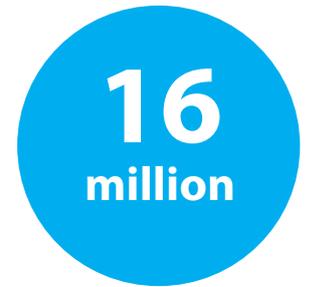
In addition, in contexts of high inequality, the rates of growth required to lift people out of poverty without a change in the distribution of the gains from growth may be unachievably high. This recognition has informed the increasing emphasis on the need for inclusive growth – growth in which an increased proportion of the gains from growth reach the poor. The crucial policy question is how best to shift the trajectory of growth to change its distributional impacts: an issue at the heart of economic policy debate in South Africa.

In this context, this paper explores how social and economic inequality in South Africa impact on economic development. Economic development is a wider concept than simply that of economic growth. Todaro and Smith (2011) define it as an increase in living standards, citizens' self-esteem, freedom from oppression and greater choice, best measured by the Human Development Index. By this definition, economic development is the converse of poverty, which is how it is used in this paper.

Although not formally included in the definition, there is a relationship between the scope for economic development and

## the number of people on social assistance by 2014

Twenty Year Review: South Africa 1994-2014  
RSA, 2014



economic growth. The centrality of debates over the relationships and causality between inequality and growth make further discussion of key themes in this literature necessary. Section 2 addresses this issue.

Thereafter, the paper explores the following crucial dimensions of inequality in South Africa:

- Inequality and the structure of the economy (Section 3)
- Spatial inequality (Section 4)
- Inequality in opportunities and human development outcomes (Section 5)
- Income inequality in South Africa (Section 6).

While income inequality is often the starting point for discussion on inequality in South Africa, it is dealt with last, not because it matters least, but because income inequality is, to a significant extent, an outcome and a manifestation of these other dimensions of inequality.

These sections are followed by a concluding analysis of the impacts of social and economic inequality on economic development and reflections on what this means for policy.

● Income inequality is, to a significant extent, an outcome and a manifestation of these other dimensions of inequality

**Inequality has a crucial impact on the sustainability of growth, which in turn determines its cumulative effects and impacts on poverty**



# Inequality, growth and economic development:

## Review of the theory

2

THE INTERACTION BETWEEN poverty, inequality and growth is the focus of a vast literature. For many years the focus of debate on the relationship between inequality and growth was on the impact of growth on inequality, and the discourse was dominated by Simon Kuznet's theory that in the early phases of industrialization, growth exacerbates inequality, but that it then decreases in the advanced phases of economic development. According to Thomas Piketty, however, "the magical Kuznets curve theory was formulated in large part for the wrong reasons, and its empirical underpinnings were extremely fragile" (Piketty, 2014). As inequality started its inexorable rise in the advanced economies of the world from the 1980s, the Kuznets Curve fell from favour.

Meanwhile, in the developing world, the distributional effects of economic growth were coming under increasing scrutiny. While economic growth clearly matters for poverty reduction, not all growth is equal in its effects on poverty, with the same rate of growth in different contexts having widely divergent outcomes. This recognition has fuelled the growing focus on how to achieve pro-poor growth and inclusive growth, and on the distributive effects of growth. In the process, it has become clear that prior patterns of distribution influence these outcomes.

As part of debate, Ravallion (2004) cites cross-country evidence that the higher the initial level of inequality in a country, the less the poor tend to share in the gains from growth. High inequality can make poverty

unresponsive to growth, and growth can simply by-pass the poor. In addition, high levels of inequality can create a feedback effect in which inequality impedes the scope for growth of any kind.

In comparisons of 153 developed and developing countries, Ostry, Berg and Tsangarides (2014) find that lower inequality is highly correlated with faster growth in all countries. Building on earlier work (Berg and Ostry, 2011), they also find that more equality in the income distribution is associated with longer growth spells, and argue that inequality has a crucial impact on the sustainability of growth, which in turn determines its cumulative effects and impacts on poverty.

If high levels of inequality constrain growth, and limit its pro-poor impacts, then reducing inequality may be a prior and necessary condition for growth as well as for a sustainable reduction in poverty. At the same time, can it be assumed that all forms of inequality are equal? What dimensions of inequality are the most damaging to the prospects for pro-poor growth? Through what trajectories does inequality have these impacts – and what does this mean for policy? These questions are the subject of significant debate and a brief review of the central arguments in the literature is attempted in this section.

In the beginning, there was primitive accumulation – Marx's term for the initial processes by which some people acquired land and capital, and others did not. Historically, these processes relied on the use of political power and force – on capture and

● If high levels of inequality constrain growth, and limit its pro-poor impacts, then reducing inequality may be a prior and necessary condition for growth as well as for a sustainable reduction in poverty

control, plunder in the context of war, and in more recent modern history, on colonialism and associated dispossession. Although this dimension of the origins of inequality is often either taken as given or ignored in the debate, no society grappling with high inequality today started on a level playing field. There has always been some process – deep in the mists of history or more recent – in which the dispossession of some and the capture of resources by others informed patterns of ownership.

This is the more brutal dimension of the concept of rents, which matters for inequality and for why and how this impacts on economic development and growth. Much of the focus on rents relates to the private capture of value from assets such as natural resources that should accrue to society as a whole, but the term “rents” has come to apply to any context in which a benefit is secured for less than its real value with rent-seeking behavior focused on the attempt to do just this, usually using forms of political leverage or monopoly power. The use of the concept includes the use of lobbying to secure special subsidies, or the ability to use monopoly power to inflate prices beyond the real value of what is produced. The ability to capture rents can be crucial in influencing patterns of inequality and elite formation. Where there is scope to capture rents – to secure benefits for less than their value or to secure preferential market advantage – this incentivizes a focus on such capture rather than on productive investment or innovation, with potentially negative impacts on economic development.

These processes of primitive accumulation and rent-seeking are the more obvious ways in which political power translates into distributional outcomes. Whether these outcomes lead to more inequality or more equity depends on the interests this political power represents. So, rare as these may be, there are contexts in which rents derived from natural resources are captured by government and used to fund social programmes, such as in Norway (The Economist, 2013).

A literature has also emerged on the vital role that the ability to allocate rents has played in creating political stability in the context of fragile states and post-conflict situations, enabling levels of political stability that has in turn enabled economic development, as well as instances in which the allocation of rents is used to play a redistributive role that enhances equity in contexts of prior inequality (Khan, 2005; North, Wallis, Webb and Weingast, 2007).

As Stiglitz (2012) argues, inequality is a result of political forces as much as economic ones, with government setting the rules of the game in ways that profoundly impact on distributional outcomes – not only in ways that exacerbate inequality, but in ways that can by contrast create equity also. While every country’s context is specific, a critical overarching factor that influences the extent of inequality is the role of public policy and of institutions.

While institutions play a crucial role in reproducing inequality, inequality also shapes institutions, creating what Chong and Gradstein (2004) have called a double causality relationship. In contexts of high inequality, elites are typically able to influence the rules of the game and shape institutions across the full spectrum, including the education system, the courts, competition policy, tenure regimes, labour market institutions, industrial policy and much more. Insofar as these institutions favour the interests of elites, they are likely to perpetuate inequalities in power, status and wealth (Stiglitz, 2012; Ravallion, 2004; Chong and Gradstein, 2004).

In addition, it is increasingly recognized that incentives and opportunities that are biased towards a small section of the population can constrain economic growth,

There is a high level of correlation between **asset inequality and slow growth**, with initial inequality of assets having a negative and significant effect on subsequent growth



because this limits innovation, risk-taking and investment. It is also unfair, and while fairness matters for its own sake, unfairness can have a wide range of negative social and economic consequences,

Lack of fairness influences equality of opportunities. When, for reasons of circumstance or discrimination, part of the population has a reduced likelihood of access to decent quality schooling, or carries a greater disease burden as a consequence of poor sanitation, or has a reduced likelihood of being employed, their productive potential is constrained, limiting their economic contribution. Inequality of opportunity also leads to inefficient allocation of resources. The net effect is to limit the scope for economic growth at an aggregate level. (World Bank, 2012).

Often, inequality of opportunity has a strong gender dimension. In a review of the literature exploring the interaction between gender equity and economic growth, Kabeer and Natali (2013) find that the relationship is asymmetrical: the evidence that gender equality, particularly in education and employment, contributes to economic growth is far more consistent than the evidence that growth contributes to gender equality.

People's sense of fairness also matters for well-being. A sense of unfairness can give rise to social conflict and a lack of social cohesion. This has a range of economic spillover effects. Stiglitz highlights evidence from the workplace context that a sense of fairness and equity positively influences productivity and innovation, while a belief among the workforce that they are unfairly treated impacts negatively (Stiglitz, 2012).

Lack of social cohesion as a result of inequality also lowers social trust, which makes it difficult for different interest groups to work together for a common social goal.

Contexts of high inequality undermine prospects for stability and the possibility of forging a social compact to launch onto higher and sustainable rates of economic growth. It can be argued that the progress attained in South East Asia (and other developmental states) was made possible in part by low levels of inequality and the sense of sharing and sacrifice, particularly when they launched onto higher growth trajectories some 40 years ago (Netshitenzhe, 2013).

High levels of inequality in assets or incomes can also create social instability and increase the risk of crisis. People seldom accept such inequality as fair, and use the instruments and institutions at their disposal to change whatever social order is delivering these outcomes. This creates uncertainty:

[E]conomic actors react to this uncertainty by reducing the scope of their activities, arranging their businesses so they are less exposed to risk, and investing in inherently less risky enterprises (where their investments can be easily withdrawn or shifted to other activities). These reactions slow the rate of economic growth (Keefer and Knack, 2000).

Often, this means investment in financial instruments rather than in productive capacity. This limits growth and constrains employment creation, in a context in which labour markets are crucial in determining the spread of income in society. In a context of low private investment, if the profit share of national income rises relative to the wage share, this is likely to reinforce inequality at the same time as slowing growth.

There is a high level of correlation between asset inequality and slow growth, with initial inequality of assets having a negative and significant effect on subsequent growth. Asset inequality impacts on growth in a number of ways. It affects the functioning of credit markets. Lending decisions by financial institutions are informed by assessments of risk that are often linked more to the profile of the borrower than to an assessment of likely returns from the investment. In practice, assets are often required as collateral and those without assets will find it harder to borrow regardless of the merits of the investment. This creates inefficiencies in the allocation of credit; poor investments secured by collateral are more likely to be financed than good investments that lack collateral. This includes the ability to invest in human capital – such as securing a loan to enable access to better schooling or to attend university. This leads to a low growth rate in the long-run and the emergence of poverty traps, which reflect the persistence of initial wealth inequality from generation to generation (Ehrhart, 2009; Deininger and Squire, 1997; World Bank, 2006).

Interestingly, Deininger and Squire (1997) argue that creating new assets will have a better effect on the poor than redistributing old ones.

Land is particularly important. Concentration in the distribution of land and land market imperfections, such as lack of clear titling and imperfect rental markets, reduce investment in productive capacity and limit the use of land as collateral, leading to sub-optimal use of this factor of production (World Bank, 2006). Gender inequality adds an additional dimension, with gender gaps prevalent in women's access to land ownership and rights, as well as to most inputs, assets and services important for agricultural activities, including for example access to credit markets. All of these reduce the productive contribution of women.

An underlying theme in the literature about why high inequality leads to low investment and the resulting outcomes on growth focuses on the part played by high levels of uncertainty. Attempts to address this uncertainty take different forms. In many developing countries, policy advice has focused on the importance of stable property rights in creating the kind of certainty necessary for investment. Yet Mushtaq Khan argues that attempting to replicate this and other sets of institutions believed to have enabled growth in the developed world to achieve the same effects in the developing world overlooks critical elements of context.

We have seen that the liberal-market consensus argues that the institutional structure for maximising growth is one which ensures that there are no rents in markets, where the state maintains stable property rights, and limits the transfers it carries out. The main task for the state is to concentrate on the delivery of democratically agreed upon public goods and to have a tax system that is efficient in raising resources for these tasks. While public good delivery is very important, evidence from developing countries casts doubt on the adequacy of these positions. The state's ability to carry out relatively massive interventions in property rights systems has been critical in dynamic social transformations in many high-growth economies, as has been the creation and management of growth-generating rents. States have also carried out significant transfers which contributed to political stability and thereby made the emerging institution structure politically viable (Khan, 2005).

Khan also argues that far from stable property rights being a necessary condition for growth, high-growth transitions have by contrast often been characterized by a

rupture in existing property relations, with such ruptures creating new conditions for growth. According to Khan, stability in institutions such as property rights follows, rather than precedes, such transitions. He argues further that "the most persistent types of state failure occur when institutions fail because of an inappropriate match between internal political settlements and the institutions and interventions through which states attempt to accelerate transformation and growth".

In the South African context, in which unemployment is a driver of income inequality, the larger debates on the causes of unemployment and the interface of these with inequality become central also. John Maynard Keynes argued: "The outstanding faults of the economic society in which we live are its failure to provide for full employment and its arbitrary and inequitable distribution of wealth and incomes." (Keynes 1936). From a Keynesian viewpoint, governments have two main levers with which to achieve full employment: the use of public investment to provide economic stimulus, coupled with welfare spending. Part of the purpose of such welfare spending is to contribute to aggregate demand, with social spending providing a stimulus for productive investment.

The question of aggregate demand is also affected by the share of national income that goes to profits relative to labour. This shapes patterns of consumption and the composition and scale of local demand, which in turn limits the scope for industrial development and employment creation.

The relationship between the relative shares of wealth going to capital and labour as "factors of production" are at the centre of Thomas Piketty's arguments in *Capital in the Twenty-First Century*. Piketty (2014) argues the importance of differentiating between inequality at this level, and inequality at the level of individual income. While the received wisdom for a long time was that the most appropriate split was two thirds for labour and one third for capital, he provides a historical analysis that shows the extent to which capital's share has risen, in particular in the wake of financial globalization and liberalization in the 1990s.

Piketty uses detailed statistical analysis of tax records to produce new evidence on trends in wealth creation going back over long periods in history. He argues that the systematic historical tendency of capitalism is for entrepreneurial capital to turn into rentier capital held in real estate, stock market shares, and government debt instruments, with forms of wealth accumulated in the past growing more rapidly than output and wages – leading to a context in which “the past devours the future” – and inequality keeps rising:

This inequality expresses a fundamental logical contradiction. The entrepreneur inevitably tends to become a rentier, more and more dominant over those who own nothing but their labour. Once constituted, capital reproduces itself faster than output increases. The past devours the future (Piketty, 2014).

The gap between capital and earned income grows exponentially when the ratio between the two strengthens in favor of capital. Within this, inherited wealth is pivotal.

In a review of Piketty’s book in *The New York Review of Books* Paul Krugman argues that Piketty’s work has created “a revolution” in our understanding of long-term trends in inequality.

Before this revolution, most discussions of economic disparity more or less ignored the very rich. Some economists (not to mention politicians) tried to shout down any mention of inequality at all: “Of the tendencies that are harmful to sound economics, the most seductive, and in my opinion the most poisonous, is to focus on questions of distribution,” declared Robert Lucas Jr. of the University of Chicago, the most influential macroeconomist of his generation, in 2004. But even those willing to discuss inequality generally focused on the gap between the poor or the working class and the merely well-off, not the truly rich (Krugman, 2014).

Piketty’s work has focused attention on the one percent and with it the role of public policy in mitigating growing inequality. A critical part of this relates to the tax regime. Piketty’s work shows how shifts in distribution patterns over the last century link quite clearly to the extent to which progressive tax systems are in place, and to the role of wealth taxes and inheritance taxes. His work has led to a renewed focus on the potential role of wealth taxes of various forms.

In  
comparisons of  
developed  
and developing  
countries... **lower inequality  
is highly correlated  
with faster growth** in all  
countries.

Ostry, Berg and Tsangarides, 2014

In the US context, Stiglitz’s work also illustrates how changes to the tax regime initiated in Reagan years contribute directly to rising inequality. Yet Stiglitz also emphasises other dimensions of public policy, including the role of regulation. For Krugman, the lack of attention to the role of deregulation in enabling growing inequality is a key weakness in Piketty’s analysis – despite its significance.

These are only some of the main trajectories through which high levels of inequality are believed to constrain growth, and to limit inclusive forms of growth in particular. While inequality matters for its own sake, it also matters because of how distributional issues limit the scope to address poverty, directly and through the effects of inclusive growth.

**Apartheid kept labour cheap  
by limiting the scope for  
Africans to farm, forcing  
them into labour markets**



# Inequality and the structure of the economy in South Africa

## 3.1 The inherited legacies of inequality in South Africa

IN THE LITERATURE on institutions and inequality, the persistence of institutionalized political and economic inequality over time is highlighted, as well as the extent to which early institutions affect institutions in the present (Rodrik 2007; North 1994; Chang 2005). In the discourse in South Africa today, there is a certain fatigue at referencing the past as an explanation for problems in the present and a tendency to do so fairly cursorily. Yet in the process, this risks overlooking just how deep the structural constraints are on transformation – and therefore just how concerted a policy response is required to change South Africa’s trajectory. The historical roots of economic inequality in South Africa are, therefore, sketched briefly in this section.

While the history of inequality in South Africa certainly predates this, the discovery of gold and diamonds in the late 19th Century changed the course of South Africa’s political and economic development. Along with the later discovery of coal, platinum and many other strategic mineral resources, this provided the basis for the South African economy to become what has been described as a Mineral-Energy Complex, with an industrial base founded around mining and energy intensive activities (see Chabane, Goldstein and Roberts, 2006 and Fine and Rustonjee, 1996). The state actively promoted a cluster of energy and mining industries focused on raw and semi-processed mineral products (Ashman, Fine

and Newman, 2011). Industrial policy in the apartheid period focused on building an industrial structure with large dominant firms in key industries such as steel, petroleum and telecommunications, built on the back of state funding. These processes also drove rapid urbanization, with the cities providing a growing market for agricultural produce. Although the ruling National Party retained a strong political power base in the agriculture sector, a coalescence of interests also emerged between the state and big business in relation to the mining industry.

The expansion of both mining and agriculture was built on the back of cheap labour and the institutionalization of a migrant labour system. The 1913 Land Act was a critical part of this process: a defining moment both in land dispossession as well as in shaping the future of South African labour markets. Less than a decade after the Anglo-Boer war, it represented an unlikely alliance between mining capital (mainly English) and agricultural capital (mainly Afrikaans), with the common purpose of forcing black people off the land and into a set of native reserves that were to become the 10 bantustans under apartheid.

● In the discourse in South Africa today, there is a certain fatigue at referencing the past as an explanation for problems in the present and a tendency to do so fairly cursorily

**1913** Land Act defined land dispossession and shaped the future of South African labour markets

For mining capital, the purpose was to limit land-based livelihoods and thereby force black people into the labour market as cheap labour – a process that until then had been successfully resisted. For white landowners, the purpose was to gain access to increased land in a context in which the discovery of gold and diamonds had opened new urban markets for food, and to remove competition from black farmers, who were also accessing these markets (Callinicos, 1980). Apartheid kept labour cheap by limiting the scope for black Africans to farm, forcing them into labour markets; contracts were, however, kept short term, to prevent permanent urbanization, with a system of “passes” linked to employment contracts and used to limit their rights to live in the cities. A system of racially discriminatory forms of job reservation also limited black African people to unskilled work; skilled jobs were reserved for whites only.

Industrial policy was used to develop import-substitution capabilities and state-owned enterprises in support of mining. The manufacturing sector grew, also supported by cheap energy, abundant mineral resources, and spending on defence. From the 1960s onwards the state invested heavily in large projects in petrochemicals, iron and steel, and electricity generation, creating state-owned monopolies in key industries. At the same time, extensive state support to agriculture enabled a large, commercial agricultural sector.

Sanctions coupled with foreign exchange controls imposed by the government further strengthened import-substituting industries and led to ever greater levels of concentration – and also inefficiency. Wealth that could not leave the country was redirected to investments in financial services, retail and agro-processing, creating

strong vertical and horizontal linkages across sectors. Wealth was highly concentrated, with four main conglomerates controlling most of the economic activity: Anglo American Corporation, Sanlam, Old Mutual and Rembrandt/Remgro (Roberts, 2004).

Fedderke and Szalontia (2003) examined industry concentration in South African manufacturing between 1976 and 1996 and found that a small proportion of firms accounted for the bulk of production and output across almost all manufacturing sectors. In almost all of the 24 sectors they considered, less than five percent of firms accounted for over half the industry output. They also found that high levels of concentration tended to lower output growth and labour productivity, while raising unit labour costs. They found that increased inequality in market shares raised investment rates whereas falling firm numbers lowered them. They also found that increased concentration unambiguously lowered employment. South Africa’s unemployment crisis – and its impacts on poverty and inequality – begins in this period.

Chabane, Machaka, Molabo, Roberts and Taka (2003) confirm this analysis post-1994, noting no changes in concentration between 1996 and 2001 (in employment and value added). The report notes that continuing levels of concentration point to the dependency of economic activity and growth on a few large (dominant) firms or “lead dynamic firms”. This heavily influences economic performance and intuitively points to reduced scope for broadening participation in certain industries for historically disadvantaged people.

In addition, from the late 1970s, the apartheid economy began to slow due to falling global commodity prices, rising welfare costs, rising unionization, international sanctions, rising domestic debt, and the costs of policing a country erupting in political resistance to apartheid. With the exception of brief periods when gold prices were up, the economy contracted throughout the period 1970 to 1993 (RSA, 2011). The political crisis of apartheid was underpinned by an economic crisis – an important factor influencing the willingness of the business community to countenance change, which assisted in shifting the balance of forces in ways that enabled the transition to democracy.

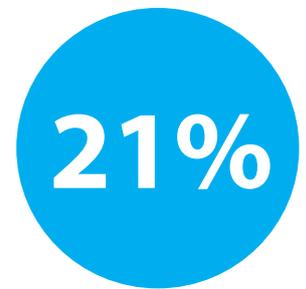
The South African economy has been described as a Mineral-Energy Complex: with an industrial base founded around mining and energy intensive activities

1970  
-  
1993

**the economy contracted** with the exception of brief periods when gold prices were up

RSA, 2011

# black ownership of the top 100 companies listed on the JSE by 2012



This economic structure – and the crisis in which it was mired – was inherited by the new democratic government in 1994, with its options for the future framed by a negotiated constitution that enabled a peaceful transition to democracy, but at the cost of a historic compromise that recognized existing property rights – no matter how ill-gotten they might have been..

The structure of the economy continues to impact on inequality in the following main ways:

- Through the structure of ownership and asset inequality, and how capital is invested
- Through the sectoral composition of the economy, which influences its ability to absorb labour and the composition of skills demand, both of which impact on income inequality
- Through the relative gains from growth accruing to capital and labour, which contribute to the distribution of wealth.

Key shifts and trends in the South African economy in relation to these issues post 1994 are explored in the sections 3.2 to 3.4.

## 3.2 Ownership structures, asset inequality and trends in capital investment

### 3.2.1 Ownership and concentration

South Africa's highly unequal structures of asset ownership, and the strong racial profile of this inequality, meant this was a necessary target for transformation in the post-apartheid period. In terms of capital ownership, the Johannesburg Stock Exchange (JSE) represents the commanding heights of the economy. There were several dimensions to the policies intended to transform ownership at this level. The aim was to change the racial profile of ownership, to achieve deconcentration of ownership, to reduce inequality, and to promote efficiency.

Strategies to increase black ownership coincided with a big push to privatise a range of state-owned enterprises, in a process in which the government divested itself of many of the companies

on which apartheid industrial policy had been built. In the same period, many of South Africa's largest conglomerates also unbundled or restructured, creating share offers in the process that enabled some black participation in ownership. Such participation often relied on loan finance to enable the sale, in a context in which few black people had the capital needed to buy into large listed companies. This meant loans had to be repaid from dividends, creating pressure for profit-taking over reinvestment. The viability of this market-based mechanism was also vulnerable in contexts such as the 1998 economic crisis, when many share-ownership deals suffered setbacks. These deals also entailed large-scale financial transactions that were good for the financial sector but did not translate into new productive investment.

By 2012, black ownership of the top 100 companies listed on the JSE was estimated at only 21 percent (with 21 percent of shares still to be assessed). Of this, only nine percent is held directly, with the rest through mandated investments such as pension funds (Chandler, 2012).

An approach to black economic empowerment based simply on changes to share ownership at the top came in for much criticism, described as "a form of redistribution of shareholding but between elites" (Khalil, 2012). This gave rise to a new policy acronym: BBBEE, or broad-based black economic empowerment, and a focus on strategies intended to have a wider reach. These include a set of codes promulgated by the Department of Trade and Industry (the dti) that link government procurement to a set of incentives based on black ownership, management, and also to corporate social investment and training activities by companies. Procurement policies can make a significant difference in creating access into the economy and into value chains for new entrants and small businesses. An assessment of the impact of this is beyond the scope of this paper, but it is an important

issue both because of its potential positive impacts and also because of whether and how the creation of these kinds of incentives may have created opportunities for rents to be captured in the process. There is evidence of this being the case in government's own application of these procurement policies, in each of the three spheres of government, with implications for the value of services delivered. Insofar as this is the case, and depending on its scale, this can affect equality of opportunity and therefore distribution.

The focus on shifts in the demographic profile of ownership has left the underlying structures of ownership unchanged in key respects, with high levels of firm concentration continuing to characterize the economy. Arguably, the focus on changing the demographics of ownership without at the same time addressing these more structural issues has changed the political economy of doing so. Demographic changes in ownership – limited though they are – have nevertheless created a new alignment of interest between the old economic elite and new beneficiaries of the existing economic structure. In the early days of the post-apartheid period, there was a disjuncture between those who controlled the commanding heights of the economy and those newly in political power. This gap has narrowed. While some of the existing economic elite resisted even this limited level of change, others quickly grasped the strategic importance of creating a new alignment of interests. In the process of constructing share-ownership deals and appointing black directors, it was surely no coincidence that the sweetest deals went to those deemed to have the most political influence.

The opening up of the economy through trade liberalization in the post-apartheid period also created new pressures for consolidating capital, with some inefficient firms closing and others attempting to create greater economies of scale through mergers and acquisitions. At one level, economies of scale can enhance efficiency and the potential for South African firms to compete in global markets. Yet high levels of concentration are also associated with negative effects on efficiency, through raised prices and the creation of barriers to

competition (Roberts, 2013). The bread price fixing scandal, in which a few large players were found in 2010 to have colluded to raise prices artificially high, illustrates how poor consumers are harmed by monopolies. Other forms of collusion, such as in the construction industry, lock out new entrants, ensuring that economic power and opportunity in a given sector remains in the hands of a few players – reproducing patterns of inequality.

With competition policy as it stands, monopoly supply and pricing of key inputs such as steel and plastics constrains downstream manufacturing. Some investigations show that aligning competition policy with industrial policy lowers costs of inputs for manufacturing and in other product categories that affect the poor e.g. fertiliser, maize and wheat milling and other food industries.

While competition policy was designed to tackle concentration in the economy, it has been a relatively blunt instrument. Despite successes in addressing the most collusive practices, it has been unable to achieve the structural shifts in levels of concentration required to change patterns of asset ownership.

### 3.2.2 Patterns of private investment and financialization

The section on the theoretical debates highlighted the tendency for high-asset inequality to make investors risk-averse and for this to lead to disinvestment and/or a decline in longer-term investments in productive assets. Both of these outcomes are evident in the South African context.

The restructuring and unbundling of some of South Africa's biggest conglomerates during the transition period appeared on one level to be a positive response to government's policies of promoting deconcentration in the economy. But there were other rationales for this process also. First, the levels of concentration in the economy made nationalization a tempting policy proposition, in a context in which this option had only recently been removed from the economic policy wish list of the ruling African National Congress (ANC) party. Unbundling may have seemed like a judicious way to limit the risks of a reversal on

South Africa's bread price fixing scandal, in which a few large players were found in 2010 to have colluded to raise prices artificially high, illustrates the negative impact on poor consumers

this score. Second, some of the restructuring and unbundling went hand in hand with off-shore listings for strategic parts of these former conglomerates. This disinvestment was accompanied by significant capital flight; some of it legal and enabled by the liberalization of foreign exchange controls, but much of it illegal and based on transfer-pricing practices. According to Fine (2012), at its peak in 2007, illegal capital flight exceeded 20 percent of gross domestic product (GDP).

In addition to removing capital from the economy, there has also been disinvestment from productive activity, with the Organisation for Economic Co-operation and Development (OECD) arguing that private investment has “decoupled” from corporate profits (Figure 1). While corporate profits offer attractive investment returns by global standards, private investment is nevertheless going into financial markets instead of into productive investment. This is contributing to what has been referred to as the “financialization” of the South African economy, creating a heavy reliance on public investment to attempt to stimulate growth.

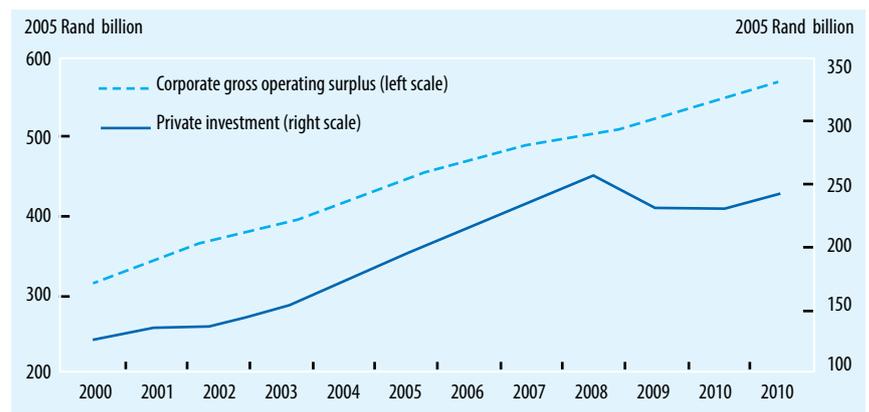
at its peak in 2007,  
**illegal capital flight** exceeded  
 20 percent of GDP

Fine, 2012



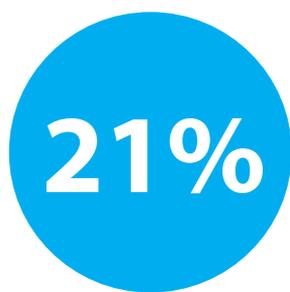
FIGURE 1

Private investment has decoupled from corporate profits



Source: OECD, 2013

While the issue of financialization is a global one, it is also a specific feature of the South African economy in the post-apartheid period, with implications for the structure of asset-holdings and inequality. According to Fine (2012), “financialization has produced a particular combination of short-term capital inflows and massive long-term outflows of capital as major ‘domestic’ corporations have chosen offshore listing and internationalization while concentrating within South Africa on core profitable MEC [Minerals Energy Complex] sectors”. This has made the South African economy highly dependent on short-term capital inflows to maintain the overall balance of payments, with these short-term inflows also focused on financial rather than productive investment.



of GDP accounted  
for **financial  
services** in 2010

Rashid, 2012

Ashman et al (2011) also argue that since the 1990s, the South African economy's growth path has been shaped by financialization<sup>1</sup>. Capital has been directed away from the kinds of productive investments necessary to diversify the industrial base, and into finance and consumption instead, as well as into sectors with strong linkages to these, such as the retail sector. The financialization phenomenon has also been linked to entrenching inequality in South Africa.

The major banks are part of a highly concentrated industry, and they have increased their provision of credit, which has fuelled consumption. Unsecured lending has also drastically increased with interest receipts being a major driver of revenues.

This has been compounded by the financialization of commodity markets internationally, with the rise of new financial institutions and instruments, particularly the use of derivatives linked to commodities and the proliferation of exchange traded funds including those tracking commodities stocks.

According to the United Nations Committee on Trade and Development (2012) the volumes of exchange-traded derivatives on commodity markets is 20 to 30 times larger than physical production. As a result, these "real" markets have been systematically transformed into financial markets, with an increasing disconnect between prices and actual production and between demand and supply linked to the productive use of such commodities.

This has contributed to the further financialization of South Africa's Minerals Energy Complex (Fine and Rustomjee, 1996) creating high levels of volatility in commodities markets, making investment planning harder for mining companies and promoting a preference for liquidity, where speculation on price changes is more profitable than long-term real investment in mines or into the expansion of mining output. These developments do not favour investment and employment. They are compounded by events that include the shooting by police of protesting miners at Marikana in 2012, when 34 miners were killed, the five-month strike in the platinum sector in 2014, and renewed calls for nationalization of the mines by the Economic Freedom Fighters (a new political party represented in parliament since the 2014 elections).

The impacts of financialization on inequality also reach beyond the mining industry. Rashid (2012) highlights how, relative to GDP, South Africa has one of the world's largest stock markets, and how financial services accounted for nearly 21 percent of GDP in 2010. The financial sector is highly concentrated, with four major banks that earn high rates of returns, especially from products offered to households.

In the post-apartheid period, in the name of "banking the unbanked", and against a backdrop of financial market deregulation, the provision of consumer credit and unsecured lending increased drastically, with interest receipts being a major driver of revenues. Consumer credit contributed to high levels of household debt, particularly in the middle-income and upper-income brackets. Such household debt exacerbates inequality, because high interest rates on consumption-based debt raises the cost of living for those dependent on it without creating assets – and often eroding them. This widens the gap for both income and asset inequality.

<sup>1</sup> Financialization refers not only to the growth and proliferation of financial institutions, actors and products, but to the increased centrality of financial markets in all aspects of social, economic and political life, and the way in which the interests of financial markets now dominate economic discourse (Ashman et al, 2013).

Access to credit for investment in assets also remains constrained for those without collateral. A key example of this concerns access to housing, with a band of people who fall above the means-test limit for state-funded housing but also fall below the thresholds for access to bonds to purchase housing (Rust, 2007).

### 3.2.3 The land question

Another dimension of asset inequality is the land question. It is common cause that land restitution and reform policies have been largely unsuccessful and that the outcomes of such policies have been limited, with limited impacts on poverty or on the structures of asset ownership.

What have been the impacts of problematic land reform policies? In twenty years land reform has only marginally altered the agrarian structure of South Africa, and made relatively minor positive impacts on the livelihoods of those to whom land has been transferred. To date only around 8% of farmland has been transferred through restitution and redistribution, and many settled restitution claims have not been fully implemented. The great majority of 69 119 urban restitution claims have been settled through payment of cash compensation. Empirical evidence suggests that around half of rural land reform projects have seen improvements in the livelihoods of beneficiaries – but often these are quite marginal. On farms with high-value fruit orchards, restitution claims settled through the establishment of joint ventures between claimant communities and private sector partners have not been successful either. In many cases government funds have not been fully released and often private sector partners have withdrawn following severe economic difficulties (Cousins, 2014).

With the land question, South Africa appears to be caught in the worst of all scenarios. Little meaningful redistribution has taken place, making the land issue an easy target for popular political mobilization. Yet the uncertainty over whether, when and how land policy might get more assertive has significantly disincentivised private investment in agriculture, leading to a declining contribution by the agricultural sector to sorely needed unskilled employment, to GDP and to exports. At the same time, deagrarianization in the former bantustan areas – arising from the terms on which migrant labour became the dominant

source of livelihoods – means South Africa has a relatively small number of black smallholder farmers willing and able to take on a greater role in commercial farming, and new entrants into agriculture often start from a low skills base.

The impacts of this uncertainty are illustrated by the trends in agricultural output and fixed capital formation (Figures 2 and 3). The decline of private investment in agriculture has been accompanied by a decline in public investment, including in agricultural research and development and irrigation capacity.

● Little meaningful redistribution has taken place, making the land issue an easy target for popular political mobilization – yet the uncertainty over whether, when and how land policy might get more assertive has significantly disincentivised private investment in agriculture

FIGURE 2

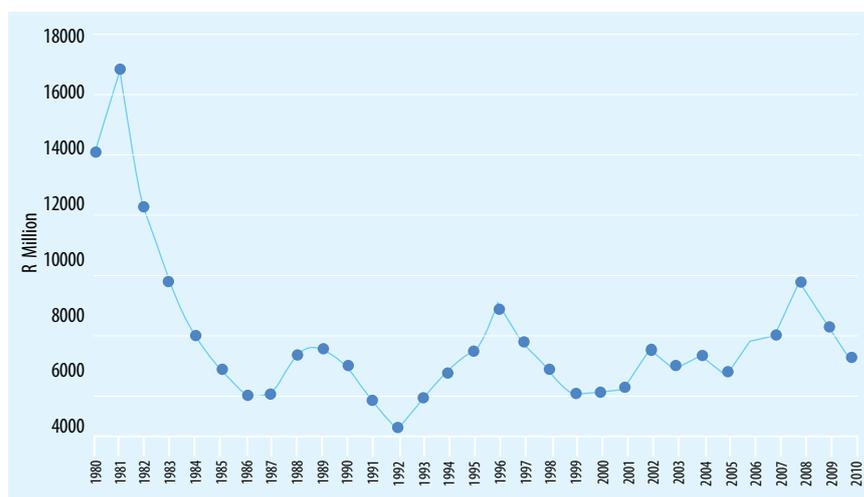
Index of agricultural production per capita, 1961 to 2011 (2004 to 2006 = 100)



Source: Sender, 2014

FIGURE 3

Fixed capital formation in agriculture forestry and fisheries, 1980 to 2010 (Rand)

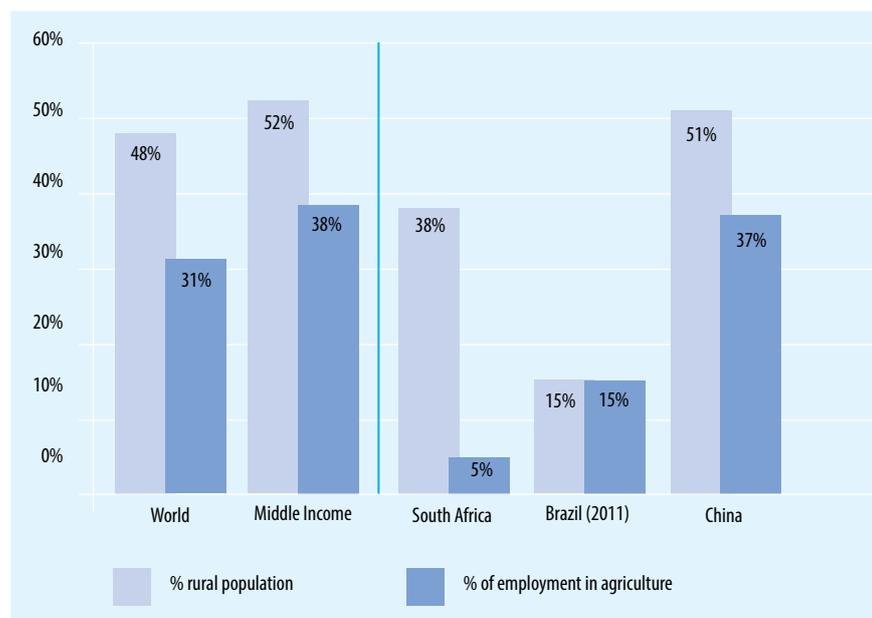


Source: Hall, 2012

These trends have severe implications for the labour absorptiveness of the agricultural sector, with South Africa a global outlier. In 2013, agriculture accounted for only five percent of total employment, while over a third of the population was classified as rural (Figure 4).

FIGURE 4

Ratio of rural population to employment in agriculture: a global comparison



Source: Makgetla and Dicks, 2014

Dynamics in the commercial agricultural sector are compounded by those in the former bantustan areas, where communal land tenure systems prevail, and where deagrarianization has been a feature for some decades. While there is debate over the causes of such deagrarianization, access to land within former bantustan areas is also highly unequal, with only 13 percent of people living in these areas having access to land, and with 80 percent of these spending less than seven hours a week doing farm work (Makgetla and Dicks, 2014).

Policy solutions to this context are not straightforward. It is clear that the appropriation of land had a deep impact on South Africa’s race-based structures of asset inequality, but land no longer plays the economic role it did at the time it was taken away. Today, most value in agricultural value chains is concentrated

further up the chain, in South Africa’s highly vertically-integrated agro-processing sector and the retail sector, with farmers often squeezed by low farm-gate prices. Low profitability in agriculture is compounded by the post-apartheid decision to lower agricultural tariffs in South Africa below the levels required by the World Trade Organisation, making South Africa’s farmers (black and white) among the least protected in the world (Sender, 2014).

The gap between the size of South Africa’s rural population and (linked) employment in agriculture represents a major economic development challenge. Remuneration for farmworkers is another boiling point.

In addition, therefore, to confronting the question of how to create greater racial equity in land-ownership patterns, policy has to address the question of how to ensure that the terms on which this happens don’t end up simply setting new black farmers up for failure – in a context in which market conditions for farmers are extremely tough. In addition, the opportunities for the kind of accumulation that land-ownership in the early 20th century allowed relatively small farmers are now mainly absent, with land ownership increasingly corporatized (Sender, 2014).

The number of small-scale black farmers farming commercially is hard to determine, but recent estimates in which this category is defined as comprising black households “able to market most of their production” and derived from the General Household Survey of 2009 put this figure at 47 000 (Aliber and Hall, 2012). At one level, the relatively small scale of this sector should make the identification, procurement and transfer of

**13%** of people living in former bantustan areas have access to land

## the number of small-scale black farmers in 2009

47 000

high-quality agricultural land and support services for this grouping a manageable proposition and a priority of policy. Scope does also exist for increasing household smallholder schemes and employment in agro-processing through land reform programmes that provide comprehensive support around infrastructure, marketing and extension services.

Yet, in practice, restitution policies and agricultural support policies have been disconnected (Cousins, 2014). The net effect has been that much of the land redistributed through restitution has not primarily benefited those black farmers engaged in agriculture. Perhaps predictably, many of the beneficiaries of land restitution processes had lost productive ties to the land. Even when they have opted to return to the land, the purpose has not always been to farm, with land sometimes used for residential purposes or part-time livelihood activity. Even where productive commercial farms have been transferred through restitution processes, the failure rate has been high (Sender, 2014).

In addition, continued uncertainty over proposed reforms to communal tenure systems in former bantustan areas is as likely to impact on investment decisions by poor and subsistence farmers as it does for commercial investors on private land. The breakdown of land administration in bantustan areas such as the former Transkei and Ciskei has compounded such uncertainty (Robinson and Philip, 2014).

Despite the centrality of the land question and the importance of agriculture for GDP and unskilled employment, policy continues to be based on a continuous stream of mixed messages, with a track record of unintended consequences that negatively impact on the poor. Probably the most damaging example of this was the promulgation of the Extension of Security of Tenure Act in 1997. This aimed to provide security of tenure to black farmworkers on white farms, but led instead to the eviction of more than two million farmworkers, significantly increasing rural poverty (Pepeteka, 2013).

Right now, South Africa seems to be at risk of repeating this experience. Currently on the table is a policy called Strengthening the Relative Rights of People Working the Land. The

policy proposes to create 50 percent equity share ownership schemes for farmworkers on all privately owned farms, but has managed to unite both landowners and farmworkers in opposition. Criticism of the policy argues that it creates powerful incentives for farmers to remove farmworkers from farms, at the same time as creating divisions between farmworkers because of proposed ownership ratios that give farmworkers an interest in reducing their own numbers (Hall and Du Toit, 2014).

Also on the table is the proposed new Communal Land Tenure Policy, introduced by the National Department of Rural Development and Land Reform. The Communal Land Tenure Policy explains that traditional leaders were imposed on people under colonialism and apartheid, and points to “much tension concerning the role of traditional leadership institutions in land administration”. Yet the policy nevertheless proposes to transfer communal land titles to traditional councils and to delegate certain governance responsibilities to them – placing traditional leaders at the centre of land management and allocation.

Criticism of this approach has raised concerns that the proposed policy may have the effect of weakening people’s security of tenure on communal land, and that the policy may worsen rural inequalities, with risks of capture by elites and erosion of the rights of the most vulnerable (Centre for Law and Society, 2014)

In conclusion: land access in South Africa remains highly unequal, and South Africa is a global outlier in its limited contribution of agriculture to GDP, limited levels of private and even public investment in this area, its limited role in providing unskilled employment as well as the limited role played by subsistence agriculture in providing a form of safety net and level of food security for the rural poor: all of which add up to it being a significant driver of inequality – and an area of significant policy weakness.

### 3.3 Sectoral composition of the economy and employment

The sectoral composition of the economy impacts on its ability to generate employment – and the kinds of employment that it creates. This sectoral structure has its roots in the MEC. Fine and Rustonjee (1996) have described South Africa as having a specific system of accumulation, centred on mining and energy, and sectors linked to them. At its height in the 1940s and 1950s, they argue that the MEC drove the South African economy, and that surpluses from mining-enabled state investment (and the creation of opportunities for Afrikaner capital) in electricity, steel, petroleum, and transport. This created strong interlinkages and synergies between the state and the market within the South African economy. The development of manufacturing in South Africa was also, to a significant extent, tied to and supported by the MEC.

The post-apartheid period has seen a series of attempts to change this economic structure. The emphasis has changed over time, but the common features include a consistent aspiration to reduce the dependence on mining and develop an export-oriented manufacturing sector able to compete in global markets. In more recent years, strategies to achieve this have increasingly focused on industrial policy and supporting those sub-sectors most likely to create jobs. In practice, while the contribution of the mining sector to GDP has declined, the health of the manufacturing sector remains closely tied to it.

Table 1 illustrates the sectoral shifts in the South African economy since the end of apartheid.

**TABLE 1**

**Structure of the economy (gross value added), 1994 and 2012**

SECTOR	Percentage of total gross value added	
	1990	2012
<b>Primary</b>	<b>13.9</b>	<b>7.9</b>
Agriculture, forestry and fisheries	3.3	2.4
Mining and quarrying	10.6	5.5
<b>Secondary</b>	<b>25.5</b>	<b>22.6</b>
Manufacturing	20.2	17.2
Electricity, gas and water	2.3	2.0
Construction	3.0	3.4
<b>Tertiary</b>	<b>60.6</b>	<b>65.5</b>
Wholesale and retail trade, catering and accommodation	13.0	14.0
Transport, storage and communication	6.6	10.1
Finance, insurance, real estate and business services	16.4	23.9
General government	18.7	15.3
Other	5.9	6.2
<b>Total</b>	<b>100</b>	<b>100</b>

Source: Adapted from Roux, 2014

In the second half of the 1990s, the manufacturing sector faced major adjustments due to the opening up of the South African economy and rapid trade liberalization. The sector benefitted from the depreciation of the Rand from 1998, but export performance was hampered as the currency strengthened after 2001. In more recent years, the manufacturing sector's performance was also boosted by strong domestic demand, while export-oriented industries faced a challenging trading environment, characterized by fierce competition in global markets and a strong exchange rate (Hanival and Maia, 2008).

With mining serving a historically significant role in the economy, current developments certainly warrant attention. The mining sector witnessed diverse performance, with a number of sub-sectors (e.g. platinum group metals) posting solid performances during the commodity boom of the 2000s, while the continued decline in gold production dragged down overall mining sector growth. The mining sector still employs more than half-a-million people and generates more than half of the country's export revenues.

In mining, the declining contribution of the gold sector is related to depleted mineral resources. Deeper-level mining is also seeing labour replaced by technology. The resultant decline in unskilled employment has exacerbated poverty and inequality in labour sending areas – primarily the former bantustans. Mining sectors on the rise, such as platinum, are less labour-absorptive.

Manufacturing's share in GDP dropped from over 20 percent in 1994 to just over 12 percent in 2012, with related decreases in employment (RSA, 2014). Manufacturing output rose until 2008 before declining sharply; it is also the only sector that has not recovered since the third quarter of 2010 (Makgetla and Dicks, 2014). Yet its relative share of exports has risen. The main sectors that contribute to these exports are machinery and equipment, motor vehicles (including components for auto assembly), refined petroleum products and other chemicals.

The decline of manufacturing sector matters because the sector has the highest economic and employment multipliers of any sector with the backward linkages in manufacturing

pulling through inputs from primary and other manufacturing and services sectors and transforming them into higher-value added products, stimulating employment and economic linkages value chains. At the same time manufacturing provides an added impetus to employment and growth through forward linkages to downstream sectors, including services (the dti, 2014).

Manufacturing growth trends in the 2000s highlight interesting dynamics in employment creation. As noted by Simon Roberts and others (Roberts, 2004, 2013; Chabane et al, 2003), many of the fastest growing manufacturing sectors were resource or capital intensive. Hanival and Rustomjee (2010) highlight how growing sectors (e.g. glass and basic chemicals) are capital intensive, noting that though they may not create substantial employment, they do significantly affect manufacturing output. Kaplan (2013) further illustrates the impact of the increased role that services in the economy have had on employment in the "productive" sectors including manufacturing, infrastructure and agriculture.

Although manufacturing growth is important, manufacturing is also among the most inequitable sectors, with high disparities in earnings in part still a reflection of the apartheid division of labour – and its associated inequalities of remuneration. Growth in manufacturing without a change in these patterns of distribution would limit its potential for inclusive growth.

Manufacturing exports are highly concentrated, with the top 20 manufacturing sub-sectors (out of 120) accounting for 77 percent of South Africa's manufacturing export basket in 2012 and with the top five percent of South African export companies accounting for more than 90 percent of total exports (RSA, 2014). What is striking is that the main manufactured exports are from sectors dominated by previously highly protected and/or state-sponsored sectors – lending credence to the argument that the main exporting firms have developed historic capabilities that allow them export dominance, making them "super-exporters".

● Almost every manufactured item in the consumption basket of poor people was – and still is – produced by large, vertically integrated companies or conglomerates with a strong presence on the Johannesburg Stock Exchange

These high levels of concentration in manufacturing limit the scope for a small-scale manufacturing sector, which is largely missing from South Africa's economic profile. This has direct implications for economic inclusion, in terms of the scope for new entrants into markets.

A feature of the apartheid era was the reinvestment of mining profits into cross-holdings in other parts of the economy, in a context in which capital was not mobile, because of strong foreign exchange controls and sanctions. This investment was targeted at manufacturing for the domestic market – including the poor as consumers. Anglo American, for example, had large or controlling shares in South African Breweries, producing beer; Premier Milling, producing maize meal and flour; Hulets, producing sugar – among others. Almost every manufactured item in the consumption basket of poor people was – and still is – produced by large, vertically integrated companies or conglomerates with a strong presence on the JSE.

In most developing countries, the easiest entry point into markets for small producers is from local production for local consumption, where producers manufacture goods they use themselves and know their neighbours' needs. Similarly, for small farmers, the easiest way up the value chain to secure greater returns is through participation in small-scale agro-processing of local surpluses. In South Africa, the levels of concentration in the core economy mean that this avenue into markets is either closed or highly inaccessible. It is rare that small producers can compete on price or brand recognition.

As Philip (2010) argues, this creates a massive barrier to entry for small producers. In the South African context, in which black people were excluded from markets for so long, emergent entrepreneurs now find that this important market space has long since been

occupied. This constraint on small-scale manufacturing is an outcome of the levels of concentration in the economy, and is a factor that has driven so many entrepreneurs into retail activities instead: moving mass-produced consumption items from the core to the margins of the economy.

Opportunities for small producers in the South African economy are not therefore typically in local markets targeting poor consumers. Instead, they are in higher-value markets, targeting people (or companies) with higher levels of disposable income. In a context of high inequality, such markets are typically outside their own community – and often, outside their own experience.

Accessing these markets requires participation in business-to-business transactions and value chains, and a step-change in business sophistication compared to informal transactions in local markets, where entrepreneurs can draw on their own local knowledge and local networks. In a context in which, for historical reasons, there is already a low base of business networks, experience and skill, all of this poses major obstacles for new entrants, creating a gulf between entry-level black entrepreneurs and the economic opportunities that do exist (Philip, 2010).

The one sector that has seen growth in the post-apartheid period is the tertiary sector, with growth between 1994 and 2012 in retail, telecommunications, financial services and security. The financial services sector does not create large numbers of jobs, and these are high-skilled, in a context in which the unemployed are largely unskilled: an unfortunate mismatch. The low levels of employment in agriculture and its declining contribution have been noted, but in a context in which unskilled work is a major priority, limitations in the absorptive capacity of the agriculture sector pose a real problem for economic development.

● These high levels of concentration in manufacturing limit the scope for a small-scale manufacturing sector, which is largely missing from South Africa's economic profile. This has direct implications for economic inclusion, in terms of the scope for new entrants into markets



**tertiary sector** growth in retail, telecommunications, financial services and security

While noting the positive developments in industrial policy, a challenge remains the slow pace of recovery in global economic conditions, dampening growth prospects in South Africa.

Industrial policy will therefore continue to focus on significantly allocating more capital (investments) into labour-intensive, value-adding productive sectors as part of South Africa's New Growth Path. Given the country's growth performance, another key developmental issue is "sustainability" – whether South Africa can sustain positive growth for extended periods. Although growth has ups and downs like other cycles, sustaining it for a long period seems to be what separates growth miracles from growth laggards.

Berg and Ostry (2011) make the point that inequality matters in itself for influencing or determining the length of growth spells in a country. Other "variables" they highlight for extending growth periods include better political institutions, trade openness, stable real exchange rates, competitiveness and export structure and exposure to global finances through foreign direct investment and lower external debt. What matters for growth is its quality and duration. The issue of quality, or that growth must be "strong and inclusive" is already encapsulated in numerous policy frameworks, e.g. the Millennium Development Goals. Further to this, while growth is necessary for development, it is not the only condition; the fact that inequality has risen parallel to growth illustrates this. Growing inequality poses a threat to the very sustainability of growth and development (see World Bank, 2008 on all these points).

With manufacturing set as a key growth and employment driver by government's industrial policy, an interesting policy question arises as the sector is no longer a major source of employment creation globally, and in South Africa – with implications for IPAP and South Africa's growth prospects and potential.

## Policy responses to promote industrialisation and economic transformation

In response to these trends, government has initiated a series of policy responses, leading to the adoption of a rolling four-year Industrial Policy Action Plan (IPAP) by the dti, and the New Growth Path by the Economic Development Department.

IPAP is aimed at bringing about structural economic change in South Africa by leveraging state support for industrial development through value-added production focused primarily on manufacturing sectors.

IPAP promotes labour-absorbing industrialization, with a key focus on raising competitiveness and broadening economic participation. It aligns trade policy, investment and export promotion, industrial finance, public procurement and competition policy. IPAP is an attempt to bring manufacturing back to the forefront of South Africa's economy by targeting investments in high labour-absorbing sectors.

A key focus has been placed on sectors that can generate employment on a large scale while improving the production of relevant skills especially engineers and artisans. The New Growth Path, launched in 2010, is government's economic strategy aimed at enhancing growth, employment creation and equity. The New Growth Path complements the National Development Plan by identifying mass joblessness, poverty and inequality as the core challenges facing South Africa.

Hence, job creation (linked to better quality jobs) is at the heart of the economic strategy developed and driven by the Economic Development Department.

The New Growth Path has a target of creating five-million new jobs by 2020 focusing on areas and sectors with the potential for large-scale job creation backed up by a growing GDP. Five "jobs drivers" were unveiled as the core employment creating opportunities that the public and private sector should be targeting:

- Public investment in infrastructure
- Targeting more labour-absorbing activities in agriculture, mining, manufacturing and services
- Taking advantage of new opportunities in the knowledge and green economies
- Leveraging social capital in the social economy and the public service, and
- Fostering rural development and regional integration.

The New Growth Path highlights significant industrial linkages throughout the job drivers – infrastructure, which includes construction and intermediate inputs; agricultural and manufacturing sectors (where trade with foreign entities is common especially considering the need for expanded regional integration); and opportunities in new fields such as the knowledge economy and green industries. The construction industry features prominently in the job creation target given the extended public expenditure forecast on infrastructure projects. While agriculture (including agro-processing) and manufacturing were identified for their job creation potential as these two sectors are among the most labour-intensive in South Africa.



Photo: Chris Kirchoff, MediaClubSouthAfrica.com

### 3.4 The distribution of gains between capital and labour

*During much of the past century, a stable labour income share was accepted as a natural corollary or “stylized fact” of economic growth. As industrialized countries became more prosperous, the total incomes both of workers and of capital owners grew at almost exactly the same rate, and the division of national income between labour and capital therefore remained constant over a long period of time, with only minor fluctuations...An outpouring of literature has provided consistent new empirical evidence indicating that recent decades have seen a downward trend for the labour share in a majority of countries for which data are available (ILO 2013).*

When high levels of inequality in South Africa are invoked, the comparison is often made between Sandton and the nearby informal settlement of Diepsloot. But while the glass towers of Sandton are largely funded by corporate rather than private wealth, the role of corporate profits has tended not to

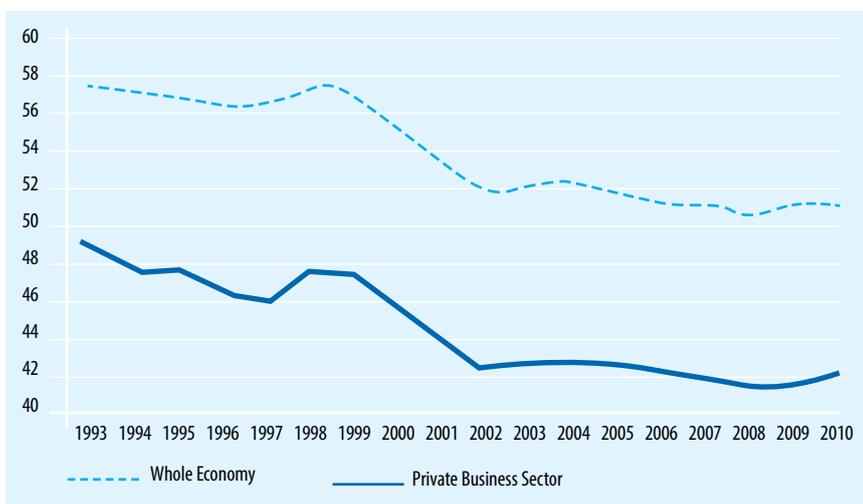
feature much in the analysis of inequality. Income inequality is measured in relation to private wealth. In this regard, labour market outcomes are the main driver of inequality – with the role of profits in private income at the top end of the distribution seeming surprisingly low.

What a focus on private income and on earnings overlooks, however, is the relative share of profits to earnings in GDP.

In South Africa, while productivity rose by 72.9 percent between 1994 and 2012, the wage share of GDP fell over the same period (Figure 5). This is in line with global trends, with a lower wage share of GDP correlating with the global rise in inequality. The work of Piketty has brought this dimension of inequality into sharper focus in the international debate. Closer examination of the relationship between wage income and corporate profits in the composition of inequality in South Africa is needed – rather than just the contribution of profits to personal income.

FIGURE 5

Wage share of GDP in South Africa 2011



Source: Reddy, 2014

# Spatial inequality

MANY OF THE racial and ethnic separations and inequalities inherent in the concept of “apartheid” – of being apart – took a spatial form and were enforced on those terms. This spatial inequality remains difficult to overcome, because it is structural in a very literal sense. Many of its elements are set in concrete, in where housing is located, where infrastructure and services exist and where roads lead, as well as where economic opportunities exist – or not – and where institutions are well established.

This dimension of inequality is highlighted because it is integral to the apartheid legacy, with a range of important social and economic dimensions affecting economic development and inclusive growth.

Under apartheid, race and class tended to converge – intentionally so. Insofar as black and white people (and coloureds and Indians, and Zulus and Sothos, for that matter) were kept apart by race and ethnicity, spatial divisions also overlaid class divisions. In a post-apartheid context, despite new forms of mobility that include the rapid growth of a black middle class, the convergence of class and space remains largely unchanged. So, while demographic change is taking place in the composition of the middle class and of the suburbs, the poor are often being left behind in the spaces where most black people continue to live, whether in urban or rural areas: because most poor people in South Africa are black (and most black people are still poor).

The area effects of concentrated poverty include inferior basic services, enhanced vulnerability to risks including crime, disease and the drastic shock of fire, the limited reach of social networks, particularly in labour market access, and the impacts of negative peer pressures and a lack of role models. This translates into poverty and inequality traps characterized by a lack of upward mobility which easily becomes inter-generational (Turok, undated).

In the World Bank’s South African Economic Update: Focus on Inequality of Opportunity, the Human Opportunity Index looks at the factors that most influence equity of opportunity for children growing up in South Africa. According to the report, location is a crucial determinant of access to opportunity, particularly where such opportunity is linked to infrastructure. This includes inter alia access to clean water, sanitation, and energy. “Children who grow up in townships, informal settlements and rural villages are at a distinct disadvantage” (World Bank 2012).

The spatial disadvantages of these places act as a brake on economic opportunity for those who live there, with “being apart” continuing to be a visible and material part of people’s experience of inequality in their day to day lives. This undermines a sense of social inclusion and equity, and on the chances to build any commonly-held consensus that society is fair.

The role of spatial inequality cuts across all the other dimensions discussed in this section (as does race and gender), but its relevance is so specific to the South African story that it is necessary to foreground its continued role in reproducing other dimensions of inequality. It has distinct rural and urban characteristics.

## 4.1 Spatial inequality in the rural context

Reference has already been made to the role of the 1913 Land Act as a defining moment for land dispossession as well as in shaping the future of South African labour markets. This massive dispossession of land provided the conditions for the migrant labour system, shaping the South African labour market in ways still evident today, and giving labour markets a spatial dimension.

Today, the former bantustans still largely perform the role of labour reserves and act as sites of social reproduction. These areas continue to be associated with high levels of disadvantage. They score the worst on every dimension of the multiple deprivation

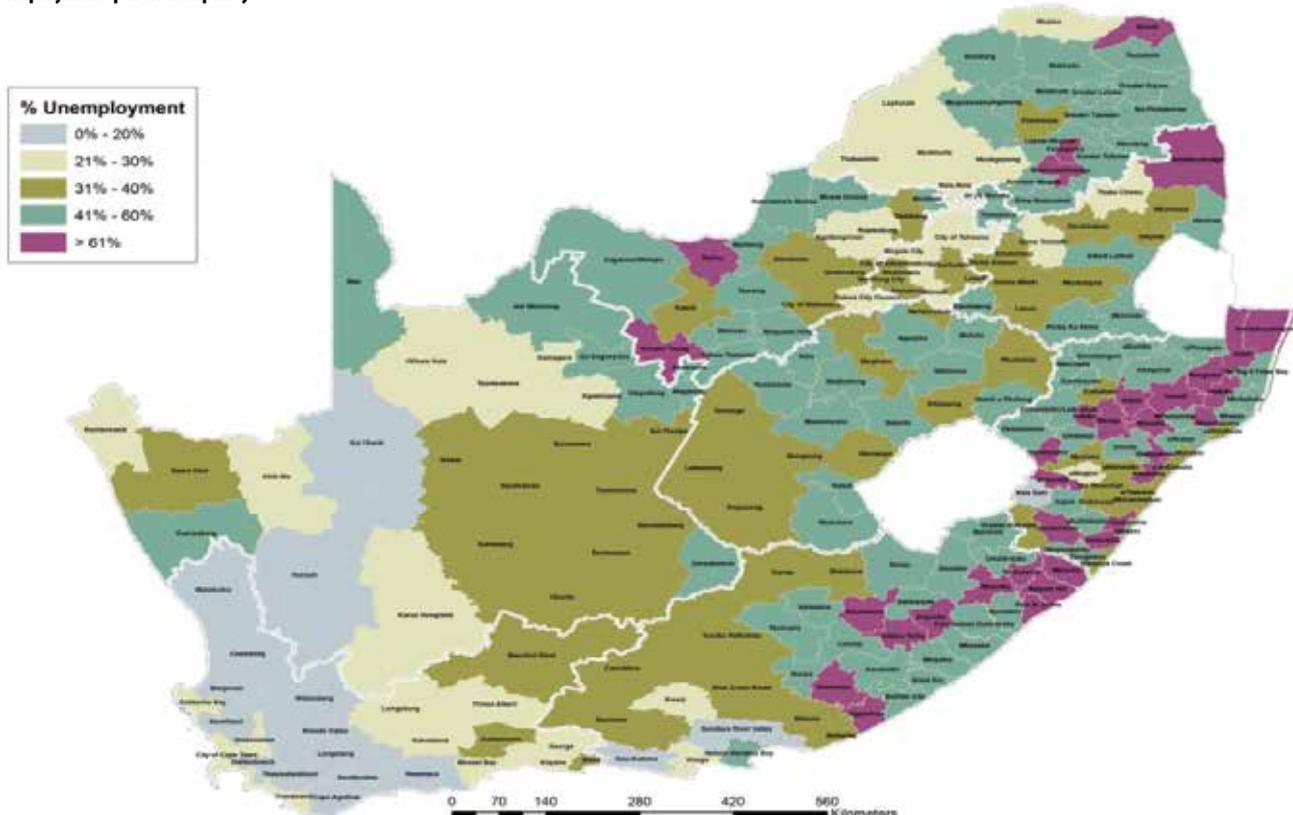
index for unemployment, nutrition, health outcomes, school outcomes, access to public services, clean water, energy, sanitation and decent housing. (Leibbrand, 2013). The spatial concentration of unemployment, for example, is illustrated in Figure 6. Its highest levels of concentration correlate closely with former bantustan areas.

High levels of migrancy continue, with population demographics showing disproportionate numbers of women and children living in former bantustan areas. A factor keeping women in these areas is that securing and retaining access to land and the right to establish a homestead under communal land tenure systems depends on the family continuing to be resident. Maintaining access to such rights for the wider family often ties women to these areas, and, in the absence of equivalent rights in urban areas, provides an incentive for patterns of migrancy to be maintained, at significant social and economic cost.

Yet, while women are the backbone of these rural communities, it is in these areas that gender rights and their application are most ambiguous and contested.

FIGURE 6

### Unemployment per municipality



Map produced for TIPS by A Esterhuizen using Stat SA 2011 data

Black women and girls in former bantustan areas are the **most disadvantaged** people in the country for many crucial social and economic indicators



In former bantustan areas, systems of traditional authority under the auspices of traditional leaders continue in a sometimes uneasy relationship with the constitutional right to gender equality. While the Constitution recognizes “living custom” as a source of authority (Thornberry, 2013), some aspects of living custom impinge on the constitutional rights of women and girls. In a series of recent battles, the courts have upheld these rights despite counter-claims that this breaches the commitment to “living custom” in the Constitution. Important as these court decisions are, the courts are often least accessible to the most vulnerable and disadvantaged.

It is in this context that the Traditional Courts Bill met with such opposition – leading to its temporary withdrawal, after rejection in the National Council of Provinces in 2013. The Bill aimed to establish a separate set of courts with jurisdiction in those areas where traditional authority is still exercised by chiefs – effectively, in former bantustans. The Bill was criticized for institutionalizing a parallel legal system in which rights embedded in the Constitution were at risk of being subordinated to “living customs” that do not recognize such rights.

Black women and girls in former bantustan areas are the most disadvantaged people in the country for many crucial social and economic indicators. Elements of customary practice reinforce such disadvantage, with this an area of ongoing contestation in South Africa’s democratic institutions:

So, even as parliament and the courts have granted women equal rights within the family and to inheritance and recognition as traditional leaders, a ‘stubborn persistence of patriarchy’ means that these rights remain contested in the public and private spheres. Women’s rights of access to communal land and within customary courts remain sites of struggle between the claims of traditional leaders and those of community members, including women. Much of this currently centres on the nature and extent of traditional (male) power over land, property and community (Albertyn, 2009).

While levels of disadvantage between former bantustan areas and the rest of country are clear, there are also high levels of inequality within what are now called the commercial farming areas, as a consequence of a history of low wages and poor working conditions on the farms.

Rural poverty in these areas has, however, been exacerbated by the evictions following the

promulgation of The Extension of Security of Tenure Act. This has led to the rapid development of informal settlements on the perimeter of many small rural towns, escalating social tensions and placing significant pressure on basic services. While residents of former bantustan areas typically have some kind of access to land to build a homestead and a degree of tenure security, the evicted farmworkers have neither. These rural informal settlements represent “the people left behind”: lacking the resources to migrate to the cities, they are trapped on the outskirts of rural towns (Cross, 2009).

## 4.2 Spatial inequality in the urban context

The 1913 Land Act achieved the purpose of making cheap labour available to the mines, and so began the influx of black people to the cities – and with it, the advent of what was called “influx control”. This concept underpinned the pass laws that governed South Africa’s migrant labour system. This was designed to link black people’s rights to live in urban areas to their contract of work, on the basis of an underlying logic that the reserves or bantustans were their home – and that they should not be encouraged – or allowed – to live in urban areas as permanent residents, nor to bring their families to live with them.

Urban development policies had the dual aim of entrenching racial separation at the same time as securing a ready supply of cheap labour. This led to the development of the uniquely South African definition of a “township” as an urban area designated for black people that had to be at a distance from the white town, separated by a buffer area, with only one access road for security control purposes, and with housing provided only on a rental basis. Townships were designed as dormitory towns – with no business districts, no internal economic logic, and limited services. All of these were instead located in the nearest “white” town (RSA, 2009).

This definition of a township shaped the development of urban South Africa, in a way characterized as “exerting control through form”:

The key focus of the specifications set down for Townships was to enable the government to assert its control. Row upon row of identical dirt streets radiating from a central hub, line upon line of drab, cheap, uniform houses – a colourless mind-numbing monotony. Through regimentation and uniformity the government sought to establish a firm control that could not be challenged (Bonner and Segal, 1998).

This configuration of urban areas was inherited at the end of apartheid. Settlement patterns were literally set in concrete; existing housing stock could not be moved, and in the face of massive housing backlogs, could not be abandoned either. Policy errors and oversights have, however, combined to reproduce and even in some instances exacerbate this inherited pattern of urban spatial inequality, with significant negative economic implications, particularly for the poor.

The driver of this process has been one of post-apartheid South Africa’s most ambitious redistributive policies, a public housing programme which provides a free housing asset for people below a certain income threshold. This programme was initially known as the RDP subsidy, a reference to the Reconstruction and Development Programme of the first democratic administration in 1994 and is now part of the Department of Human Settlements’ Breaking New Ground policy.

The initial target was to build a million RDP houses. Over the last twenty years, more than 2.8 million RDP housing units have been built, and more than 876 774 serviced sites handed over, giving about 12.4 million

people access to accommodation and a significant fixed asset. Over 56 percent of these subsidies went to households headed by women (RSA, 2014).

This massive asset transfer programme has, however, been criticized for the poor quality of some of the housing construction and for the focus on the number of houses built – without linking this to wider planning for sustainable human settlements: with inadequate integration of social services, recreational spaces, or space for local business activity. These housing developments have also often been located far from economic opportunities (Figure 7) without adequate planning for public transport – reproducing the spatial patterns of apartheid (Zack, 2008). The process of building state housing has also not been able to keep up with the rate of urbanization and household formation, with informal settlements becoming a permanent feature of the urban landscape.

Another problem is the delay in the registration of properties and a backlog in issuing title deeds. Many of the beneficiaries do not have proof of ownership for their properties, which has eroded the potential value of this massive asset transfer by the government. A study on the asset performance of the government-subsidized stock showed that, of an estimated 2.94 million units delivered, only 1.44 million were visible on the deeds registry. This means that only about 50 percent of houses delivered had been formally registered (Shisaka, 2011).

Among the consequences is that resale of property is difficult, and this sometimes takes place without formal transfer of title, making proof of ownership even more complicated – and people cannot use the asset as security.

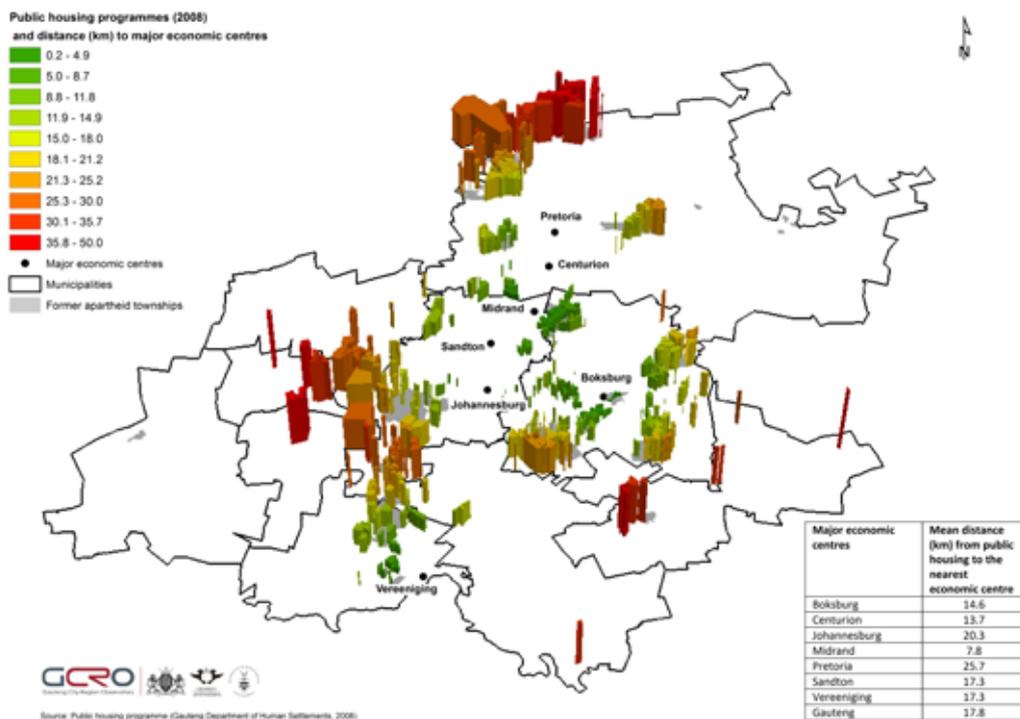


only of houses  
delivered have  
been **formally**  
**registered**

Shisaka, 2011

FIGURE 7

Proximity of RDP housing to major economic centres



Source: Gauteng Department of Human Settlements (July 2008 Housing Programmes)

The construction of affordable housing on cheap but poorly located land may have responded to short-term budget constraints affecting municipalities under pressure to deliver, but these decisions have had longer-term social and economic costs in a range of ways:

- Establishing housing settlements far from existing infrastructure has raised the upfront and ongoing costs of delivering basic services such as water, sanitation, electricity and roads
- The distances from economic opportunities create upward wage pressures in the economy; the high costs of transport erode the purchasing power of wages, and raise the reservation wage
- Transport costs are often cited as a constraint on work-seeking for unemployed people with limited incomes
- The time spent traveling to work has social costs, raising stress, and limiting time for recreation and parenting.

Policy responses to urban spatial inequality

By 2004, the Department of Human Settlements had launched a new housing policy called Breaking New Ground, which proposed “utilizing housing as an instrument for the development of sustainable settlements, in support of spatial restructuring” (Quoted in RSA, 2011). According to the policy:

After the 1994 elections, Government committed itself to developing more liveable, equitable and sustainable cities. Key elements of this framework include pursuing more compact urban form, facilitating higher densities, mixed land use development, and integrating land use and public transport planning, so as to ensure more diverse and responsive environments whilst reducing travelling distance. Despite all these well-intentioned measures, the inequalities and inefficiencies of the apartheid space economy have lingered on.

Breaking New Ground renewed the focus on achieving these goals. This has included support for informal settlement upgrading (where such settlements are well located), through the National Upgrading Support Programme.

The eradication of spatial inequality was also identified as a national priority in the National Development Plan. Located in National Treasury, the Neighbourhood Development Programme’s Urban Network Strategy is aimed at leveraging private sector investment to transform the urban spatial economy, creating development corridors between current centers of economic activity and marginalised residential areas, with public transport as a critical element. The process focuses on public infrastructure investment, fiscal and regulatory development incentives, and coordinated urban management in targeted locations.

## Despite the formal rights framework, social practice often lags behind



# Inequality in opportunities and human development outcomes

## 5.1 The rights framework

ALTHOUGH RACISM, gender-based inequality and other forms of discrimination are far from eradicated, the achievement of equal rights for all people in society, within the wider framework of the Declaration of Human Rights and the rule of law remains a deeply significant achievement, protected and promoted through instruments that include the Constitution, the Chapter Nine state institutions set up to safeguard constitutional democracy, as well as laws, policies and practices that attempt to remedy past and present injustices. The turning point in institutionalizing these rights was the advent of democracy in 1994. While access to such rights and their application may be uneven, their existence in law represents a systemic break with the past, providing an important framework within which to advance meaningful levels of social equity – with the added element of social justice implied in the term.

This is the necessary starting point for equality of opportunity, providing the basis for a set of intangible features within a society that include dignity and agency, and can't be reduced to levels of income. The power of this equality of rights – and the contrast it provides with the past – is at its most visible in the queues of people lining up to vote in the election process. In terms of social transformation, a significant level of diversity at the level of leadership and representation has become normal in public life. The black

woman judge presiding over the trial of Oscar Pistorius for killing his girlfriend barely elicited comment in South Africa. Such a scenario was unprecedented earlier in Judge Thokozile Masipa's own lifetime.

Despite the formal rights framework, social practice often lags behind. The levels of violence against women and children in South Africa all too graphically illustrate the continued imbalances in power that limit the reach of society's formal rules, both in public spaces and in the personal domain. Again, women and children are most at risk in contexts of poverty – where they have to walk long distances to attend school, or to fetch water and fuel; where they return home from work – or work-seeking – after dark; where they cannot afford childcare; where even their homes provide limited security from incursions (and where the threat to their security often lies inside those same doors); and where their recourse to police services or the protection of the courts is more limited.

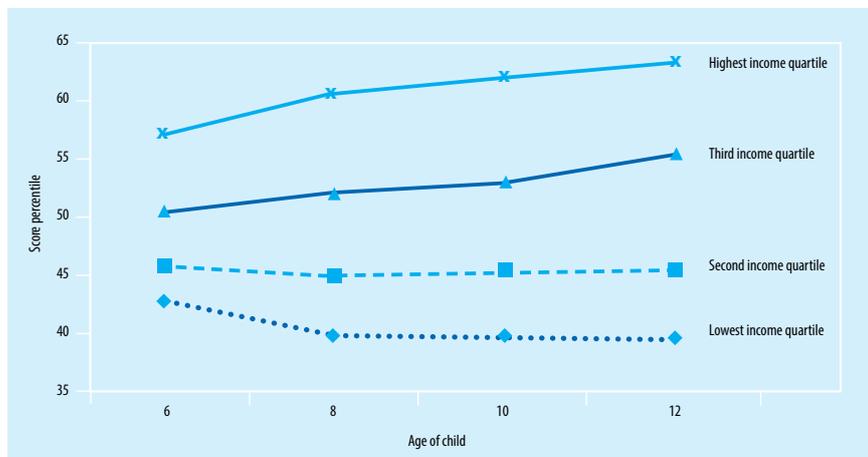
Despite South Africa's recognition of gay rights, gay people still face threats and violence in many contexts. People with HIV and Aids have had to fight against stigma and discrimination, people with disabilities still experience forms of social exclusion, and xenophobia has reared its ugly head. As important and necessary as the legal frameworks are, they are not sufficient in eradicating discrimination and prejudice. While South Africa has made remarkable strides, this is still a work in progress.

## 5.2 Drivers of deprivation and disadvantage

The highest levels of social consensus that inequality is bad for society relate to inequality of opportunities: where, for reasons of circumstance or discrimination, some people are denied access to the basic necessities of life, such as water, sanitation, shelter, energy, or health services, or to the opportunity to reach their potential through access to education. Education holds a special place in the literature on opportunities, and for good reason. But, as important as it is, international literature has drawn attention to the role of socio-economic status in establishing an opportunity gap even before children start school. Figure 8 illustrates how wide this gap already is for children aged six in the context of schools in the United States, and the impact of this on outcomes by the age of 12 (Taylor, Van der Berg, Reddy and Van Rensburg, 2011).

FIGURE 8

Academic achievement by socio-economic status and age



Source: Heckman, 2006

Performance improves for those in the highest income quartile, and worsens for those in the lowest deciles. While it appears that the schooling system is failing poor children, the variances in performance over time are actually overshadowed by the impacts of initial advantage and disadvantage – and given their dramatic impact on initial outcomes, these may well be playing a role in later school performance also.

Inequality of opportunity takes a toll very early, playing a crucial role in the inter-

generational reproduction of inequality. A range of forms of deprivation drive such disadvantage. In the South African context, Finn, Leibbrandt and Woolard (2013) have developed an index of multiple deprivation that provides a basis for identifying such drivers. Figure 9 illustrates how these drivers of deprivation have been reduced in South Africa in the post apartheid period.

In its Human Opportunities Index, the World Bank explores what circumstances shape inequality of opportunity in some of the same categories. Location is the most pronounced factor for opportunities related to infrastructure, such as safe water on site, improved sanitation and electricity, with people living in townships, informal settlements and former bantustans most likely to be disadvantaged. Gender does not come through strongly as a variable because access is assessed at the household level. The children most likely not to complete primary school or be exposed to early childhood development, and to lack access to safe water on site, are overwhelmingly black Africans under household heads who have limited or no education and live in rural areas. School attendance for under-16s and access to telecommunications are near universal (World Bank, 2012).

Within this range of drivers of deprivation and opportunity, the role of education and health receive more focus in the following two sections.

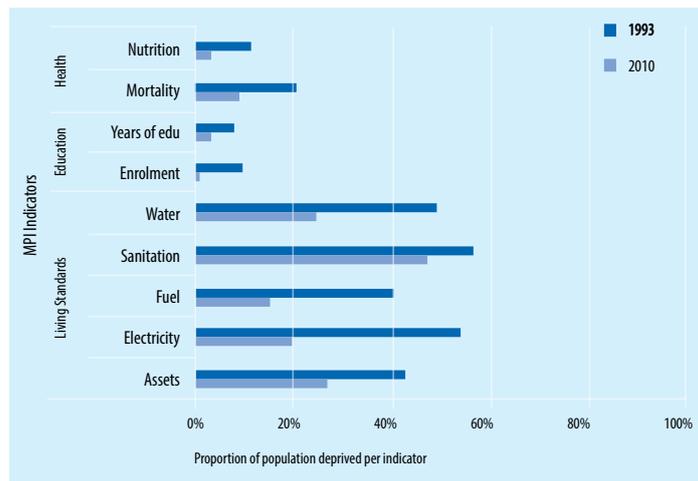
## 5.3 Inequality of opportunity in education

Apartheid introduced different education systems for different racial groups, with an inferior curriculum for black students, in the form of bantu education. In 1954, in explaining the rationale for bantu education, Dr Hendrik Verwoerd, later Prime Minister, described black people as “hewers of wood and drawers of water”, and famously said:

There is no place for [the Bantu] in the European community above the level of certain forms of labour ... What is the use of teaching the Bantu child mathematics when it cannot use it in practice? That is quite absurd. Education must train people in accordance with their opportunities in life, according to the sphere in which they live (Lapping, 1987).

FIGURE 9

Drivers of deprivation among the population



Source: Finn, Leibbrandt and Woolard, 2013

In this context, opportunities were unequal by design. As a consequence, black students were not taught mathematics beyond basic arithmetic. This policy decision entrenched a key form of educational disadvantage, with far-reaching consequences to this day.

Racial segregation of schools and the inferior curricula were rapidly abolished after 1994. Institutionally, this involved amalgamating the education departments responsible for each race group (black, white, coloured and Indian) as well as the education departments in the former bantustans to create one integrated system, run through nine provinces. This was not a simple task.

South Africa spends about six percent of GDP on education, on par with the OECD average (OECD, 2013). Spending has been biased to the poorer schools, with no-fee policies covering 80 percent of schools by 2013 (RSA, 2013). Recognition of the importance of early childhood development has informed a focus on provision of access to Early Childhood Development Centres and the introduction of Grade R (pre Grade 1) By 2011, 67 percent of five year olds were enrolled. Access to Early Childhood Development poses a bigger challenge, with uneven access and quality (Atmore, Van Niekerk and Ashley-Cooper, 2012). South Africa has, however, achieved near-universal school enrolment, with over 98 percent of children between the ages of seven to 15 attending school (Stats SA, 2012a). Yet the dropout rate after that point is high.

This investment in education has not yet had the anticipated results in turning around a situation of deep dysfunction in the formerly black schools. Spaull argues that “ongoing informal institutions of disorder, distrust, rebellion, and lack of cooperation have undermined efforts to create an appropriate culture of teaching and learning in these schools”. The result is a schooling system whose outcomes are so unequal they have been described as “bi-modal” (Spaull, 2013).

This is illustrated in Figure 10, which shows the distribution of Grade 4 numeracy achievement, separated based on schools that were historically black (former department of education and townships schools) and schools that were historically white. About 75 percent of students in the country attend the former.

While formerly white schools now have integrated student bodies, they are typically located in more affluent, areas and most students attending them are from higher income deciles.

The overlay of race and socio-economic status is illustrated by the distribution of reading performance in Grade 6. Based on school wealth quartiles this has a similar distribution when disaggregated by the former racial categorization of schools (Figure 11).

FIGURE 10

Distribution of Grade 4 numeracy achievement by historical education department (Data NSES 20017/8/9)

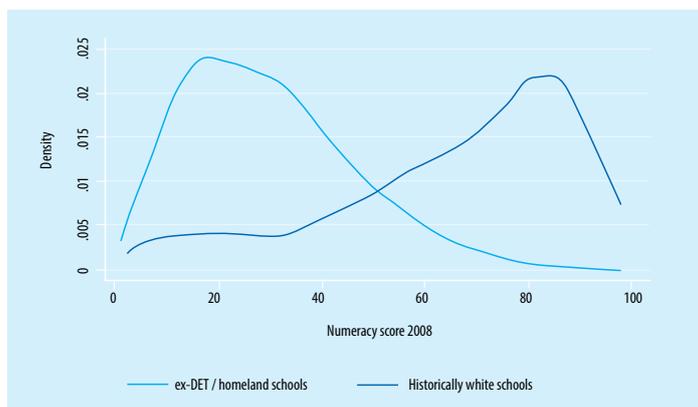
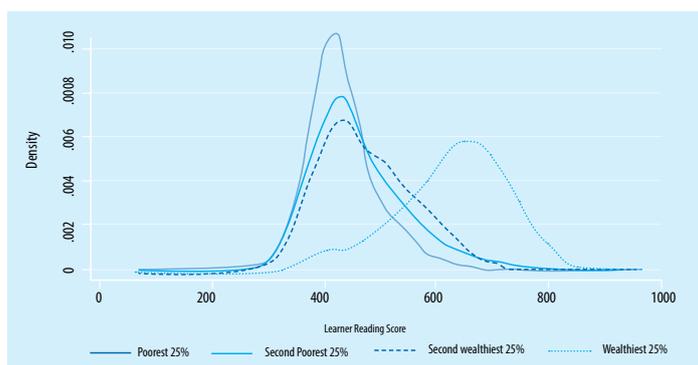


FIGURE 11

Distribution of Grade 6 reading performance by school wealth quintile (Data: SACMEQ III 2007)



Source: Spaull, 2013

26.6%

The results of a 2012 survey indicate **an increase in stunting** in children under the age of three from 23.4 percent to 26.6 percent

Sender, 2014

Starting in lower grades, improved performances are, however, becoming evident year on year, raising hopes that improved outcomes will start to flow through the system. In addition, despite the overall patterns, sites of excellence do exist in some of the poorest areas, where principals and teachers defy the odds to deliver quality outcomes.

The net effect of inequalities in education outcomes has been low pass rates in Grade 12 and constraints on the throughput in universities. Despite shifts in the demographics of enrolment, the universities have a 49 percent dropout rate.

Overall, inequalities in education translate into significant inequality of opportunity, and continue to correlate with spatial inequality and the distribution of poverty, in turn correlated with race. The net effect is the reproduction of patterns of racial inequality in education outcomes, which in turn impact on labour market outcomes – an issue explored further in Section 6.

## 5.4 Health and inequality

Child health and nutrition are critical variables impacting on wider opportunities and outcomes. While the percentage of people going hungry has been cut by more than half, and South Africa has met its Millennium Development Goal target for this, the levels of stunting remain high. The results of a 2012 survey indicate an increase in stunting in children under the age of three from 23.4 percent to 26.6 percent, as well as a large increase in the incidence of severe stunting over the same period (Sender, 2014).

Stunting increases a child's vulnerability to disease, and the consequences of inadequate nutrition are severe.

Even in mild cases, malnourishment can cause direct and irreversible structural damage to the brain, impair motor development, cause significant development retardation, affect cognitive development, impair exploratory behaviour, impair learning abilities and educational attainment and can have lasting impacts on their health. (Atmore et al, 2012).

Longitudinal research has shown that malnourishment in childhood is directly related to later negative adult outcomes, in relation to educational achievement, a higher risk of adult diseases and reduced economic productivity (Atmore et al, 2012).

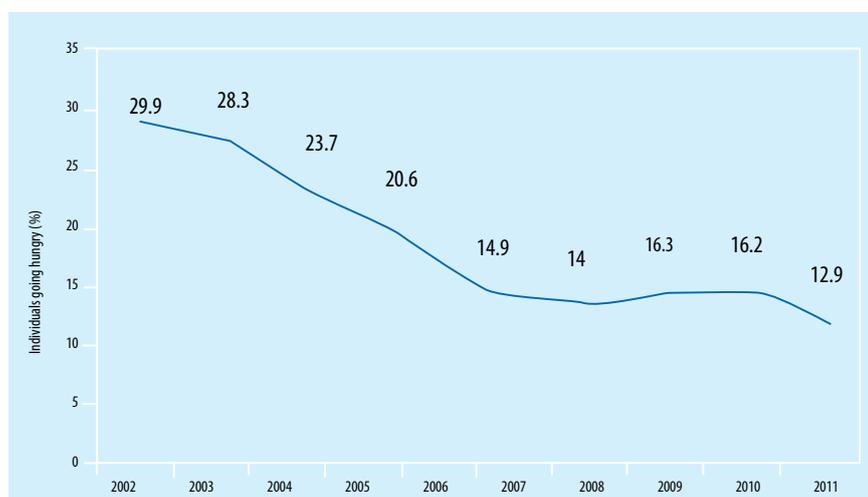
South Africa also has a rising number of maternal orphans (Stats SA, 2014b). This affects rural women in particular, where preventable deaths from direct obstetric causes are highest, as a result of lack of blood for transfusion, inadequate emergency support, poor referral systems, insufficient intensive care unit facilities and a lack of appropriately trained staff to manage obstetric emergencies (Sender, 2014).

Sender argues that women in rural areas are also often subject to coercive and patriarchal forms of rural authority, in which their ability to assert their sexual and reproductive rights, as well as their rights to health, may be compromised.

Stuckler, Basu and McKee (2011) find that, despite policy commitments to health equity, the health funding model takes only partial account of the relative disease burden in different areas, and that regions with the capacity to spend funds tend to benefit more relative to those with greater health needs. As a consequence, "historical infrastructure

FIGURE 12

Percentage of individuals going hungry



Source: RSA, 2014

inequalities may have created an infrastructure-inequality trap, in which the distribution of funds to those with greater 'absorptive capacity' exacerbates inequalities".

In addition, because former bantustan areas have been labour-sending areas for the mines and other industries, the costs of occupational injuries and diseases is higher in these areas. This includes, for example, high rates of tuberculosis. Migrant labour has also increased vulnerability to HIV and Aids, with the burden of this disease also unevenly borne in former bantustan areas and informal settlements. While today, South Africa has rolled out extensive anti-retroviral treatment, the epidemic took an enormous toll in poor communities during the government's denialist phase, with significant negative impacts on the assets and incomes of affected households, exacerbating poverty and inequality in ways that have not been adequately measured.

Health and the burden of disease is also inextricably linked to access to basic services, including in particular access to clean water, sanitation and shelter.

## 5.5 Inequality of opportunity and institutions

Why, when policy and budgets are geared towards creating greater equality of opportunities, are the results so consistently unequal? The answers to this lie largely in the role of institutions, making this a necessary area for increased focus that goes beyond capacity as the default explanatory variable. What is it about the institutional context that is contributing to the consistent reproduction of inequality in all the main areas that comprise "equality of opportunity"?

For an answer, it is essential to look beyond the transition to democracy as a key moment in which state power was transferred. There is a need to look at the administration of such power and the incentives and disincentives that drive current processes of government administration, looking at systems as well as the functioning of elements within those systems, and the roots of highly uneven outcomes.

The starting point has to reflect back on the nature of the challenge of transforming the apartheid state.

By the end of apartheid, the territory of South Africa was governed and administered by an astonishingly

complex puzzle of governments, agencies, departments and legislatures. Over and above the Dr Seuss-like arrangements of the Tri-Cameral parliament – three houses of parliament, a President's Council and the myriad of white and black, local authorities – the homelands (Lebowa, QwaQwa, Bophuthatswana, KwaZulu, KaNgwane, Transkei and Ciskei, Gazankulu, Venda and KwaNdebele), collectively, consisted of 14 legislatures and 151 departments (Picard, 2005, quoted in Chipkin and Meny-Gilbert, 2011).

The creation of a post-apartheid administration had to rationalize this system, at the same time as dealing with the politics of absorbing incumbent administrators who had been responsible for the administration of apartheid. In the core apartheid state machinery, these officials were mainly white men; in the former bantustan areas, such officials were mainly black.

This included nearly 650 000 homeland officials often with rudimentary qualifications, formed and apprenticed in dysfunctional administrations that operated less according to standing orders and impersonal processes and more through patronage and personal rule (Chipkin and Meny-Gilbert, 2011).

The bantustan administrations had to be absorbed into the new provincial administrations, and in the context of the imperatives of affirmative action, many such officials were also absorbed into other levels of the post-apartheid state (Chipkin and Meny-Gilbert, 2011).

In discussing corruption in post-apartheid South Africa, Hyslop finds that while the phenomenon has been relatively contained at the level of national departments, the provincial governments have been "severely afflicted", with "a clear correlation between the level of systematic corruption and the degree of administrative continuity with the old homeland administrations" (Hyslop, 2005 quoted in Chipkin and Meny-Gilbert, 2011).

While the richer provinces (Gauteng and the Western Cape) did not have to absorb any former bantustans, some of the poorest provinces have had to absorb several. This has compounded the institutional challenges they face and deepened the spatial dimension of performance outcomes.

This dimension of governance and administration is simply one of the more apparent of the institutional factors underpinning inequality of outcomes in relation to human opportunities. This is an area in which a great deal more work is required.

## Race remains the dominant factor in relation to income inequality in South Africa



# Income inequality in South Africa

## 6.1 The big picture

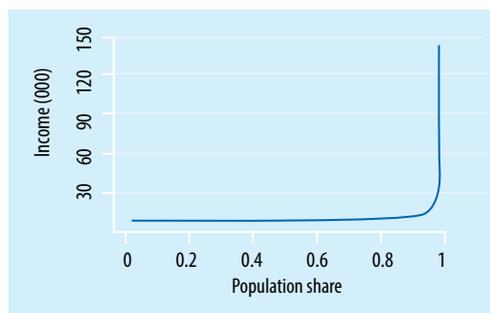
WITH A RECORDED Gini coefficient for income inequality of 0.69 in 2011, South Africa is the most unequal society in the world (among those societies that measure inequality) (Stats SA, 2013: 14. Gini co-efficient calculated on income per capita). That South Africa was highly unequal in 1994 was no real surprise. More surprising is that – despite the wide range of policies intended to transform this reality – inequality rose from 0.64 to 0.69 by 2005, according to Borhat and Van der Westhuizen (2012). According to Statistics South Africa, it reached 0.72 in 2006 before dropping back to 0.69 by 2011.

Different measures of inequality reinforce the same picture. The Pen’s Parade presents the distribution as a “parade” of the population, from poorest to richest (Figure 13). A feature of this remarkable pattern of inequality is the exceptionally steep rise in incomes at the very top of the distribution.

Gabriel Palma’s work has highlighted that across 131 countries, the middle deciles in the population consistently control approximately 50 percent of national income, with low levels of inequality within this band. He argues that the real differentiation between different types and scales of inequality comes from measuring the ratio of national income held by the top 10 percent of the population relative to the bottom 40 percent. In South Africa, this ratio is 8.5: making South Africa a global outlier once again (Palma, 2014).

FIGURE 13

Pen’s Parade of income, 2006



Source: Tregenna and Tsela, 2012

Race remains the dominant factor in relation to income inequality in South Africa. In 2012, the average income for households headed by black Africans was R69 632, while the average for white-headed households was more than 5.5 times this amount, at R387 011 (Stats SA, 2012b).

FIGURE 14

Average annual household income by population group of household head (2012) – in Rands



Source: Stats SA, 2012b



...of national income controlled by the middle deciles across 131 countries

Palma, 2014

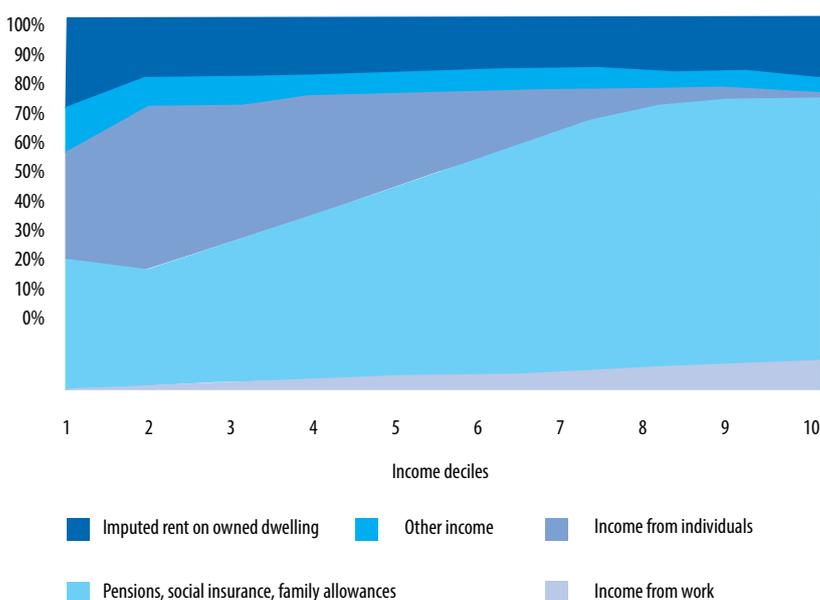
In a context of disputes over the reliability of available datasets, the extent to which the main driver of increasing levels of income inequality in the post-apartheid period has been inequality between races, or rising inequality within racial groups is being debated.

Studies using either the 1996 and 2001 Census data or the 1995 and 2000 Income and Expenditure Survey data have found an increase in the contribution of within-group inequality driven to a large extent by increasing inequality within the black African population (See Hoogeveen and Ozler, 2006; Leibbrandt, Woolard, McEwan and Koep 2005); using the Theil index, Borat and Van Der Westhuizen (2012) find instead that by 2005, within-group and between-group inequality contributed to aggregate inequality in almost equal measures.

The breakdown of income components by deciles in Figure 15 illustrates the extent to which different types of income contribute to incomes in the different deciles. Social grants play a crucial role in the poorest deciles, while income from wages and remuneration remain the biggest contributor to overall income inequality, making the role of labour markets in inequality an issue.

FIGURE 15

#### Income components by deciles, 2011



Source: Stats SA, 2012b

## 6.2 Income inequality and the role of the labour market

### 6.2.1 Key labour market trends

There is consensus that labour market outcomes are the leading factor driving income inequality; Leibbrandt, Finn and Woolard (2012) attribute 85 percent of income inequality to the impact of labour market income in 2008.

The accepted centrality of labour market outcomes has led to a tendency for policy discussion on income inequality to focus on labour market policy. Important as this is, outcomes in labour markets are driven, to a large extent, by factors that fall outside of labour markets, on both the demand and the supply side. Labour market policy governs the interface between the demand and supply of labour, but the main determinants of the composition of such demand as well as of the characteristics of labour on the supply side lie at least partly – and often entirely – outside the scope of labour market policy. For example, most of the dimensions of inequality already discussed in this paper have impacts on outcomes in labour markets. This includes, for example, the financialization of the economy, the lack of private investment, the sectoral composition of the economy, spatial issues and access to opportunities. These all impact in different ways on unemployment, the composition of labour demand and the characteristics of labour supply. Yet the extent to which these dimensions of inequality are in turn influenced by labour market policy is highly variable.

Despite a high level of agreement on the significance of labour market outcomes in the composition of income inequality, debate over the drivers of different dimensions of such inequality continues. Even while overall measures of such inequality may be fairly constant, elements of underlying change are taking place. This includes changes in the composition of labour market participation, in the returns to education and its demographics.

Figure 16 illustrates the changing composition of South Africa's labour force at an aggregate level over the last twenty years.

Figure 16 illustrates that the number of unemployed and discouraged work-seekers has grown by 2.2 million from 1994 to 2013, while the number of people in employment has grown by 5.7 million. This is not jobless growth. Yet the combination of successive economic crises coupled with population growth and increased levels of participation in the labour force all combine to mean that this absolute growth in employment has not been enough to bring the rate of unemployment down.

The increases in labour force participation were mainly by black Africans, particularly women, as well as youth with low levels of education. Women's participation in the labour market rose from 39 percent in 1993 to 53.8 percent by 2008 (Leibbrandt, Woolard, Finn and Argent, 2010).

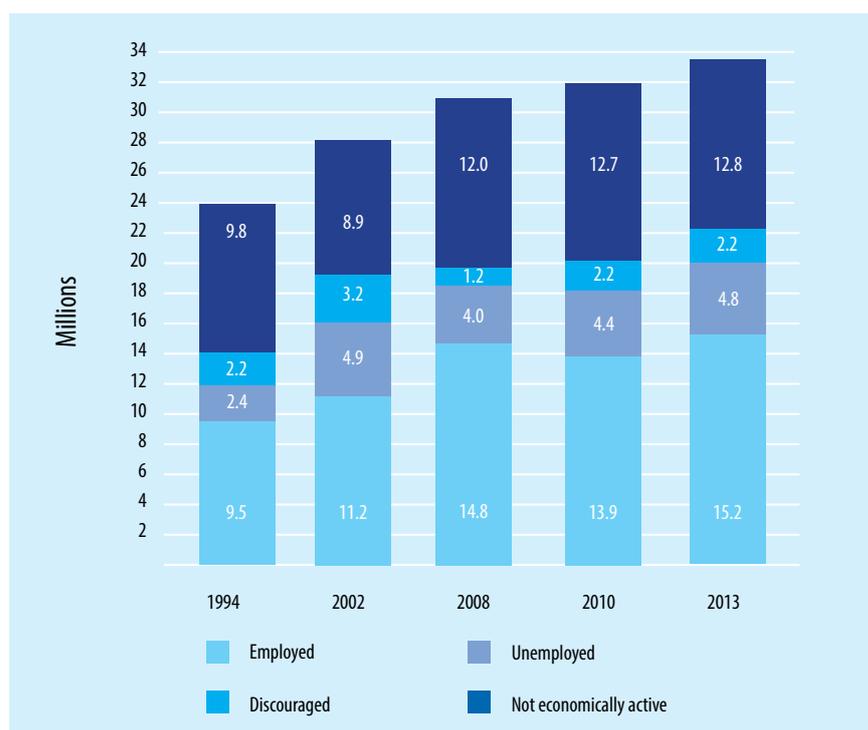
So, labour market outcomes are driving income inequality; but what are the critical drivers of this outcome? There are two main factors: the distribution of jobs, and the wage formation process (Leibbrandt et al, 2010; Van der Berg, 2010; Tregenna 2011).

Tregenna (2011) finds that the bulk of earnings inequality can be attributed to the rate of unemployment.

Static and dynamic decompositions of earnings inequality by employment status reveal the centrality of unemployment in accounting for both the level and trend of earnings inequality. The distribution of employment in the formal and informal sectors is found to be of lesser importance in explaining earnings inequality, as is wage dispersion within each of these categories (Tregenna, 2011).

**FIGURE 16**

**Labour force status of working age population, 1994-2013, in millions<sup>2</sup>**



Sources: StatsSA (2012)

### 6.2.2 Unemployment as a driver of earnings inequality

The distribution of unemployment reflects the expected faultiness of South African inequality, in terms of race, gender and location, with age an additional factor.

**TABLE 2**

**Unemployment by race and gender**

BY GENDER	NARROW (%)	EXPANDED (%)
<b>Women</b>	<b>26.3</b>	<b>37.7</b>
Men	22.4	30.7
<b>BY POPULATION GROUP</b>		
African	27.1	38.5
Coloured	23.0	26.8
Indian/Asian	12.5	17.1
White	7.2	8.4

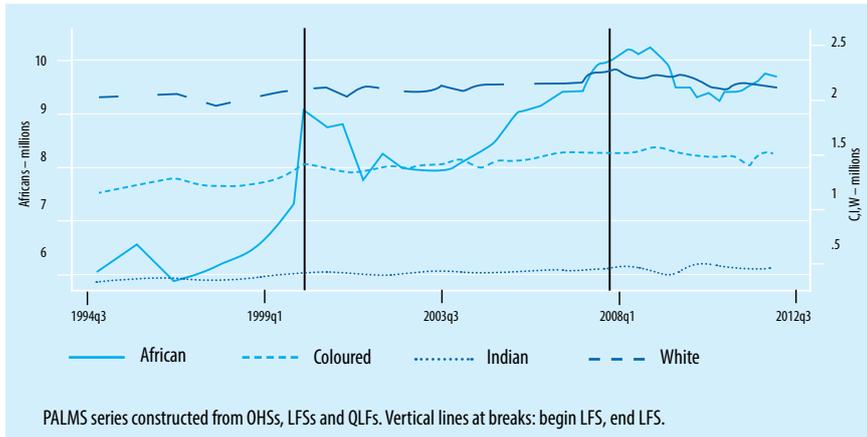
Source: Stats SA, 2012c

<sup>2</sup>1994 is taken as the starting point, because comparison with the apartheid period is limited by data constraints: in particular the fact that all unemployed Africans in the bantustans were deemed to be employed in subsistence agriculture in this period. The 1994 figures represent the first attempt to overcome this weakness; it can be assumed that challenges in doing so contribute to some extent to gaps in statistical accuracy in the early post-apartheid period. This applies to many statistical issues, and is a cautionary note relevant to many contexts in which there are sharp shifts in data in early post-apartheid labour market trends.

While unemployment affects black Africans the most, they have gained the most from changes in the distribution of employment in the post-apartheid labour market as illustrated in Figure 17.

FIGURE 17

#### Employment in post-apartheid labour markets by race



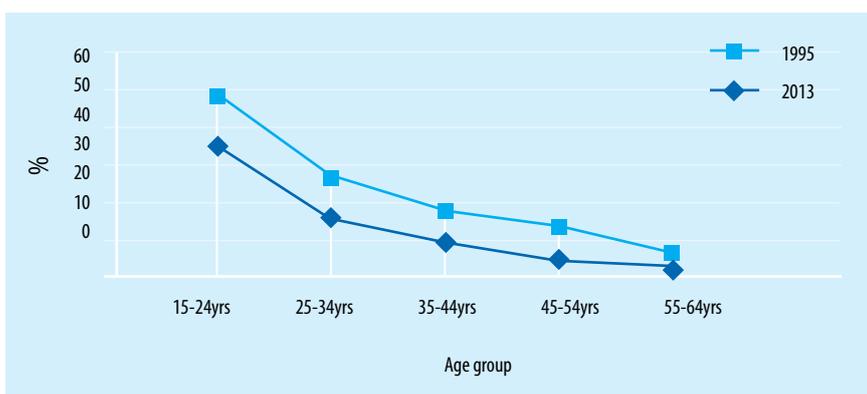
Source: Wittenburg, 2014

There is a strong spatial dimension to the distribution of unemployment also, with the rate of unemployment in the Eastern Cape nearly double the Western Cape.

Unemployment has a strong age dimension, with the youth confronting significantly higher levels of unemployment than older groups, as illustrated in Figure 18. Women are also more likely to be unemployed than men.

FIGURE 18

#### Age distribution of unemployment rates in South Africa: 1995-2005



Source: Compiled by authors using Stats SA data

### 6.2.3 The role of wage inequality in overall inequality

Along with unemployment, wage inequality is the second major factor affecting overall labour market inequality. This is not surprising as the inherited apartheid labour market structure was built on cheap black labour and an alliance between the then-ruling Nationalist Party and the white working class, who were paid relatively high wages. In addition, however, unemployment is also a major factor because it means a large number of "zero-earners" are stacked at the bottom of the wage distribution (Leibbrandt et al, 2010).

The continued high level of wage inequality has been the subject of significant debate and diverse interpretations. This is linked in turn to debate over whether South Africa is a high-wage economy, with high wages for formal sector workers as a result of strong trade union organisation, which negatively impacts on the scope for employment creation, and in turn contributes to high inequality – or whether instead, analysis of South Africa's wage structure is itself distorted by inequality, with unskilled workers earning very little, and with a high level of working poverty even in the formal sector. It's a debate that data might have been expected to resolve, but the debate continues to rage on the basis of competing and sometimes incomplete data sets: with significant policy implications. For example, the mean wage reported by Stats SA between 1994 and 2012 in the Quarterly Employment Statistics (QES) is almost double the mean wage from the Quarterly Labour Force Survey (QLFS). As Wittenberg (2014) highlights, despite a range of hypotheses, the scale of the gap remains at least in part unexplained. This often leaves data at the mercy of ideology rather than the reverse.

In addition, in contexts of high inequality, the choice of average or median wages provides an evidence basis for different arguments. Average wages are often used to argue that South Africa has a high wage structure; yet with 50 percent of black workers earning at or below the median wage of R2 600 a month in 2013 (about \$240), it is hard to sustain an argument that high wages for unskilled workers are the main constraint on employment creation.

Instead, working poverty is arguably a critical dimension of both poverty and inequality, with South Africa's wage structure reflecting the legacy of a multi-tiered racial labour market built on cheap black African labour, in which skilled work was reserved for whites who were paid a racial premium. In the process of deracialising this wage structure, its unequal dimensions have remained. These have been compounded by changes in the composition of demand for labour, with a declining demand for unskilled labour and an increasing demand for skilled labour, in the face of severe shortages.

In a detailed analysis for the International Labour Organization, Wittenberg (2014) finds that real wages have increased in the post-apartheid period, but that the gains from this increase are unequally distributed, with the gains accruing to the top deciles while real median wages of employees have remained stagnant:

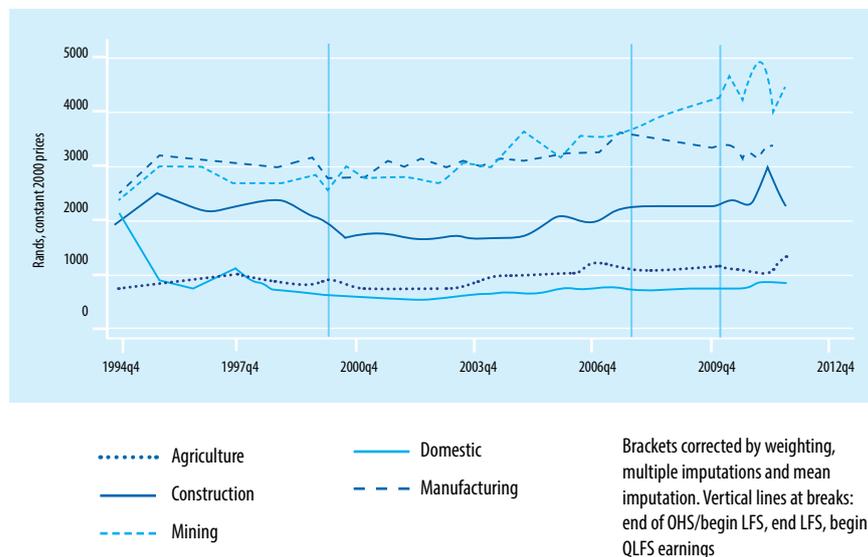
The top tail of the earnings distribution has “fanned out”, with larger gains at the 90th percentile than at the 75th, but both showing good real earnings growth. At the bottom end of the distribution there seems to have been compression – with the 10th percentile making real gains relative to the median. Among the self-employed, there is no evidence for systematic shifts in distribution over the post-apartheid period (Wittenberg, 2014).

Across the board, women earn less than men (Figure 19).

There are also substantial variations in the wages paid in different sectors – yet another example of the risks of average figures in contexts of high inequality (Figures 20 and 21).

**FIGURE 20**

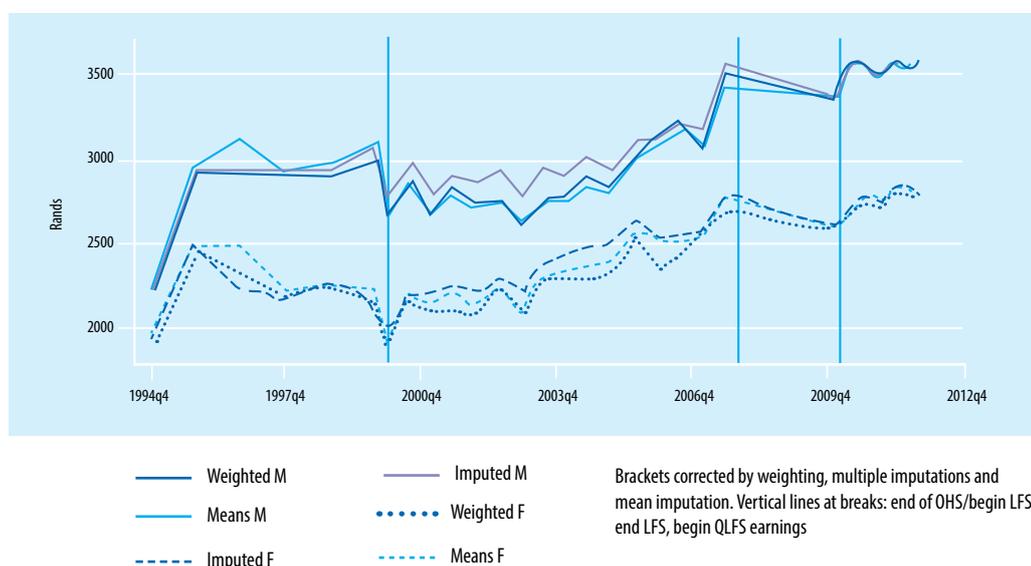
**Mean real earnings in the post-apartheid labour market – Wage workers by sector Part 1**



Source: Wittenberg, 2014

**FIGURE 19**

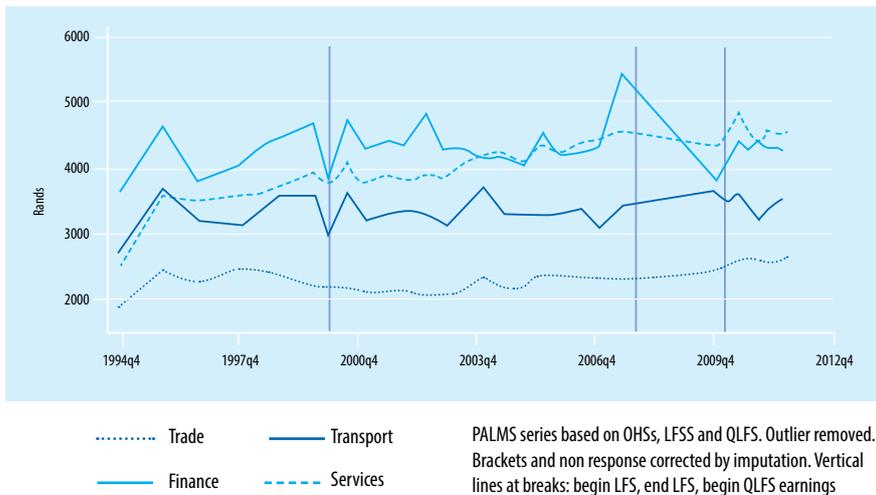
**Real earnings of wage-workers by gender**



Source: Wittenberg, 2014

FIGURE 21

## Mean real earnings in the post-apartheid labour market – Wage workers by sector Part 2



Source: Wittenberg, 2014

A premium is paid for professional and managerial skills in the South African economy. Clarke, Xu and Zou (2006) find that the median monthly wage for a manager in South Africa was more than double that of Poland and three times that in Brazil. A benchmarking study by BMA Analytics comparing South Africa and Thai automotive sectors found the ratio of artisan wages to be “an incredible 12:1”. (Bisseker, 2012): reflecting the premium paid for skilled work.

In 2013, the median monthly earnings of the white population group was R10 500, while at R2 600, the median monthly earnings of black Africans amounted to barely 25 percent of this (Stats SA, 2014a). In sum, according to the World Bank:

High wages in South Africa appear to be mainly due to high wages for managers and professionals and not to high wages at the bottom of the income distribution (World Bank, 2012).

A key part of the debate is also the extent to which increases in wages track or diverge from increases in productivity. Klein (2012), for example, argues that wage increases have outstripped productivity growth. However, following a detailed review of the data difficulties, Wittenberg finds that, on average, there is little evidence that wages have outstripped productivity or vice versa, but that a decomposition of the data by sector illustrates a clear pattern of divergence, with sectors that were relatively low productivity ones in 1994 (agriculture,

construction, trade and services) showing much lower labour productivity growth, while the remaining ones seem to have increased productivity.

Wage dynamics in the South African economy have been reinforced by changes in the composition of labour demand. Over three to four decades, there has been a steady decline in the demand for unskilled workers in the primary sector, and a steady increase in the demand for highly skilled workers in the services sector (Bhorat and Jacobs 2010). The key cause of the decline in demand for unskilled labour has been technological change, with labour replaced by machinery. In the agriculture sector, structural shifts away from primary to secondary and tertiary activities have also played a role. South Africa’s growth path, however, has a skills-biased labour demand trajectory, which is at direct odds with current supply characteristics (Bhorat and Jacobs, 2010).

#### 6.2.4 Dynamics in the middle of the distribution

While the focus has been on the top and the bottom ends of the distribution, there are also important shifts in the middle, which reflect social change in the country. So while the significant premiums paid for more skilled employment have led to increased wage inequality, they have also contributed to the emergence of a black middle class. This middle-income band reflects the greatest shifts in racial composition. The rich are still mainly white and the poor are almost all black, but the composition of the middle ground – made up of skilled workers, managers and professionals – has shifted, with growth in the black middle class of 250% in eight years.

There is a rapidly growing group of determined, ambitious, confident spenders driving consumption and growth in our pedestrian economy. In just eight years, the black middle class has grown from 1.6 million to 4.2 million adults (UCT Unilever Institute of Strategic Marketing, 2013).

In the institute’s classification of middle class, an adult must live in a household with an income of between R16 000 and R50 000 a month, or meet at least two alternative criteria. Of the 8.3 million adults classified

# monthly median earnings of the white population groups vs black africans in 2013

Stats SA, 2014



middle class in 2012, 51 percent are black, 34 percent white, 9 percent coloured and 6 percent Indian. This is a dramatic shift from the 2004 proportions, in which white people made up 52 percent of the middle class. Within the black middle class, 57 percent work in the public sector, making the racial transformation of the public service – and its higher-than-average wage increases – a significant driver of this demographic shift in the middle.

The emergence and increasing visibility of a black middle class is an important social phenomenon, particularly in a context in which by definition the majority of this group are first-generation entrants to this category, from families in poorer deciles.

More specificity and analysis of the middle is needed. If the middle is defined as covering percentiles 30 to 70, then Growth Incidence Curves based on expenditure patterns show that, in relative terms, this section of the distribution has benefited the least from growth, across all races, but in particular for black Africans (Figure 22).

Recently, political analyst Steven Friedman (2014) argued that the black middle class is the angriest in South Africa today, because in their working life they are at the sharp edge of the race interface in society, having

to break down the barriers of past privilege, the strength of old networks and residual prejudice – real and perceived. They are also at (or at least close to) that dramatic upward curve in the trend line in the Pens' Parade: directly confronted with just how steep that curve of inequality is, in a context in which their share of the benefits from growth have been the most constrained.

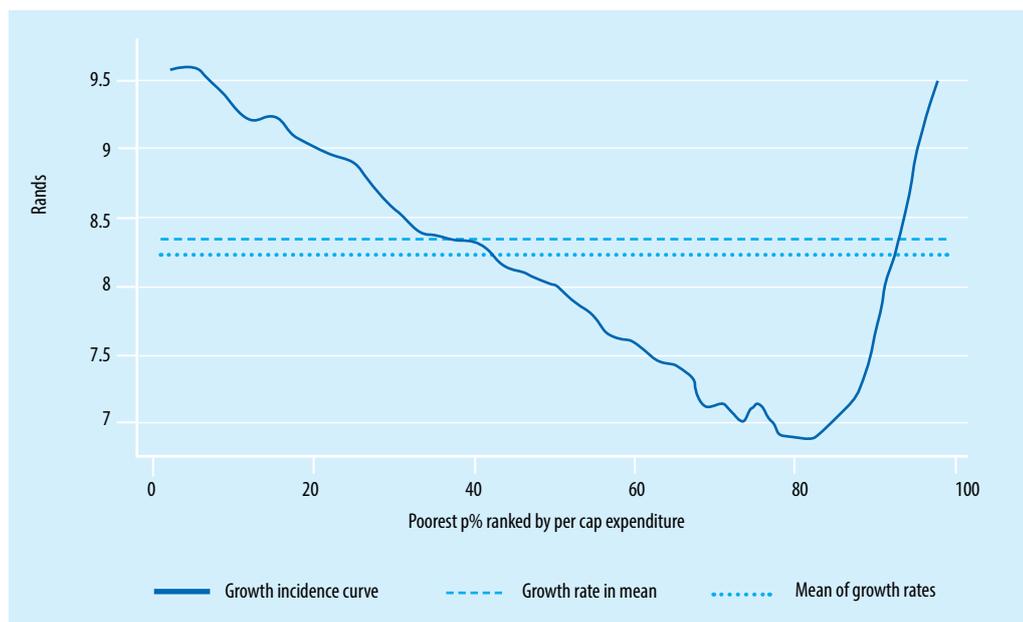
## 6.2.5 Labour market flexibility and inequality

Few topics have generated more heat and less light than debate on labour market flexibility in South Africa. This is because the policy stakes are so high, pointing either in the direction of deregulation and the erosion of rights in the workplace, or maintaining protections that labour secured as part of the transition to democracy.

● The rich are still mainly white and the poor are almost all black, but the composition of the middle ground – made up of skilled workers, managers and professionals – has shifted, with growth in the black middle class of 250% in eight years

FIGURE 22

Growth Incidence Curves for black Africans: 1995-2005



Source: Borat and Van Der Westhuizen, 2012

Part of this argument relates to the role of trade unions and the role of centralized wage bargaining structures in the economy, with these accused of raising minimum wages to levels that are unaffordable for small enterprise and new entrants, limiting job creation. Yet, as has been highlighted, high wage inequality is driven by high wages at the top end – and low wages at the bottom end. The former are not primarily a function of trade union bargaining power, while the low wages at the bottom illustrate the limits of trade union power in raising the wage floor.

A second key point of dispute is whether or not labour market rigidity is a critical factor constraining employment growth, for unskilled workers in particular. For anyone with a sense of history, this debate is loaded with irony. Under apartheid, different labour market regimes applied to four different racial categories of workers; employers had to provide segregated toilets and canteen facilities, and the pass laws were a highly onerous requirement, requiring passes to be issued for every black African worker employed. Yet it is only since the introduction of a rights-based labour market regime that the issue of “labor market flexibility” has entered the debate.

The widespread belief that South Africa’s post-apartheid labour markets are excessively rigid is highly charged, and highly reliant on perception-based surveys undertaken among employers. This is not borne out by the evidence. The OECD, for example, ranks South Africa among the top

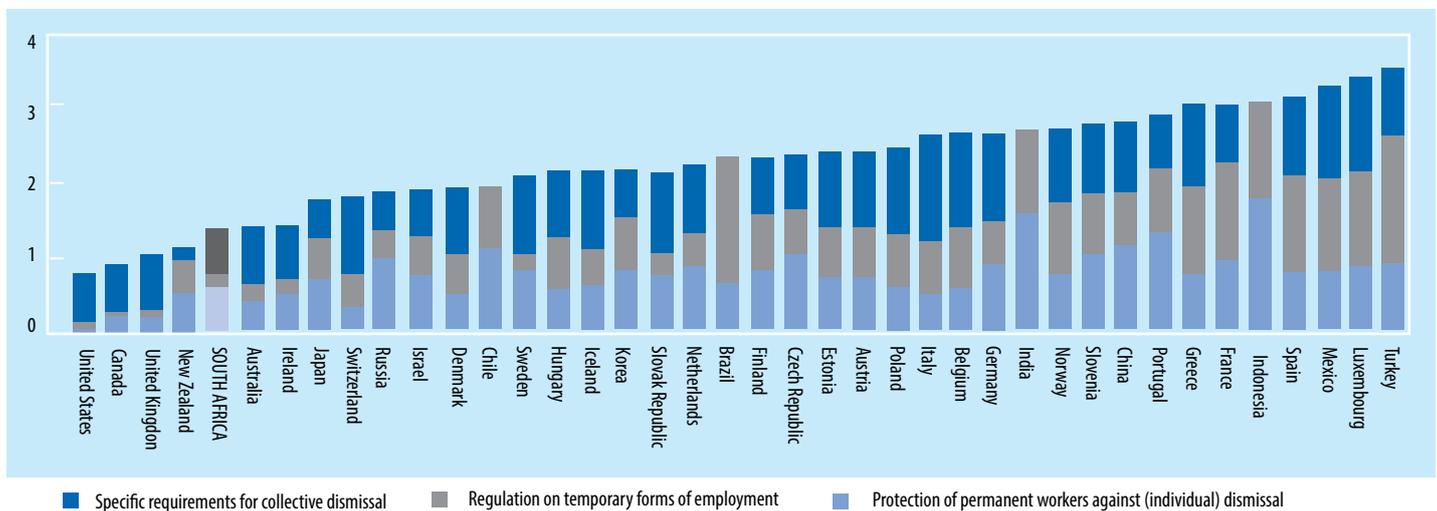
five most flexible labour markets in a cross-country comparison (Figure 23).

A detailed comparative study of labour market regulation by Borhat and Cheadle (2009) found that in most measures of labour regulation for both the 1990s and the 2006 data, “South Africa is not an extraordinarily over-regulated (or indeed under-regulated) labour market. This holds true for both the global samples and the sample of middle-income economies”.

An area of particular focus in the debate has been on the extent to which regulation of hiring and firing is excessively onerous. Borhat and Cheadle (2009) found that in this area, there had been an increase in hiring and firing rigidity, but a decline in hiring and firing costs. Borhat and Cheadle point out that regulation that is “neutral” can be rendered rigid by a malfunctioning institutional architecture, and find that in South Africa, the causes of rigidity relate primarily to institutional weaknesses in the application and interpretation of the regulations by the Commission for Conciliation, Mediation and Arbitration and the Labour Court, both of which have had erratic outcomes and divergent rulings on similar issues. The uncertainty this has created and the associated calls for labour market deregulation has put the underlying right to fairness at risk. Rather than changing the rights regime, however, solutions would appear to lie in addressing institutional weaknesses in the formulation of regulation and its administration.

FIGURE 23

Employment protection legislation is relatively liberal.



Source: OECD, 2013

## 6.2.6 The role of education in labour market inequality

Education is important for labour market outcomes, strongly influencing both the distribution of employment and wage dispersion. The graphs in Figure 24 illustrate the impact of different levels of schooling on both earnings and employment for black African and white men. African and white men.

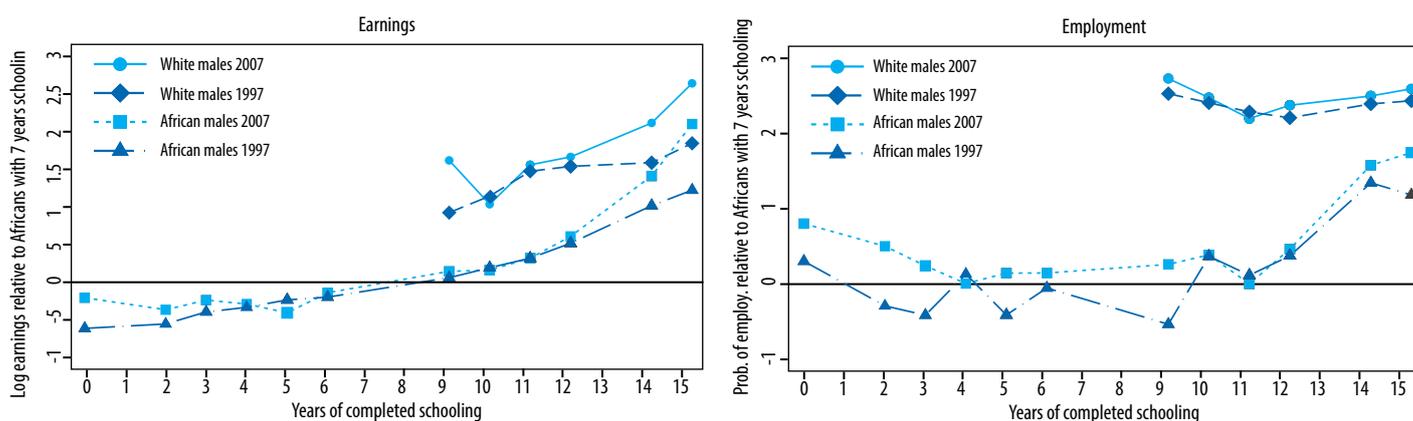
a man with 14 years of education earns almost **double** to one with 12 years



Branson, Garlick, Lam and Leibbrandt, 2012

FIGURE 24

Returns to schooling: Black African and white men age 25-59; South Africa OHS/LFS



Source: Branson, Garlick, Lam and Leibbrandt, 2012

Figure 24 also illustrates that returns to schooling are relatively modest until the completion of secondary school. While the earnings returns for black Africans who complete Grade 12 versus those who complete only Grade 11 are consistently high, the highest returns are for post-secondary education. Black African men with only two years of post-secondary schooling had earnings that are 40 percent higher than those with Grade 12 in 1997, and 70 percent higher in 2007: with the result that a man with 14 years of education earns almost double one with 12 years (Branson, Garlick, Lam and Leibbrandt, 2012). In addition, the premium to tertiary education increases at a higher rate for black Africans than the overall population, narrowing the wage gap at this level, with convergence potentially in sight (Branson and Leibbrandt, 2013).

In a society committed to overcoming a legacy of racial inequality, the slow rate of convergence in the racial wage gap is an obvious cause for concern. While discrimination is no doubt still a factor, research shows that if the causes of the racial wage gap are decomposed, quality of

education outcomes and other observed characteristics account for most of the difference. This shifts the focus from the labour market back to education.

Branson et al (2012) argue that South Africa has experienced a “skills twist”, in which the equalizing effects of increased access to education in the post-apartheid period have been negated by changes in the nature of skills demand, in the context of a changing economic structure in South Africa. So, while there has been a rapid increase in school enrolment and also in years of schooling, much of this is still at the level of incomplete secondary education.

In the past, this increase could have been expected to have an equalizing effect in labour markets, but changes in labour demand mean that the returns to education at this level have remained flat, while returns to Grade 12 and in particular to any form of tertiary education have increased. Labour demand has shifted away from unskilled to more skilled opportunities; shortages of skilled labour increase the premium for skilled labour being paid. As a result, the potential equalizing effect of increased

### Notes

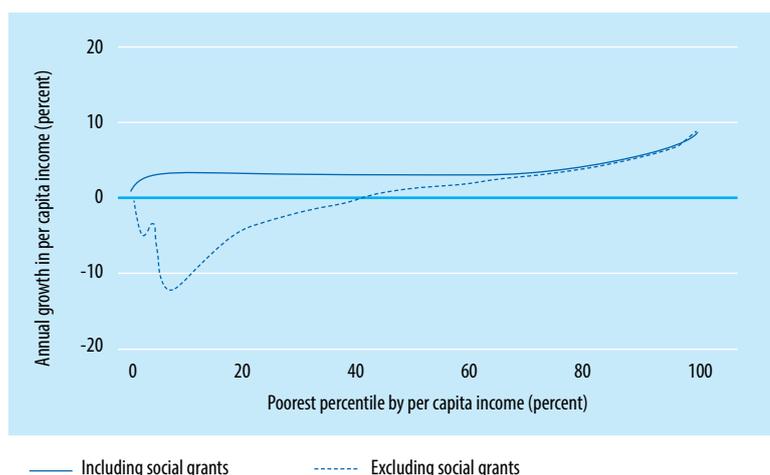
The figure is based on separate regressions for Africans and whites in each year on dummy variables for single years of schooling along with age and age squared. The figure shows real log earnings for each education group relative to Africans with seven years of schooling (end of primary school) in the given school. Whites are only shown above grade 8 due to low observation numbers.

access to education has been neutralized by the extent to which premiums to educational attainment are increasingly concentrated at the upper level.

In sum, labour market outcomes are a significant factor contributing to income inequality in South Africa, both in the distribution of unemployment and in wage inequality, with education playing a strong underlying role in influencing outcomes. Labour market outcomes are also manifestations of a far wider set of social and economic factors, including the structure of the economy, spatial issues and the impacts of social policies – as well as of legacies from the past.

FIGURE 25

Growth Incidence Curves for South Africa, 1995-2005



Source: Borat and Van der Westhuizen, 2012

TABLE 3

Gini coefficients broken down by deciles, showing deciles 1-4 with and without social grants

Gini	1993	2010
Overall	0.674	0.696
Deciles 1-9	0.524	0.525
Deciles 1-8	0.450	0.438
Decile 10	0.327	0.351
Deciles 1-4		
With grants	0.338	0.297
Without grants	0.491	0.604

Source: Calculations by Murray Leibbrandt

## 6.3 Social grants, social protection and the social wage

### 6.3.1 The impact of social grants on inequality

While labour market outcomes have the largest impacts on income inequality, social grants play a critical role for the poor. These grants include the old age pension, the child support grant, disability grants and foster care grants.

The transfer of these incomes to the poorest has had a vital impact on poverty. Yet because of the magnitude of wealth concentrated in the top decile, this transfer of income – dispersed as it is across a wide number of people – makes relatively little difference to aggregate income inequality. The argument, however, is that there is a risk that looking only at the big picture obscures shifts in income distribution that have real impacts on social equity and well-being, and that as a consequence, play a big role in limiting the social and economic damage caused by aggregate levels of inequality.

As illustrated in Figure 25, social grants have not only impacted on poverty, they have also had a significant equalizing impact on the incidence of growth all the way to the 8th decile. This has converted potential losses in real income into growth for the first four deciles – with the strongest impacts on deciles one and two. While the main effect of this has been to prevent income inequality getting worse, it's nevertheless a vital distributional impact, providing a corrective to what would otherwise have been a further rise in inequality.

The analysis of the Gini coefficient for different combinations of deciles (Table 3: undertaken by Murray Leibbrandt for this paper) illustrates a few important points about the dynamics of inequality. So while overall inequality increased between 1993 and 2010, the biggest increases appear to be in Deciles 9 and 10. Inequality actually dropped within deciles 1-8.



child support grant recipients report not only increased expenditure on **food** (79 percent), but also **school fees** (26 percent), **school uniforms** (25 percent) and **electricity** (22 percent)

Most significant are the dynamics within deciles 1-4: among the poor. At this level, the economy, left to its own devices, yielded an increase in inequality within these deciles from 0.491 to 0.604 – a staggeringly high level of inequality within just four deciles. Yet with social grants, inequality within these deciles is reduced to a relatively equitable 0.297.

How significant is this? Certainly, the extent of inequality between the richest and the poorest sets a framework that casts a shadow over all of society, and strongly influences aspirations and expectations. Highlighting the decline in inequality within these deciles is not intended to divert attention from the significance of this bigger picture inequality.

Yet it is also true that on a day-to-day basis, people's experience of inequality is influenced by how their lives compare to that of their neighbours, of family members, and of other people in their wider networks and community.

Reductions in inequality within poor communities can be expected to have important impacts on social equity and dignity, particularly in a context in which, as the growth incidence curve illustrates, the gap has been closed overwhelmingly by bringing the incomes of the poorest up. Social grants are not only alleviating poverty; within poor communities they are leading to significant increases in equity also. The impacts of this – and other dynamics within the bigger picture of inequality – require more sociological research.

In addition, assessing the impact of social grants on inequality needs to go beyond merely measuring changes in income. As previous sections have illustrated, some of the critical determinants of inequality are rooted in the forms of socio-economic deprivation that limit opportunities. Neves, Samson, Van Niekerk Hlatshwayo and Du Toit (2009) draw on a large literature on social grants to highlight that both the old age pension and the child support grant are strongly associated with improving the quantity and quality of food consumption, which improves nutritional status and lowers documented levels of morbidity and stunting. This is crucial in limiting the inter-generational transmission of not only poverty but also inequality, because of the knock-on

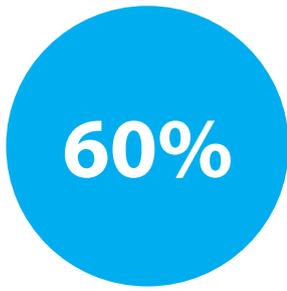
impacts of this on educational attainment and performance, linked in turn to labour market outcomes. They highlight data and research showing that child support grant recipients report not only increased expenditure on food (79 percent), but also school fees (26 percent), school uniforms (25 percent) and electricity (22 percent). In addition, research shows that social grants support investments in productive physical capital, such as improved housing and, particularly in rural areas, investments in smallholder agriculture, with concomitant increases in food consumption (Neves et al, 2009).

The evidence also highlights the role of social grants in changing power relations in the resource allocation within households, strengthening the hand of those responsible for the care of children in financial decision-making – usually women.

Less tangible but also important is the way social grants enhance social inclusion, in part in turn a function of social equity. Social grants strengthen the position of the marginalised within networks of social reciprocity, without which they would be disempowered. Neves et al. (2009) draw on wider research to illustrate how the old age pension, for example, incentivizes the care of old people, repositioning them in their households, cementing their roles as resource lynchpins.

These are outcomes not evident at the level of 'big picture' inequality, but they make a substantive difference to levels of social equity within which communities function on a day-to-day basis.

● At this level, the economy, left to its own devices, yielded an increase in inequality within these deciles from 0.491 to 0.604 – a staggeringly high level of inequality within just four deciles. Yet with social grants, inequality within these deciles is reduced to a relatively equitable 0.297



of spending in  
South Africa goes  
to the **social  
wage**

Stats SA, 2013

### 6.3.2 South Africa's social protection gap

Despite the extensive nature of South Africa's social protection system, a significant gap remains. This is the lack of support for most unemployed people. The Unemployment Insurance Fund is a contributory fund that supports about three percent of the unemployed at any time (Klasen and Woolard, 2008). Unemployed people have no access to any other form of support by virtue of their unemployed status. In practice, unemployed women with children are able to access the child support grant; this allows these women to contribute to supporting their families and reduces their dependency on others, even if the child support grant is not actually directed at them. The rest of the unemployed, however, have no access to any direct form of income support based on their status as unemployed people.

This group of unemployed people (which, because of the child support grant is comprised disproportionately of men) is dependent on the support and goodwill of others for their means of survival. This is deeply disempowering. It doesn't take too great a leap of analysis to imagine that this disempowerment has a range of harmful consequences, particularly when unemployment anyway contributes to social and health problems including crime, violence against women, alcohol and substance abuse, as well as depression and other health problems.

In a context in which the distribution of unemployment has already been identified as the single biggest factor impacting on

labour market inequality, the exclusion of a significant proportion of unemployed people from any form of income benefit compounds this effect.

This social protection gap exacerbates income inequality in other ways. In looking at the impacts of unemployment and household formation, Ebrahim, Woolard and Leibbrandt (2013) show that most unemployed people rely on the labour income of other household members, present or absent. In a context in which the median monthly wage for workers was R2 600 in 2013, every additional adult dependant that has to be supported on that income pushes the household further into poverty.

The second largest group of unemployed people live in households in which there is no labour-market income. This group is dependent instead on people with access to grant income – already by definition poor. This dilutes the impacts of these social grants on their intended beneficiaries.

As a consequence, poor people are carrying the cost burden of unemployment rather than this being recognized as a social cost to be shared across society as a whole.. The unemployment rate spreads the resources of poor households even more thinly, while wealthier households typically carry less of the burden – either in the direct economic costs of supporting unemployed people or in the associated social costs to families and communities.



## Public employment and the social protection gap

As part of addressing the social protection gap, South Africa has invested in large-scale public employment, in which sectoral programmes in infrastructure, the environment, the social sector as well as community-driven forms of public employment are coordinated under the auspices of the Expanded Public Works Programme. Participants in such programmes are included in national employment statistics, rather than as part of the unemployed. Most of this work is of short duration.

For some, such as in the social sector, public employment can become a stepping stone into decent work in the health sector. But in a context in which the economy is not producing jobs at the scale required, many people, particularly in the most marginal areas, are more likely to exit from public employment back into poverty. This is why the Community Work Programme offers regular and predictable part-time work on an ongoing basis – to provide a predictable income contribution to livelihoods.

The impacts of public employment programmes include the income earned, the assets and ser-

vices created, and the social and economic benefits that derive from enabling participation in work.

Participation in work matters in people's lives. It builds skills and capabilities, and contributes to countering the many adverse social and psychological impacts of unemployment. It provides structure, access to networks, and social inclusion. In programmes such as the Community Work Programme, communities also participate in identifying what work needs to be done to improve the quality of life in their communities, and implementation involves new forms of partnership between government, civil society and communities. In the process, labour that would otherwise be unused is instead used to create social value.

The Expanded Public Works Programme is in its third phase, characterized by a focus on strengthening the developmental outcomes from public employment. While it is expected to scale up considerably, the sheer scale of unemployment in South Africa means there is a real question over whether public employment can usefully absorb all those willing and able to work. This raises the question over whether complementary measures are required to address the remaining social protection gap.

**R2 600**

the  
**median  
monthly  
wage** for  
workers in  
2013

Ebrahim, Woolard and Leibbrandt,  
2013

**The roots of inequality today are the two great episodes of dispossession: in relation to land and in relation to South Africa's mineral wealth**



Chris Kirchoff, MediaClubSouthAfrica.com

# How social and economic inequality impact on economic development in South Africa

A CRUCIAL ASPECT of the political settlement in South Africa that enabled the transition to democracy was the recognition of property rights. In practice, this meant the recognition of property rights as they existed at that time – rather than prioritizing any prior rights. Restitution would, therefore, take place only on the basis of fair compensation. The trade-off was the transfer of political power and the establishment of a rights-based system. This enabled South Africa's peaceful transition to democracy, its integration into global markets, and the promise of social and economic policies that would lead to a better life for all.

In key respects, this promise has been kept. Yet high levels of economic inequality that are rooted to a significant extent in these ownership structures continue to constrain the achievement of a better life for all, in particular in terms of outcomes in employment creation and inclusive growth, and the impacts of these in turn on poverty and inequality. The range of theoretical explanations provided in section 2 show how high levels of social and economic inequality constrain economic development and growth – and South Africa matches the profile of all the conditions likely to have this effect.

The roots of inequality today lie in the two great episodes of dispossession in South Africa's history: in relation to land and in relation to South Africa's mineral wealth. The loss of the former closed an important

trajectory of asset accumulation and market participation for black South Africans, forcing them into labour markets, where cheap labour was needed to extract the mineral wealth at maximum profit. The interlinked set of processes through which land dispossession was used to create a pool of cheap labour for the mines and other industries created the foundations for the structure of South Africa's economy and for inequality. White minority ownership of assets was secured through the use of political power backed by armed force; economic power was consolidated through the development of rules of the game in which inequality of opportunity was institutionalized and became systemic. This has had inter-generational impacts that reinforce and contribute to reproducing economic inequality, in a negative spiral from which South Africa has yet to break free.

Despite the gains made, equality of opportunity continues to impact not just on the wellbeing and life chances of individuals, but also on the scope for economic development and growth, through its negative impacts on productivity and innovation. Important as it is to address this, the potential impact of equality of opportunities on the economy and on society can only be optimized if there are, in fact, opportunities available.

In South Africa today, the lack of economic opportunities as a result of high

unemployment is the heart of the issue. This is the driver of poverty, inequality and rising social tension. In this, South Africa is a global outlier: no other middle-income country has had unemployment levels of more than 20 percent for more than 20 years. There is no precedent for this, or for what it might mean for a society over time.

The causes of unemployment are complex. Yet debate in South Africa often focuses narrowly on labour market policy as a critical causal factor in this regard. In the process, lobbying for labour market deregulation as a necessary condition for addressing unemployment has become the new frontier for a renegotiation of South Africa's historic compromise, with the cession of rights won by labour at this level presented as a necessary condition for private investment in productive activity, in a context in which the owners of capital still hold trump cards in this regard.

This is not an evidence-based debate. While South Africa is a global outlier on a range of fronts – this is not one of them. The levels of protection provided to workers recognize core rights, but are not excessively onerous by any global standard. Yet weaknesses in the administration of these rights, and costs and uncertainties associated with such weaknesses have opened the door to an assault on the rights themselves. Closing that door requires serious attention to addressing such institutional weaknesses.

In addition, important as labour market policy is, labour markets are simply where demand meets supply, and, as this paper has illustrated, both the demand for and the supply of labour are shaped by dynamics that lie well beyond labour markets, and that can be impacted only indirectly by changes at this level.

The net effect of continuous high levels of unemployment mean, however, that the processes of change are falling behind levels of popular expectation. As has been argued, the deep sense of unfairness that comes with high levels of inequality make social instability more likely, and with it, the terms of South Africa's original trade-off are being brought into question. The levels of asset inequality cast a long shadow over society, and popular memory has not forgotten that the processes of original accumulation were

not fair. In a context in which poverty and income inequality shape daily realities, there is easy – and legitimate – political capital to be made from both the land question and the structures of ownership in the economy; the re-emergence of calls for nationalization of the mines and for more radical land redistribution policies are setting the current terms of the debate.

Regardless of constitutional commitments, this makes the owners of capital nervous: particularly those in mining and agriculture, but also others – including international capital. Will the trade-off last? Will democracy ensure social and economic stability? How far can social policy mitigate economic inequality? At what point might South Africa face some form of social revolt? Will the ANC ally with the Economic Freedom Fighters to change the property rights clause in the constitution? The wait-and-see attitude this creates in the owners of capital is, arguably, at the root of the investment strike in South Africa and has played a role in the financialization of the economy.

Large amounts of local capital are being invested in financial markets rather than in productive activity. Large amounts of international capital flow into financial markets also – flowing out at the drop of a hat (or the drop of an emerging market index), with an ease enabled by current financial market policy in South Africa. This bias towards financial markets is despite returns to productive investment on par with – and often better than – other middle-income countries. This lack of investment is a critical constraint on employment creation.

Uncertainty over future policy, in a context of highly unequal asset ownership structure, is central to these investor choices. In agriculture, as has been argued, South Africa finds itself in the worst of all possible situations: while little land has actually been redistributed, the continuous uncertainty and sense that more radical policies are pending has contributed to the rapid decline of investment, and with this, a decline in employment and in agriculture's contribution to GDP, making South Africa a global outlier in the lack of contribution this sector makes to inclusive growth. Yet the decline in investment has not only been in

private investment. After years of extensive state support in the apartheid years, this sector saw government disinvestment in the post-apartheid period. Solutions to the land question are not simple. While in theory land redistribution unlocks increased productivity (which is a key reason why it contributes to increased growth) the process in South Africa has all too often seen previously productive land no longer being used productively. The potential trade-offs between jobs, agricultural productivity and land redistribution therefore make policy particularly difficult. At present, the price of equivocation is being paid in the decline of agriculture's contribution to inclusive growth.

Yet most dynamics in South Africa fit comfortably within the classic explanations for why high levels of inequality constrain growth. Even without the political uncertainty, however, the structure of the South African economy and its high levels of concentration impact on inclusive growth in other ways, in particular, because of how levels of concentration constrain employment growth. At the same time, the structure of the economy is increasingly biased towards higher-skilled jobs, with manufacturing growing slowly. In the context of skills shortages, this reinforces existing levels of wage inequality, the second most important contributor to income inequality.

A particular feature of concentration in the economy and of its sectoral composition is the extent to which core consumption goods typically found in the basket of the poor are mass produced in the core economy – including agro-processed goods. This significantly constrains the scope for small enterprise development to follow the classic local economic development trajectory, in which small producers start off by manufacturing goods for sale in their local community and/or smallholder farmers engage in agro-processing of surplus production, and grow and expand from there. Poor communities – rural and urban – are already well serviced by the large corporates in the core economy. This limits manufacturing opportunities at the local level, leading to an over-representation in retail activity, often in the informal sector, with marginal returns, and significantly raises

In South Africa today,  
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heart of the issue



the barriers to entry for small enterprise trying to access markets beyond their local context. The high barriers to entry in this sector contribute to unemployment, while the poor returns to entrepreneurial effort contribute to earnings inequality.

High levels of unemployment and associated poverty in turn impact on aggregate demand in the economy, and the nature of that demand, with greater demand for imported goods from high-income earners. This in turn exacerbates balance of payments problems and increases South Africa's dependence on speculative foreign inflows.

Spatial inequality is another critical component of structural inequality: with a unique role in adding a range of different kinds of costs to the economy in South Africa. Large numbers of people live in rural areas, but do not earn their livelihoods there, and have little prospects of doing so. The population in these communities is skewed towards women, and to the care and reproduction of children. In terms of limiting the inter-generational reproduction of poverty and inequality, this is a vital target group. Yet the costs of delivering basic services to often remote areas, is prohibitive – significantly raising the costs of reducing inter-generational socio-economic disadvantage.

In urban areas, spatial inequality translates into human settlements at a distance from economic activity. With communities far from existing infrastructure grids, this also significantly raises the costs of delivering basic services. High transport costs raise the reservation wage, and hence the costs of labour, in ways that create wage pressures without this translating into improvements in living conditions. Long distances reduce quality of life for workers, in particular, the

## A feature of post-apartheid South Africa was the initial disconnect between the political and economic elites, yet the nature of elites is undergoing change

quality of family life, with long commutes eating into the time available for social reproduction. All of this increases the costs of reproduction of labour, with knock-on effects in the economy. These costs are translated into wage costs rather than being carried as social costs, contributing to wage pressures.

High levels of unemployment mean that a large proportion of the working age population is not contributing to the creation of economic value. This means that GDP output per capita is produced by the economic outputs of a far smaller number of people than are available to the economy and the society, constraining the scope for growth. In addition, the long-term nature of much unemployment erodes the skills involved in productive work. Even when and if work becomes available, long-term unemployment is likely to hold back levels of

productivity. High wage inequality can also translate into lower levels of productivity, if this is associated with a sense of unfairness.

In South Africa, unemployment has an additional disequalising impact, because unemployed people do not receive any form of social grant targeted at them. In a context in which most unemployed people live in households in the lower-income deciles, this means both the social and economic costs of unemployment are carried by poor communities – not shared as a social cost across society. This further impoverishes poor households and is disequalising at an overall level.

In sum, in a complex range of ways, social and economic inequality in South Africa are acting as powerful constraints on economic development and growth.



Large amounts of local capital are being invested in **financial markets** rather than in productive activity

# Priorities for public policy: dilemmas and choices

*...(E)ven though market forces help shape the degree of inequality, government policies shape those market forces. Much of the inequality that exists today is a result of government policy, both what the government does and what it does not do (Stiglitz, 2012).*

THE CRITICAL ISSUE for public policy is to prioritise what needs to be done to break the vicious cycle through which social and economic inequality combine to constrain economic development and growth. This means answering the following questions:

- How to overcome the continued reproduction of high levels of inequality of opportunity?
- How to maximize the scope for redistributive policies not only to ameliorate inequality, but also to act as an investment in unlocking economic development and growth?
- How to address the underlying structural issues that contribute to the reproduction of inequality, including the structures of ownership, the sectoral composition of the economy and spatial inequality, in order to unlock employment growth?

In relation to equality of opportunity, high levels of inequality in human development outcomes continue to be reproduced despite a strong rights framework and strong social policies. To a large extent, the challenge in this area is therefore less about improving policy than it is about addressing institutional failings that limit the realization of rights, jeopardize access to public goods

and services, and reproduce high levels of inequality on the basis of race, gender and location.

The quality of public administration is often a determinant factor in this regard, making this issue a central focus for strategy in this area. This focus needs to go beyond simply the issue of 'capacity', however, to look more deeply at what it is in the functioning of the state - in the rules, norms, and incentives and in how rents are captured - that is leading to outcomes at odds with stated policies. Innovation and improvements in this area also need to be recognised and supported, with lessons learned from how this has been achieved. What obstacles do such innovation and improvement processes face? What are the institutional incentives and disincentives for initiating change?

Despite the importance of the role of public administration, there is also a sense in which dependence solely on the state for delivery in this regard reproduces a logic in which other social institutions are absent from the process. Without detracting from the centrality of the state's role, what complementary forms of social organization and institutional development best ensure improved outcomes at this level, and how might the role of such institutions enable

levels of agency in society that include but also go further than holding the state accountable for delivery? What institutional mix in society best promotes equity of outcomes and how can such a mix be fostered?

At one level, addressing the institutional factors that contribute to reproducing inequality means strengthening the voice of the most disadvantaged within the processes through which society sets its rules - and is held accountable for keeping to them. This requires a deepening of democracy, understood not just as participation but also as agency, in communities and workplaces as well as in all spheres of life in which disadvantage is most manifest. How is this actually done? Through what instruments and processes? It's a conversation that needs to find its way more clearly back into policy priorities, because the quality of democracy plays an essential role in ensuring that the institutions of society are designed to enable equity and fairness.

By contrast, high levels of social and economic exclusion allow power to be constituted in ways that reproduce marginality and exclusion. In a current illustration of this, black women in former Bantustan areas (who are recognized as the most disadvantaged and voiceless group in South Africa and are therefore a stated focus of public policy) are currently at risk of seeing a reversal of some of the rights gained through the political process. This is as a result of the politics of accommodation in relation to the role of traditional authorities and the status of customary law, with a recurrent theme in proposals from government that would deepen their institutionalized power, including but not only over land rights. While this remains a highly contested issue, a reversal in this regard could create an even wider schism between the rights and opportunities available to black women living in these areas, relative to the trajectory of the rest of society. Preventing rights being eroded at this level is therefore a policy priority.

South Africa's strong track-record of redistributive social spending means that high levels of equality delivered by the economy are mitigated at the level of society. Understanding just how unequal the former is certainly matters - as do interventions

to change such outcomes at this level; but the economy is nevertheless just a part of society, not its sum total. How far economic inequality is allowed to determine the character of a society depends critically on the role of public policy.

At one level, this is about redistributive policies that change economic outcomes after the fact. This role has traditionally been seen as ameliorative and as a debit on the national balance sheet rather than as an investment. There is however increased recognition that such policies also actually unlock economic development and should be considered "part of the toolkit to promote growth" (Donaldson, 2014). The multiple trajectories through which redistributive policies do so include the impacts of improved human development on productivity and economic dynamism, on the impact of cash transfers on aggregate demand and on the composition of that demand, and on the scope for this to act as a form of stimulus to the economy - trickling up from spending by poor people in local economies rather than forms of stimulus that never reach them.

Yet there are limits to how far such social investment can go in addressing the structural factors that underlie the reproduction of economic inequality and constrain employment, including high asset inequality, the sectoral composition of the economy and spatial inequality. The need for economic policies that address these factors is not a new insight. Concern with it is reflected in various ways in the National Development Plan, the New Growth Path, the Industrial Policy Action Plan, and the Presidential Infrastructure Co-ordinating Commission, with the need for massive public investment and a concerted industrial policy to shift the economy onto a more labour-absorptive track and to achieve different distributional outcomes regularly asserted in the policy process. So why does this not appear to be achieving the desired results?

Perhaps the hardest element within this relates to asset inequality and concentration in the South African economy. As the National Development Plan reflects, "patterns of ownership and control have to change. This will not be easy. It requires carefully sequenced actions that transform the

● High levels of social and economic exclusion allow power to be constituted in ways that reproduce marginality and exclusion

economy without destroying its capacities.”

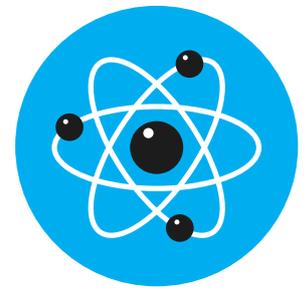
The focus of policy in this area has been on black economic empowerment policies that address racial inequality in ownership, without a concomitant focus on concentration. Important as the former is, there is a risk that focusing on this in isolation from concentration of ownership has limited impacts on other dimensions of inequality – at the same time as changing the political economy in ways that may reduce the likelihood of changes in concentration ever happening.

A feature of post-apartheid South Africa was the initial disconnect between the political and economic elites, yet the nature of elites is undergoing change. While the old elite remains dominant, space has been made for the capture of significant rents by a small but politically-connected black elite, often now with an interest in the terms on which wealth is generated within the current structure of the economy. While a shift in how rents are captured – and by whom – is necessary, the form taken in this instance has had limited effects on levels of concentration and appears to have reinforced profit-taking and financialization in the economy rather than contributing to increased productive investment. In this context, it matters to understand how far the interests of the political elite have shifted, and how much this affects the political economy of achieving change in the structures of ownership.

At present, the potential pathways for addressing asset inequality remain unclear. A core conundrum for South African policymakers is that while high levels of asset inequality appear to be constraining inclusive growth, open financial markets mean that addressing this may well compound capital flight and disinvestment, negatively affecting employment in the short term at least. Continuous uncertainty is, however, having that outcome anyway. This begs the question of why open financial markets are taken as given. Part of the answer to this lies in South Africa’s current dependence on short-term financial inflows for its balance of payments.

Although these issues are central, macroeconomic policy has largely evaded policy scrutiny as part of the discussion on inequality. This is despite its role in the financialization of the economy, in how capital flight has been – and continues to be – enabled

There is a strong inter-relationship between **equity of opportunity** and economic outcomes...



by current policies, the impact on interest rates and on exchange rates because of the dependence of the balance of payments on erratic inflows of financial capital, and how all of this contributes to inequality and what can be done to change it.

Within the overall context of asset inequality, the land question is particularly intractable. In a system divided between the former white-owned farmland and areas under communal tenure, current proposals on the table follow divergent logics. In a context of promises of more radical policies, there is nothing radical about the proposals to consolidate the power of traditional authority in land allocations in the former bantustan areas, with risks for the poorest and particularly for women.

On commercial land, the proposals under discussion to allocate 50 percent of farm ownership to farmworkers on a farm by farm basis seem designed to incentivize evictions, cause divisions among farmworkers, put jobs at risk, and lead to further reductions in productive investment in this sector. The institutional complexity involved in the proposed allocation and governance arrangements also appear unachievable, given capacity shortcomings. These proposals are no doubt intended to provide the kind of rupture in existing property relations required to unlock more equitable growth, but while they might appear to offer a neat (and radical) solution to addressing racial inequality in land ownership, the risks of unintended negative consequences seem high. To compound matters, neither the proposals for communal nor for commercial areas address the needs of the small but vital constituency of existing black farmers wanting to expand their access to commercial land, with a continued disjuncture between policies for land and for agriculture. In this area, unless serious attention is given to finding alternatives, there seems to be little ground for optimism, with a likelihood that South Africa continues

to be a global outlier in the role of the agricultural sector in creating unskilled employment and in its contribution to GDP, with a risk of the situation worsening.

In sum, with asset inequality, policy appears to be torn between approaches that give priority to building business confidence as the route to unlocking investment, and flirting with disruptions to existing property relations that might hold the potential to unlock a new and more equitable trajectory of growth. While the bulk of policy messaging certainly favours the former (and the constitution sets this as the necessary framework), the aspiration for more radical solutions is a growing part of the discourse – without much in-depth assessment of what form this might take, and with financial market policies leaving the door wide open for further capital flight.

Must changes in the distribution of assets necessarily involve destabilizing ruptures? While the answer to this question may well be “yes”, answering the challenge posed in the National Development Plan requires at least a serious attempt to find alternatives. Among the avenues for exploration, consideration of the current forms of capture and allocation of rents in South Africa’s mining sector as well as its most concentrated industries and the potential for such rents to be used to create alternative asset forms and/or social transfers is required. In the context of this debate, the argument that creating new assets can be more successful than redistributing old ones also bears some examination. Implausible as this may seem at one level, it does turn the focus of debate to the scope to build the assets of the poor. In this regard, South Africa’s massive rollout of housing units is an example – with all its limitations – of a significant form of potential asset transfer to the poor, potentially more relevant to an urbanizing population than the transfer of a small pocket of agricultural land. The creation of tenure rights in urban informal settlements is another example of such asset creation. The point is that addressing the conundrum of high asset inequality requires innovation specific to South Africa’s context and more lateral thinking, because the set of options on the table at present do not appear to offer real solutions, either for equity or for economic development.

In changing the structure of the economy, an additional critical dimension is its sectoral composition. However, without private investment the scope for change is highly constrained, and in some senses industrial policy is therefore held hostage in part at least to the wider issues impacting on such investment. The achievement of such change also depends to a significant extent on political economy issues. Most successful industrial policy processes that have achieved shifts in the sectoral composition of their economies have been premised on strong social compacts. In the wider theory, it is noted that social compacts are hardest in contexts of high inequality. In South Africa, early practices of partnership and tripartism in the post-apartheid period have largely disintegrated into mistrust on all sides.

Institutional constraints also frame what can be achieved with industrial policy. Does the institutional capacity to design and deliver effective industrial policy exist within government? And can the requisite levels of common purpose and partnership be built between government, the private sector and labour? Important as public investment is, industrial restructuring is not a process in which government can go it alone. A critical issue is whether and how private investment can be unlocked in the process.

Easy as it is to treat private capital as monolithic and as an obstacle to the realization of changed outcomes, its participation is a necessary part of the solution. The process of building partnerships and social compacts requires more attention to the different types of private interests that exist, to the different types of incentives and disincentives to which they are most likely to respond, to the different forms of public and private partnership that might be crafted, and to the scope to build on a common interest in economic dynamism. The drivers of ‘investor confidence’ for multinational finance capital are not the same as for local manufacturing capital – or for small enterprises at a local level. In addition, in South Africa’s changing political economy, the zones of influence over large amounts of private capital – such as pension funds – has also changed. Does this open new opportunities to unlock private investment – and through what levers? Prescribed investments for pension funds used to be part of the policy environment: why can’t a required

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percentage of pension fund investments go into productive investment?

Finally, in this regard, increased partnership between government and the private sector does not have to mean ganging up on labour, which tends to add to gridlock. A commitment to decent working conditions can provide the starting point for whatever incentives are on the table in such processes. The question is to what extent different elements within the private sector are willing, finally, to make peace with the rights-based terms of the original compact that secured South Africa's transition and to actually look at how they might make it work. This would certainly contribute to the scope for more constructive engagement.

The role of aggregate demand is also an important part of the equation in relation to stimulating private investment. To what extent are poverty and inequality placing limits on the kind of demand necessary to stimulate shifts in investment and in the sectoral composition of the economy that are desired? To what extent might the opportunities arising from an increase in such demand trump other factors in stimulating investment? While much of the inequality debate has focused on the notion of South Africa as a high wage economy – which it is, for skilled workers and professionals – how might higher wages below the median level stimulate aggregate demand and what impact might this have in unlocking productive investment? This is directly relevant to proposals for a minimum wage currently on the table, which look set to be approved. In this context, the focus of debate has shifted to the level at which this should be set.

In the cross-country comparisons of minimum wage levels, what is usually absent is a comparison of the costs that society treats as wage costs and those that are carried as part of the social wage. Without this, such comparisons tell us only about the cost of wages to the private sector, without telling us what this means for the well-being of workers. In South Africa, the costs of unemployment are disproportionately borne by poor people, which acts as a significant cause of wage pressure at the lowest earnings levels. How might converting this to a social cost change the parameters of the minimum wage-rate debate?

While labour market outcomes are the main determinant of income inequality, it has been argued here that the role of labour market policy in determining those outcomes and as a causal factor in relation to unemployment tends to be overstated in the debate, in a context in which the factors informing the character of both the demand and supply of labor are largely beyond the reach of labor market policy. Yet, weaknesses in the administration of the rights underpinning the current regulatory regime and the costs and uncertainties associated with such weaknesses have opened the door to an assault on the rights themselves. As has been argued, closing that door requires serious attention to addressing these institutional weaknesses to ensure efficiency, predictability and fairness in the administration of such rights, in order to prevent the political economy of defending them from worsening further.

In addressing spatial inequality, the terms on which urbanization is taking place locks new entrants to the cities into disadvantaged and disempowered spaces and places, creating and reproducing an urban underclass with each wave of new arrivals – at the same time as raising the costs of labour. While this is an area in which innovation and policy vision do exist (especially in some of the metros), operationalizing this at the required scale has not yet happened.

At an overall level, the obstacles to structural change are significant. It will be hard to achieve and even under the best of circumstances, will take time to deliver results. Yet unless results are delivered sooner rather than later, levels of social instability may sabotage the scope for policies that transform the economy without destroying its capacities.

It is in this context that the role of redistributive social policy comes to the fore once again. In a context in which it is estimated that nearly 60 percent of government spending goes to the social wage, the issue is less about the amount of social spending than its quality and focus. The institutional issues influencing the quality of outcomes have been highlighted. The focus of that spending and its impacts on inequality deserves more focus, however. Two issues stand out. In both cases, gaps in the social wage mean that instead of these costs being carried by society as a whole,

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a focus on **cost-recovery** in relation to public transport places the **burden** of this apartheid legacy squarely **into the household budgets** of workers, work-seekers and the poor

they are being carried disproportionately by the poor. Instead of being carried as part of the social wage, part at least of these social costs become wage costs, adding to wage pressures and raising the costs of social reproduction and of labour.

First is the issue of transport. In a context in which spatial inequality is, to a large extent, set in concrete, a focus on cost-recovery in relation to public transport places the burden of this apartheid legacy squarely into the household budgets of workers, work-seekers and the poor.

Second, in a context in which the single biggest driver of income inequality is unemployment, the fact that most unemployed people are not directly covered by any form of social protection exacerbates this. If the aim is to reduce inequality in the short term, then addressing this gap would be the single most important addition to South Africa's existing set of redistributive social policies.

In the first instance, it makes sense to expand public employment programmes that make a direct and visible difference at community levels. Participation in work contributes to social inclusion and to the productive capabilities of participants; such programmes are also able to contribute to improving the quality of life in communities, and to strengthening community development processes.

An option is for South Africa to follow India's lead, and create a statutory right to work, and to adapt the concept of an employment guarantee to South African conditions. However, given the far greater scale of unemployment in South Africa, concern exists that not all unemployed people can be usefully employed in this way. Insofar as this

is the case, real consideration needs to be given to complementary measures of social protection for the unemployed, to ensure an integrated basket of social protection measures – taking into account how this interacts with the existing range of transfers in cash and kind.

Is this affordable? With growing concern at rising budget deficits, it does not seem so – or not without significant cuts elsewhere in the budget, the politics of which might present a hurdle that is simply insurmountable under current conditions. But it does also beg the question of whether our fiscal dispensation is appropriate – an issue which the review of the tax system initiated under then Finance Minister Pravin Gordhan is still to pronounce on, and which is presumably considering the implications of Piketty's arguments for wealth taxes – and the scope to tax rents without negatively impacting investments, as some economists argue is possible. In addition, in a context in which the profit share of GDP has risen, how appropriate are levels of corporate tax? These issues in turn present South Africa with the golden goose dilemma: the current levels of fiscal income that fund social policies (and all other spending) rely heavily on taxes on the top 10 percent. Will increases in taxes at these levels see capital flight and another wave of emigration?

The costs of not expanding social protection to the unemployed may, however, be even higher, if not incalculable; because such a contribution to reducing income inequality in the short term may just be a necessary condition for the social stability required to achieve long-term structural change in the economy – quite apart from its intrinsic value.

# Conclusions

IF HIGH LEVELS of inequality limit the scope for economic development and growth, and also limit the pro-poor impacts of the growth that does take place, then policies cannot rely on growth to reduce inequality – strategies to reduce inequality are needed to unlock inclusive growth.

Such strategies include both social and economic policies, aimed at changing patterns of access to opportunity, to rights, to social and political power, and to the distribution of assets and incomes. This includes redistributive measures, in combination with changes to the underlying structural factors contributing to the reproduction of inequality. The role of public policy is critical: what government does and what it does not do.

While addressing inequality of opportunity is necessary, it is not sufficient, in a context in which opportunities are lacking. In South Africa today, the lack of opportunity is driven primarily by the lack of employment, with high unemployment the critical driver of both poverty and inequality.

In this regard, the challenge is to change the outcomes being delivered by the economy – in the levels of inclusion it enables, as well as the terms of such inclusion. In doing so, there is no avoiding tackling the structural issues that play such a key role in reproducing current high levels of inequality: the structures of ownership, spatial inequality and the sectoral composition of the economy.

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TWENTY YEARS AFTER the end of apartheid South Africa is a different place. It has a well-institutionalized democracy. Significant gains have been made in social equity and in reducing extreme poverty. Yet poverty, unemployment and inequality remain South Africa's most pressing problems. Social change and enhanced access to rights have not translated into comparable economic shifts – unemployment has risen and inequality has increased and remains extreme.