COVER STORY

At the end of the apartheid era, almost half of South Africa's population were categorised as poor using a national poverty line, and one-fifth earning less that $1 per day. Over 60% of Africans were poor compared to just 1% of the white population and South Africa was described by the World Bank as among the world's most unequal economies, with a Gini co-efficient measuring 0.58. Just 6% of South Africa's population captured over 40% of income.

Is poverty and inequality leading to **poor growth?**

The conventional view is that higher and more sustained levels of economic growth will reduce poverty and inequality. ***Julian May, Michael Carter*** *and* ***Vishnu Padayachee*** *argue however, that poor growth is a result of high and increasing income inequality and poverty. If this is the case then a fundamental rethink of economic policy is required.*

In 1996 the South African government released its Growth, Employment and Redistribution (Gear) strategy as a macroeconomic framework for growth and development. Despite its name, Gear's principal achievements have been macroeconomic stabilisation (reductions in the budget deficit and the inflation rate), rather than in growth, job creation and poverty reduction. Popular opinion has been hostile to Gear while surveys suggest that the economic fruit has been bitter for many. Official statistics confirm that economic growth has been low, and that unemployment has escalated, especially in sectors exposed to global competition. Recent living standards surveys suggest that both poverty and inequality remain high and may have increased during the same period.

While there is much debate about the impact of growth on poverty and inequality, South Africa's sluggish growth may be rooted in its high and increasing income inequality. The new economics contend that unequal income and wealth distributions become economically costly and growth-reducing when large numbers of a country's citizens are unable or unwilling to engage in entrepreneurial activity, are unable to save and invest, and are unable to meet charges on the provision of essential services.

The need for micro reform to address these problems has begun to enter the South African policy debate. Certainly, the introduction of reforms that result in markets working efficiently for everyone may be simultaneously a way of achieving a pro-poor set of microeconomic policy options while pursuing policies that would ensure macroeconomic stability. Standing in the way is a dual legacy of apartheid. On one hand, the social and economic policies of successive apartheid governments resulted in an ossified society in which privilege, opportunity and well-being were highly correlated with race. Less visible, but no less important is the micro legacy of apartheid in terms of missing, thin and distorted markets.

Economic policy debate and record from 1994

The ANC's *Reconstruction and Development Programme* (RDP) published in 1994 broke with the view that growth and development are processes that contradict one another. Its powerful statement of principles sets out a development strategy which attempted to integrate growth, development, reconstruction and redistribution into a unified programme. But the detail proposed sometimes contradictory ideas. For what it did was attempt to marry the ANC's old social democratic and socialist values (redistribution, basic needs) with new neo-liberal ones (trade and financial liberalisation, the independence of the central bank), ostensibly held together through institutions and accords at which all the 'social partners' would be represented.

Orthodox economic ideas were eventually given full reign in Gear. The underlying premise of Gear, which aimed to attain a growth rate of 6% per annum and job creation of 400 000 by the year 2000, is that growth would best be promoted by freeing the private sector from the fetters of the distorted racist logic and constraints of the apartheid era. The need to remove all vestiges of a state-imposed, racially-based economic order was extended to argue for a much more sweeping 'rolling back of the state'. These included the abandonment of arguably important policies such as a discrete and effective public investment programme, tariff protection for vulnerable industries, essential reform of the heavily conglomerate-controlled domestic financial system, and the tightening of controls to prevent capital flight.

Ten years into the new democracy, it is now possible to examine Gear's projections and outcomes against actual performance. It is clear that, apart from complying rather well with targets for macroeconomic stability, the real economy is performing nowhere near the levels that are needed to address the problems that South Africa inherited from apartheid. Government policy appears to have been successful in the areas of fiscal restraint, tariff reductions, and inflation control and off the mark on the real economy (growth and employment). Significantly, real interest rates remained higher and private sector investment lower than that projected on average for the period. Growth rates have not come near the estimated sustained rates of 7-8% per annum required to absorb new entrants into the labour market and make inroads into the growing pool of unemployed people.

This disappointing record took place against apartheid's legacy of racially embedded poverty and inequality. A window into the evolution of poverty over this same time comes from the KwaZulu-Natal Income Dynamics Study (KIDS) which provides panel data comparing African and Indian households surveyed in 1993 and 1998 in the province of KwaZulu-Natal. The study reveals some disturbing trends. Expenditure-based national poverty measures increased with a headcount measure below the poverty line rising from 27% to 43%. The average income shortfall for those below the poverty line increased from 27% to 33% of that poverty line, and a measure of the severity of poverty rose sharply.

While these trends are disturbing, they do not indicate a clear failure. For example, the reported trends could have been generated by significant upward and downward mobility in which initially poor and non-poor households have swapped places in the income distribution. Distinguishing between these two cases is of more than academic interest. A society in which initially poor households are trapped in poverty is clearly very different from a society in which poverty is a matter of transitory spells from which poor households expect to periodically escape.

Poverty traps and chronic poverty 1993-1998

Using a poverty threshold based on the reported expenditure of the households, the transitorily poor (meaning below the poverty threshold in one of the two periods) can be compared to the chronically poor (meaning below the poverty threshold in both periods). A static view of poverty shows that 67% of the KIDS sample were categorised as not-poor in 1993, declining to 58% in 1998. However, 48% of the sampled households could be described as never poor, 30% were poor in either 1993 or 1998 (transitorily), and 22% were poor in both periods (chronically). This suggests that there is considerable movement into and out of poverty, although a substantial proportion of the sample were unable to escape poverty despite the time that had elapsed and the political and economic reforms that occurred during the five year period.

A large clump of initially poor households have either held steady or have fallen behind. In the language of analysis of poverty dynamics, these households are chronically poor. In contrast, upward mobility is concentrated among households that were initially better off. This suggests a more nuanced notion of poverty based not just on observed levels of poverty, but on the likelihood of being poor.

The categories of the poor can now be further broken down into those that clearly fell behind during the five year period between the two waves of the survey from those that could improve their position. A significant proportion of the sample (21%) now emerge as not only poor, but also falling behind, that is to say, their ability to generate an income declined between 1993 and 1998. While still poor, just 4% of the sample were able to improve their situation.

These findings suggest that in the absence of proactive policies that lift constraints that limit the effectiveness with which the rural poor are able to use the limited assets and endowments they possess, few of the poor were positioned to be able to take advantage of new opportunities afforded by the post-apartheid economic environment.

Constraints to the use and accumulation of assets

In an effort to dig beneath these statistics, flexible econometric methods have been used to identify endowment bundles that map into livelihoods above the poverty line given the market structure in place at apartheid's end. Analysis of the KIDS data reveals significant departures from the smooth asset additivity that would characterise the mapping in a world of full and complete markets, and uncovers three dimensions of the poverty problem:

- The marginal returns to uneducated labour are positive, but are so low that they are insufficient to generate an income that meets the poverty subsistence requirements of incremental units of labour. Claims on other economic or social assets are thus necessary to lift a family above the poverty line.
- Financial constraints that limit the poor's ability to effectively utilise productive assets and endowments (eg, land) that they do have. Poverty is thus not only a matter of few assets, but also of constraints on the effective use of those assets.
- The burden of meeting basic need requirements creates a 'time poverty' that further constrains households' ability to effectively employ those resources to which they do have access in the generation of livelihood.

It would seem then that the poor are poor not only because they have few assets, but also because they are constrained in their ability to effectively utilise the assets they do have. However, inefficiencies such as those described above can be thought of as multiple market failures in which wage opportunities are weak and ancillary factor markets are not working very well. As a result the poor remain poor because they cannot borrow against future earnings to invest in inputs for production or the accumulation of assets for future production, including education. They are unable or unwilling to enter into entrepreneurial activities because the costs of failure are too high, they are unable to insure themselves against risks and they lack information about market opportunities. Finally they are deprived of many public goods necessary for such activities (such as property rights, public safety, and infrastructure) and incur high costs in terms of time and expense when trying to obtain these goods.

Life after Gear

If sluggish growth is indeed partly rooted in the numbers of people trapped with little prospects of income mobility or asset accumulation, a fundamental rethinking of economic strategy may be required. Making things right at the micro level so that the market economy can work for all, requires recognition of the interlinking nature of macroeconomic and microeconomic reforms. Microeconomic reforms and interventions need to be more ambitious if the poor are to push ahead. They would need to involve measures that improve the access of the poor to productive assets such as land reform, infrastructure and financial services, as well measures that reduce the costs of production.

For such policies to work, they have to be located within the context of an enabling, supportive and complementary macroeconomic framework. This should be one in which industrial and labour-market policy, coupled with an integrated urban and rural infrastructural development programme are directed at raising aggregate employment in the formal, secure, high productivity and organised sectors of the economy. At the same time, improvements in the provision for social security will be needed to reduce risks associated with unemployment, ill health and disability, and address the specific needs of work-seekers, children and child carers and the elderly.

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