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## “Two Nations”? Race and Economic Inequality in South Africa Today

**S**OUTH AFRICA HAS LONG BEEN INFAMOUS for its very high level of inequality. Speaking in Parliament in 1998, then-deputy president Thabo Mbeki described South Africa as divided into “two nations, the one black and the other white”:

One of these nations is white, relatively prosperous, regardless of gender or geographical dispersal. It has ready access to a developed economic, physical, educational, communication and other infrastructure. This enables it to argue that, except for the persistence of gender discrimination against women, all members of this nation have the possibility of exercising their right to equal opportunity, and the development opportunities to which the Constitution of 1993 committed our country. The second and larger nation of South Africa is black and poor, with the worst-affected being women in the rural areas, the black rural population in general and the disabled. This nation lives under conditions of grossly underdeveloped economic, physical, educational, communication and other infrastructure. It has virtually no possibility of exercising what in reality amounts to a theoretical right to equal opportunity, that right being equal within this black nation only to the extent that it is equally incapable of realisation.<sup>1</sup>

This view is often backed up with data indicating interracial inequalities. In 1994, the year apartheid ended, average per capita income among the black population was one-tenth that

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of the white population; among people aged fourteen years or more, 90 percent of the white population had passed at least standard six (corresponding to grade eight in the United States) in school, compared to 46 percent of the black population; among people aged eighteen years or more, 61 percent of the white population had passed at least matric (standard ten), compared to just 11 percent of the black population; 36 percent of black households and 0 percent of the white population lived in shacks, traditional huts, or hostels; only 18 percent of black households had internal piped water, and only 37 percent had electricity—compared to 100 percent of white households.<sup>2</sup>

The notion of a society comprising “two nations” is certainly not original. Benjamin Disraeli, who was later to become prime minister of Britain, first used the imagery of “two nations” in his 1845 novel *Sybil, or The Two Nations*. For Disraeli, the two nations were the rich and the poor of nineteenth-century England:

Two nations; between whom there is no intercourse and no sympathy; who are as ignorant of each other's habits, thoughts and feelings, as if they were dwellers in different zones, or inhabitants of different planets; who are formed by a different breeding, are fed by a different food, are ordered by different manners, and are not governed by the same laws.<sup>3</sup>

Amidst the rapid social and economic change of the industrial revolution, economic inequalities in Britain were widening dramatically. The evidence is thin and the comparison difficult, but inequality in income distribution in Britain appears to have reached its highest level in the 1860s or 1870s, at a level slightly lower than that in South Africa a century later.<sup>4</sup> In his novel, Disraeli contrasted the opulence of aristocratic life with the desperate squalor of industrial poverty. But Disraeli's primary emphasis was the social and cultural divide, rather than economic inequality per se.

More recently, the imagery of two nations has been used in the United States with reference to interracial inequalities. Ghetto riots in the 1960s led to the National Advisory Commission on Civil Disorders warning that “our nation is moving

toward two societies, one black, one white, separate and unequal." In 1992 a popular American political scientist, Andrew Hacker, used the imagery in a book on America entitled *Two Nations, Black and White: Separate, Hostile and Unequal*.<sup>5</sup> Hacker surveyed the scope of interracial inequalities in late-twentieth-century America across issues as varied as divorce rates, percentages of children born to unmarried parents, earnings and incomes, unemployment, educational achievement, and crime.

Mbeki's use of "two nations" imagery is like Disraeli's and Hacker's in that it is intended to draw attention to injustice. But there are important differences in the ways in which Mbeki, Disraeli, and Hacker each use the imagery. For Disraeli, the inequality is that of class: the rich and the poor. Hacker does not presume to comment on American inequality as a whole; he does not claim that all white Americans are rich or that all black Americans are poor. Mbeki, however, appears to reduce inequality to race: black equals poor and white equals rich. Indeed, he claims, black South Africans are "equally incapable" of realizing the right of equal opportunity.<sup>6</sup> If Mbeki had attached more importance to social and cultural divides between white and black South Africans he would probably have been on stronger ground, but in emphasizing interracial economic inequality he misunderstands the changing nature of inequality in South Africa.

In South Africa, black and white are *no longer* synonymous with rich and poor. Moreover, South African society cannot simply be divided into rich and poor, as if the distribution of incomes were bipolar. In the final decades of apartheid the deracialization of formerly discriminatory policies, upward occupational mobility among black workers, and rising unemployment resulted in declining *interracial* inequality but rising *intra*racial inequality, especially among the black population.

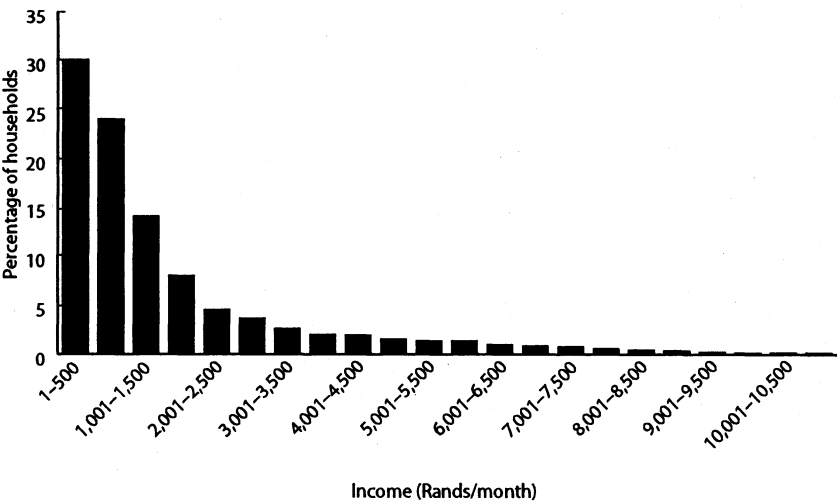
In post-apartheid South Africa, inequality is driven by two income gaps: between an increasingly multiracial upper class and everyone else; and between a middle class of mostly urban, industrial, or white-collar workers and a marginalized class of black unemployed and rural poor. A more appropriate eco-

conomic comparison might be drawn with the image of the United States painted by the American Catholic Bishops in 1995: “The U.S. economy sometimes seems to be leading to three nations living side by side, one growing prosperous and powerful, one squeezed by stagnant incomes and rising economic pressures and one left behind in increasing poverty, dependency and hopelessness.”<sup>7</sup>

THE CHANGING NATURE OF INEQUALITY

Household incomes are certainly distributed very unevenly in South Africa (see figure 1). If the population is divided into income deciles (each decile comprising one-tenth of the total number of households, ordered by ascending income), then the top or richest decile (decile ten) earned about half of the total income in 1993, whereas the bottom four deciles (deciles one through four, which actually comprised 52 percent of the population, as poor households were larger than rich ones) earned

Figure 1. Inequality in South Africa



Source: Southern African Labour and Development Research Unit at the University of Cape Town data set, 1993.

less than 10 percent of the total income. There is some evidence that inequality has widened further since 1993.<sup>8</sup>

Unsurprisingly, given South Africa's history of apartheid, there is still a strong correlation between race and household income. Nine out of ten households in the bottom six deciles (the poorest 60 percent of households) were black in 1993; a small proportion were colored, and a tiny proportion were white. By contrast, three-quarters of the top decile were white. This is unambiguous evidence of interracial inequality. But consider the following: between 1975 and 1996, the share of total income received by black people rose from 20 to 36 percent, while the share received by white people fell from 71 to 52 percent.<sup>9</sup> This shift was primarily due to the rapidly rising incomes of the black working and middle classes. In 1975 only 2 percent of households in the top income decile were black, while 95 percent were white; by 1991, 9 percent were black and 83 percent were white, and by 1996, 22 percent were black and 65 percent were white.<sup>10</sup> These shifts may be long overdue, but they are extraordinarily large and rapid.

Rising income among better-off black households has widened intraracial inequality as well as reduced interracial inequality. By 1996, the average household income in the richest tenth of black households was over two hundred and fifty times higher than the average income in the poorest tenth. The richest tenth alone earned about one-sixth of the total national income, which is more than the combined share of the other nine-tenths of black households together (and about the same share as the top tenth of the white population).<sup>11</sup> There are very few countries in the world where income inequality is higher than it is among the black population in South Africa. Whiteford and Van Seventer estimate that "within-group" inequality now accounts for over two-thirds of total inequality, whereas it only accounted for 38 percent in 1975.<sup>12</sup> If black South Africans comprise a "nation," as Mbeki puts it, it is an extremely unequal one—so unequal that it seems nonsensical to use the term "nation." Moreover, declining interracial inequality has not led to lower inequality overall, because intraracial inequality has increased.

*Sources of Income Inequality*

Table 1 shows the composition of mean household income for each income decile (using 1993 SALDRU data). Wage income clearly contributes the largest share of income for South Africans as a whole, although not for the poorest deciles that rely on pensions and remittances. Old-age pensions are very important to deciles two through four (but not the bottom decile, because receipt of a pension is enough to push the household up). Income from agricultural production is of little importance, except to the top decile (which includes high-income, capitalist farmers) and the bottom decile (in which the incomes are so low that even a meager R 8 per month, in 1993 prices, is an

Table 1. Composition of Household Income, by Income Decile and Source (in percentages)

Decile	Regular wage	Casual wage	Total wage	Remittances	Agriculture	Self emp	Pension	Other transfers	Capital income	Total
1	12.3	9.7	23.5	48.5	8.4	13.0	0	1.0	3.5	100
2	19.5	6.6	30.6	30.0	4.4	6.1	23.2	3.2	2.1	100
3	24.2	5.1	37.8	18.4	3.0	5.1	27.9	4.8	2.8	100
4	34.9	5.8	50.0	15.0	3.3	4.0	21.8	3.7	2.1	100
5	44.7	4.7	55.8	10.0	2.5	5.5	18.8	3.5	3.7	100
6	60.5	4.1	69.6	6.8	0.7	3.9	12.1	3.0	3.4	100
7	68.8	2.2	75.0	5.1	1.3	3.8	7.6	2.0	5.0	100
8	72.1	2.5	78.5	2.9	1.0	4.8	4.3	1.6	6.6	100
9	72.8	1.9	79.9	1.2	0.7	4.6	1.9	1.1	10.5	100
10	56.0	1.5	64.5	0.4	6.8	9.0	0.5	0.3	18.1	100
Total										
S.A.	59.3	2.3	67.7	3.4	4.0	6.7	4.6	1.2	12.1	100

Notes: “Regular/casual wage” represents wages from regular/casual employment. “Total wage” includes all wages, together with the value of employer subsidy of transport, food, and housing (not included here as a separate column). “Remittances” include the value of remittances in money and in kind. “Agriculture” includes the value of agricultural production whether consumed or sold. “Self-emp” comprises the profits earned from self-employment, whether formal or informal. “Pension” comprises the noncontributory, means-tested government old-age pension. “Other transfers” comprise other public transfers (primarily disability and child-support grants). “Capital income” includes income from capital, actual, and imputed rent on land and property, interest on financial assets, and income from contributory pension schemes. The rows do not add up to 100 percent because of rounding errors and the omission of some very minor sources of income. The “Total S.A.” row is the weighted average of the rows above, where data has been weighted according to shares of total national income.

Source: SALDRU data (1993); our calculations.

important mean contribution to household income). In other words, smallholder agriculture is almost irrelevant in South Africa. For every decile from the fourth up, wages comprise by far the most important source of household income.

The overwhelming importance of the labor market in the distribution of income reflects the ways in which the South African economy was transformed under apartheid. Industrialization was accompanied by deagrarianization. Black sharecroppers and labor tenants were squeezed off white-owned land. Excluded from the towns by the pass laws, they were forced into the reserves, where agricultural production collapsed through overpopulation. The pass laws (and other measures) also served to restrict the informal sector. The result was a society unusually dependent on waged work.

#### *Inequality and the Labor Market*

During the apartheid era, racial discrimination was an important determinant of wage inequality. Similarly qualified people were paid different wages for doing the same job, depending on their racial classification—especially in the public sector. As late as 1979, for example, the starting salary for a black nurse in the public sector was two-thirds that of a white nurse with the same qualifications.<sup>13</sup> Furthermore, black people were often unable to get jobs for which they were qualified. The color bar reserved most skilled jobs for white people until late in the apartheid period. The maximum salary for black secondary-school teachers and police constables was just one-half that for white teachers and constables.<sup>14</sup> When an occupation hitherto reserved for white workers was reclassified for black workers, the wage rate was typically reduced greatly.

From the 1970s, however, the impact of racial discrimination declined. Between 1980 and 1993 the contribution of racial discrimination to wage determination is estimated to have dropped from 20 to 12 percent of the average black wage.<sup>15</sup> More importantly, upward mobility into better-paying occupations raised wages for many black employees. The gap between the average wages of white and black employees narrowed sharply. But even in 1993 white employees' earnings were on average more than five times larger than black employees' earnings (see



Table 2. Characteristics of the Sample of Wage Earners

	Black		Colored		Indian		White	
	Men	Women	Men	Women	Men	Women	Men	Women
Years of education	6.8	7.6	8.5	8.5	11.0	10.7	12.2	11.2
Rates of return on education (%)								
-primary	8.4	6.2	1.4	2.3	-9.5	-8.2	-1.2	-3.4
-secondary	15.8	24.9	18.7	19.9	21.4	12.6	8.4	5.2
-higher	29.4	39.6	18.6	30.7	21.4	30.4	15.1	13.9
% living in rural areas	56.1	47.2	10.3	9.9	1.8	0.9	6.6	6.8
% working in agriculture	20	11	14	11	0	0	4	1
Hourly wage in rands	4.8	3.3	7.2	5.1	12.8	8.2	27.9	15.8

Source: T. P. Schultz and G. Mwabu, "Labor Unions and the Distribution of Wages and Employment in South Africa," *Industrial and Labour Relations Review* 51 (4) (1998): 682, 687. Analysis based on SALDRU data, 1993.

table 2). The racial wage gap is now explained primarily by factors other than overt discrimination, such as differences in education and skill, location (urban or rural), and economic sector. As shown in table 2, black workers have the lowest educational qualifications, live predominantly in rural areas, and have the highest concentration in low-paying sectors such as agriculture. Econometric estimations confirm the importance of such characteristics in explaining wage inequality.<sup>16</sup>

Education is particularly important. According to one estimate, half of the difference in racial earnings can be attributed to differences in educational qualifications.<sup>17</sup> If it were possible to include a measure of the different *quality* of education received by white and black workers, then education would probably explain an even greater proportion of wage inequality. Black workers with good educational qualifications are particularly well placed to obtain highly paid jobs. It is estimated that black men can command an extra 8 percent on wages/salaries for every year of primary education, an extra 16 percent for every year of secondary education, and an extra 29 percent for every year of tertiary education. Such rates of return on education are higher than for all other racial groups (see table 2). The returns on secondary and tertiary education

are even higher for black women. This suggests that improving the access of black men and women to secondary and tertiary education would narrow wage inequality significantly (although the rates of return would decline as more and more people obtain higher qualifications).

As apartheid unraveled, many black people moved up the occupational ladder.<sup>18</sup> Between 1980 and 1993, the proportion of black men in the laborer and semiskilled categories dropped from 57 to 38 percent. As the number of black people in higher-paying occupations rose, so the gap between high- and low-paid black workers increased. But not all the forces in the labor market were working to widen inequality in the black wage distribution. As the black trade-union movement gathered momentum in the 1980s, unskilled black workers were given a significant wage boost. Trade-union membership appears to increase wages of black workers in the bottom 10 percent of the wage distribution by 145 percent and increase the wages of those in the top 10 percent by a mere 11 percent.<sup>19</sup>

By increasing the wages of low-paid workers faster than high-paid workers, the black trade-union movement acted as a force in favor of greater wage equality. But the union movement's effects on the overall distribution of income is unclear, because higher union wage settlements might have encouraged firms to shed labor. According to Schultz and Mwabu, an increase of 10 percent in the union relative wage effect (i.e., the ability of unions to push their members' wages above those of non-members) reduced employment by 5.6 percent.<sup>20</sup> This would have acted to widen inequality by increasing the number of people without any access to wage income.

#### *Access to Wage Income*

Most employed workers are earning enough to raise their household incomes above the poverty line. Only about 30 percent of employed workers are in households in the bottom five deciles. These workers are predominantly farm workers and, to a lesser extent, domestic workers. The industrial working class, by contrast, is concentrated in the top five deciles. Only 13 percent of manufacturing workers are in households in the bottom five deciles; fully 77 percent are in the top four deciles. Mine work-

ers are distributed more widely, with the largest numbers in deciles four to seven. In terms of occupation, people in professional, technical, managerial, and administrative jobs are, unsurprisingly, in households in the top two deciles. Most workers in clerical and sales occupations are in the top three deciles. Artisans are spread across the top four deciles. Most machine operators and similar semiskilled workers are in deciles six to nine. Unskilled laborers are spread across deciles four to eight.<sup>21</sup>

Most poor households are poor because they have no access to wage income. There is a clear relationship between employment/unemployment and inequality. The majority of households in the bottom four deciles have no members in employment, whereas a majority of households in each of the top two deciles have two or more members in employment. The relationship between the lack of employment and poverty is much stronger in South Africa than in more developed economies.<sup>22</sup>

The relationship between participation rates (i.e., the proportion of adult household members participating in the labor force), unemployment rates (i.e., the proportion of the labor force that is unemployed), and income inequality is clear in table 3.<sup>23</sup> Both participation and unemployment rates are presented using the expanded definition of unemployment, which includes people who are not actively looking for jobs because they believe there are none available (i.e., the “discouraged” unemployed). Poor households are poor because their members are not in the labor force, and because of high unemployment few jobs are available. Because poor families tend to be larger than richer ones, the relationship between unemployment and income is even stronger when income deciles are calculated on a per capita basis.

There is strong evidence that unemployment increased in the 1990s. According to the October Household Survey, unemployment rose from 20 percent to 23 percent between 1994 and 1997 (if one counts only the active job seekers as unemployed) or from 32 percent to 38 percent (using an expanded definition of unemployment).

The fact that racial discrimination has declined in importance, and that employment, education, and other factors are now of primary importance, explains why intraracial inequal-

Table 3. Participation Rates and Broad Unemployment Rates by Decile (in percentages)

Income decile	Participation rate	Unemployment rate	Unemployment rate using per capita income deciles*
1	48	71	76
2	47	56	59
3	45	48	48
4	50	40	41
5	51	37	34
6	57	33	26
7	58	28	17
8	61	24	10
9	64	14	5
10	75	5	2
Total S.A.	61	30	32

\*Calculations by G. Kingdon and J. Knight, "What is the Appropriate Definition of Unemployment?" presented to the Seminar on Unemployment in South Africa, Institute for Economics and Statistics, Oxford University, 10 November 1999, 7. Analysis based on SALDRU data, 1993.

ity has grown while interracial inequality has declined. When new employment opportunities opened up for black people in the 1970s and 1980s, there was no equality of opportunity among black people. Black children who grew up in households headed by middle-class or white-collar employees were many times more likely to follow into such occupations themselves than were black children who grew up in households headed by migrant workers. Under apartheid, the presence of black people in towns was regulated under the "pass laws"; the minority of black people with the "right" to stay in town regardless of their employment status had big advantages over those who did not have this "right" to urban residency.<sup>24</sup> The opening up of new employment opportunities thus exacerbated class inequalities within the black population. Intraracial inequality was also reproduced through enduring inequalities in education. In 1993 black children living in middle-class households had completed, on average, almost three more years of schooling by the age of eighteen than black children living in households headed by farm workers or domestic workers; the differential widens dramatically after the age of eighteen, as the former continue in school while most of the latter have dropped out.

Democratic states are typically subject to political demands to mitigate, through redistributive patterns of taxation and public expenditure, the inequalities generated in the market. In South Africa, the African National Congress-led Government of National Unity inherited, in 1994, a surprisingly redistributive budget. Calculations by Michael McGrath and colleagues suggest that redistribution through the budget reduced the Gini coefficient (a measure of the amount of inequality in income distribution) from about 0.7 (for gross or original income) to 0.6 (for post-tax/transfer income, taking into account also benefits “in kind” in the form of public education and health care) in 1993–1994.<sup>25</sup> Servaas Van der Berg estimates that redistribution through the budget in 1995 was even more effective in reducing inequality, with the Gini falling to as low as 0.51. Redistribution happened because the top two deciles received fewer transfers or benefits in kind than they paid in tax, while all other deciles received more benefits than they paid taxes. Richer households benefited more in absolute terms than poorer households—but this inequality in the incidence of expenditure was more than offset by their payment of the lion’s share of income tax.

Even in 1993–1994 the South African budget was more redistributive than the budget in other middle-income economies (such as Chile, Brazil, and Argentina, although it was less redistributive than the budgets of advanced capitalist economies).<sup>26</sup> This reflected a combination of factors on both the taxation and expenditure sides. Income tax constitutes a comparatively high proportion of total tax revenue in South Africa. On the expenditure side, the democratic South African state inherited a means-tested, noncontributory old-age pension system that had, with the deracialization of benefits (completed in 1993), become well targeted on the poor,<sup>27</sup> together with an education system that may have had enduring interracial and interclass inequalities but was nonetheless less inegalitarian than in Brazil, for example (at least in terms of the number of grades completed, since secondary-school enrollment is very high among the poor in South Africa).<sup>28</sup> The pattern of health-

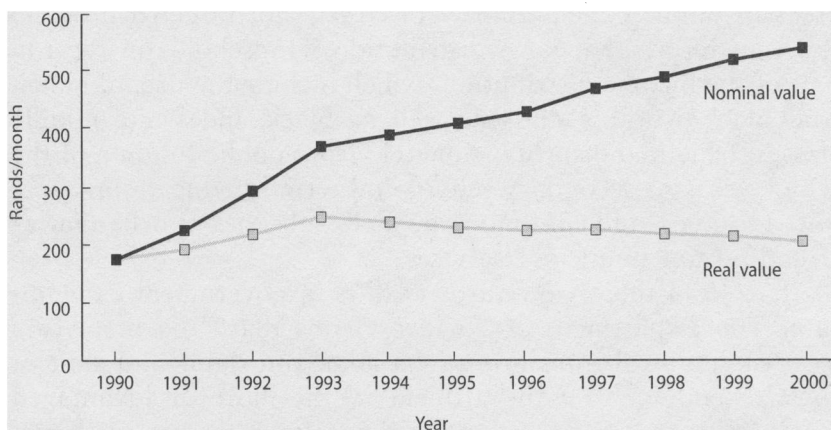
care expenditure was progressive by African standards but not by the standards of other middle-income economies.<sup>29</sup> Some areas of public expenditure were clearly not targeted progressively in terms of income distribution. Households in the top half of the income distribution, which include the urban, industrial black working class as well as black and white middle classes, benefited disproportionately from public funding of the senior years of secondary school and tertiary education, transport subsidies, and continuing de facto subsidies of urban infrastructure and municipal services.

After 1994 there were further shifts in government expenditure. The Department of Finance claims that "the first years after the political transition saw a large and significant shift of social spending from the affluent to the more disadvantaged members of society."<sup>30</sup> Taking into account government spending on welfare transfers, public education, public health, subsidies for housing, and capital expenditure on the provision of water, Van der Berg estimates that spending on the poorest 40 percent of households (i.e., the bottom four deciles) rose by about 50 percent between 1993 and 1997.<sup>31</sup> A small part of this was made possible by reduced spending on the rich, but the lion's share came from increased and well-targeted spending by the government.

However, the poor gained little in terms of cash income (through government welfare transfers). By far the most important instrument of cash redistribution through the budget is the old-age pension. As can be seen in table 2, pensions are a major source of income for the poorest 40 percent of households. In the last years of apartheid the deracialization of pension benefits was achieved through large increases in the real value of the pension paid to black people (see the 1990–1993 data in figure 2; note that the pre-1993 data in figure 2 refers to the pension paid to black pensioners only). Racial parity was achieved in 1993. Since 1993 the real value of the old-age pension has declined by an average of about 1.5 percent per year, or a total of about 20 percent (see the 1993–2000 data in figure 2).<sup>32</sup>

In addition, grants to low-income single parents were slashed, supposedly in order to free resources for improved take-up rates (i.e., the proportion of eligible claimants who actually

Figure 2. Nominal and Real Value of the Old-age Pension



Note: Pre-1993 data refers to the pension paid to black pensioners only.

Source: Department of Welfare/Social Development.

receive the grant) in poorer parts of the country. The result, in the short term, has thus almost certainly been regressive. In the longer term, improved take-up rates among the very poor might result in a more progressive outcome—but only if institutional obstacles to improved take-up rates among the poor can be overcome.<sup>33</sup>

Where the poor arguably did gain, hugely, was with respect to benefits in kind—especially in terms of public education. Van der Berg shows that the removal of indirect discrimination in teachers' salaries, together with the provision of some extra teachers and hence reduction in pupil-teacher ratios, entailed massive increases in spending in “black” schools, i.e., schools with overwhelmingly black student populations, especially in poor, rural areas.<sup>34</sup> This shift was probably driven by the political pressure of black teachers rather than a concern for the poor. But if the value of public education is deemed equal to the cost of providing it, then the poor can be said to have benefited substantially from this increase. It is unlikely, however, that the quality of schooling did improve dramatically, and in this regard the “shift” in spending toward the poor is



probably somewhat misleading. Teachers in schools in poor areas remain inadequately qualified. It is even reported that some teachers arrive at school drunk. It is probably fair to conclude that, at least in the short term, the major beneficiaries of increased educational spending were teachers (who are not poor)—and not the students sitting in their classes.

In other areas of public spending, the gains to the poor were also ambiguous. More money was spent on clinics in poor areas, but it is unclear what effect there was on the quality of the service provided. Housing policy was undoubtedly reformed in a progressive direction, but the beneficiaries were the urban poor, not the substantially worse-off rural poor. Investment in the provision of water brought clean water to many people in rural areas for the first time, but it has been reported that many pipes and taps ceased to work due to inadequate maintenance. Overall, therefore, while there were substantial shifts in the foci of spending, it is unclear how much the poor actually benefited in terms of the *quality* of the services provided.

The year 1996–1997 also proved to be the peak of government spending on social services as a percentage of the total budget. The government's projections for public expenditure for the period up to 2002–2003 indicate its plan to reduce its spending on health care, education, and welfare from just over 44 percent of the budget in 1996–1997 to less than 43 percent by 2002–2003 (see table 4).

The rising prosperity of a minority of black households combined with new government austerity with respect to social expenditure has resulted in growing numbers of black households turning away from the public sector. More than one-fifth of the population is now covered by private medical aid schemes, and this includes a fast-growing number of black people.<sup>35</sup> Similarly, many black people are members of contributory, private retirement funds. Growing numbers of better-off black parents are sending their children to semiprivate, formerly “white” public schools that charge much higher fees than public schools in formerly black areas and provide a higher-quality education. The provision of health and retirement income is increasingly linked to employment, and education is increasingly linked to income.



Table 4. Consolidated National and Provincial Spending by Function: Selected Years, 1996–1997 through 2002–2003

	1996/1997 (percent)	1999/2000 (percent)	2000/2001 (percent)	2002/2003 (percent)
Defense	5.9	4.8	5.7	6.2
Police	6.2	6.7	6.5	6.5
Justice and prisons	2.4	3.1	3.2	3.3
Education	22.4	21.4	21.1	21.0
Health	13.2	13.4	13.4	13.5
Welfare	8.6	8.8	8.7	8.3
Housing and community development	1.7	2.0	1.7	1.8
Economic services	10.0	8.5	8.6	9.1
Other	11.9	11.5	11.9	12.1
Debt Service	17.7	19.9	19.1	18.3
Total	100	100	100	100

Source: Department of Finance, *Budget Review 2000* (Pretoria: Government Printer, 2000), 140.

POLICY IMPLICATIONS

South Africa’s enduringly high level of overall inequality and even its high level of interracial inequality may be mitigated somewhat through taxation and social expenditure (including the provision of welfare). But other government policies, affecting the labor market and the overall rate and path of economic growth, serve to reproduce inequality. The imagery of “two nations” in fact serves to distract attention from the truly poor and from many of the policies that inhibit a reduction in poverty and inequality.

Access to wage employment is a key determinant of inequality in South Africa. With about a third of the workforce unemployed, job creation must clearly be at the center of any strategy designed to bring about a significant and sustainable decrease in poverty and inequality. This immediately turns the spotlight on the government’s growth strategy: to what extent have government economic policies promoted (or inhibited) job creation?

After coming to power in 1994, the ANC adopted orthodox fiscal policies. These were formalized in the “Growth, Employment and Redistribution” (GEAR) document, which promised that deficit reduction would boost growth by boosting investor confidence.<sup>36</sup> So far, the GEAR strategy has not delivered the promised benefits. Investment and output growth has been disappointing, and employment has declined (see table 5).

This lackluster performance cannot be laid entirely at the door of government. The Asian crisis and overzealous monetary policies by the independent reserve bank also acted as economic brakes. But it is nevertheless a moot point whether the ANC should have adopted such restrictive fiscal policies given the recessionary conditions of the mid- to late 1990s.<sup>37</sup> There is, for example, mounting evidence that the pursuit of anti-inflationary policies undermined growth in the developing world; South Africa is unlikely to be an exception to the rule.<sup>38</sup> Furthermore, by continuing with trade liberalization in the absence of labor-market reforms, the government probably contributed to employment losses.<sup>39</sup> Import-competing industries (particularly the ultra-labor-intensive industries) have been particularly hard hit, and South Africa’s export industries are

Table 5. GEAR Prediction versus Actual Performance

Annual growth rates	1996	1997	1998	1999
Real GDP:				
GEAR prediction	3.5	2.9	3.8	4.9
Actual performance	4.2	2.5	0.6	1.2
Private investment:				
GEAR prediction	9.3	9.1	9.3	13.9
Actual performance	6.1	4.7	-2.9	-4.4
Real wage growth (private):				
GEAR prediction	-0.5	1.0	1.0	1.0
Actual performance	1.7	2.3	8.6	3.0
Employment (non-agricultural):				
GEAR prediction	1.3	3.0	2.7	3.5
Actual performance	-0.7	-1.7	-3.7	-3.2
Conventional deficit/GDP:				
GEAR prediction	-5.1	-4.0	-3.5	-3.0
Actual performance	-4.9	-4.6	-3.3	-2.6

Source: SARB, *Quarterly Bulletin* (March 2000).

becoming increasingly capital-intensive.<sup>40</sup> Continued wage growth in the face of falling demand has no doubt also contributed to falling employment, as may have the tightening of labor-market regulation.<sup>41</sup>

South Africa's wage-setting machinery probably dampens employment growth because it enables large unions and employers to set wages that are then extended across the entire industry to the detriment of smaller, more labor-intensive firms.<sup>42</sup> GEAR claimed that wage agreements would be made more sensitive to "regional labour market conditions, the diversity of skills levels in firms of varying size, location or capital intensity."<sup>43</sup> However, this has not happened. Instead, labor-market regulation has tightened,<sup>44</sup> and even in areas earmarked as Industrial Development Zones, labor regulations and minimum wages apply, with the result that only large capital-intensive megaprojects have been attracted there.<sup>45</sup> Higher wages and reduced employment have meant that the productivity of labor has risen, and the economy has become more capital-intensive.

The combination of poor growth and pro-union labor legislation has clear effects on distribution in the short term. In the late 1990s, real wages rose at just over 2.5 percent per year, while employment fell at just under 2.5 percent per year. The unemployed have not become poorer (except insofar as they may receive less support through intra- or inter-household transfers). But the ranks of the poor and unemployed have swollen as some workers have lost their jobs. The combination of rising incomes for those with jobs and falling employment has probably led to greater inequality in the distribution of incomes in society as a whole.

Job creation could bring about a significant improvement in poverty and inequality. According to Tom Hertz, the elimination of unemployment through the creation of 3.8 million low-wage jobs would reduce the number of people in poverty by 43 percent (*ceteris paribus*) and reduce the Gini coefficient by 12 percentage points.<sup>46</sup> This result, however, assumes no change in existing wages. If new jobs could only be brought about by a reduction in existing wages, then Hertz estimates that the redistributive impact would be greatly reduced, although there would still be a reduction in absolute poverty. This points to the

importance of labor-market reforms that allow for the creation of new jobs without affecting the existing wage structure. Public-works programs and changes to the wage-setting machinery in order to create labor-intensive industries in poor, marginalized parts of the country could fall into this category. The ANC has not proceeded adequately down either path, and hence has missed an opportunity to make the growth path more redistributive.

*A Basic Income Grant?*

Gosta Esping-Andersen argues, in *The Three Worlds of Welfare Capitalism*, that welfare systems and labor-market policies work together to shape the distributive character of different versions of welfare capitalism.<sup>47</sup> In South Africa, labor-market and welfare policies were formally deracialized between the late 1970s and early 1990s, but no attempt was made to transform the system to address the problem of the unemployed poor.<sup>48</sup> To the extent that labor-market regulation constrains job creation, the system continues to foster inequality—albeit by exacerbating the divide between the employed and the unemployed rather than between the races. There is a huge gap in the welfare net with regard to income support for the unemployed. The only available unemployment support comes from the Unemployment Insurance Fund. The UIF is a contributory scheme (and hence is only available to those unemployed workers who had contributed to it while working) and only lasts for twenty-six weeks. It is thus not surprising that less than 2 percent of the unemployed draw on the UIF for support.

There are two ways of making South Africa's labor and welfare policy regime more coherent and appropriate for an economy like South Africa. South Africa is what the World Bank calls a "middle income" economy, but one with a massive surplus of labor (i.e., very high unemployment). One option would be to engage in substantial labor-market reform in order to push the economy onto a more labor-intensive growth path. This, however, is likely to be met with strong resistance from the politically powerful trade-union movement. It is also likely to be resisted by those arguing that South Africa is better off attempting to compete through upgrading the skills of the

workforce rather than competing on the basis of lower wages. The other option would be to engage in substantial welfare reform in order to provide the unemployed and marginalized with a basic income grant. This, however, will entail greater taxation of wage-earners, and hence is also vulnerable to resistance from organized labor and other constituencies.

According to estimates by Michael Samson and colleagues, it would cost R 52 billion per year to provide every individual in South Africa with a grant of R 100 a month.<sup>49</sup> This comes to about 21 percent of total government spending—i.e., more than the entire education budget, and well over twice the amount currently spent on welfare. On the face of it, the costs seem prohibitive. However, they argue that R 24 billion can be recovered from higher earners through appropriate adjustments to marginal income tax rates and tax thresholds. This leaves the net cost of transfer at R 28 billion, to be financed through further increases in taxation, including a general increase in value-added tax, a capital-gains tax, etc. There is room for this increased taxation, they argue, because South Africa's average tax rate is 26 percent, compared to 32 percent in countries at similar levels of development.<sup>50</sup> More optimistically, they go on to argue that a basic income grant would have positive spin-offs for growth (in terms of increased labor productivity and demand) and therefore partially pay for itself over time.

There are at least three problems with this proposal. First, it does not take into account the administrative costs of delivering the grant to all individuals. The costs of delivering pensions (excluding the salaries of administrators) varies from R 13 per month in the Western Cape to R 70 per month in provinces with a high proportion of pensioners living in remote, undeveloped areas.<sup>51</sup> This amounts to between 2.5 percent and 13 percent of the grant. Second, the study does not account for the possibility that some of the increased taxation (for example, increases in VAT) will be passed on to the poor in the form of higher prices, thereby lessening the redistributive impact of the grant. Third, and probably most important, the proposal is far too sanguine about increasing the burden of taxation. South Africa may have a lower proportion of tax revenue to GDP than other comparable countries, but given that most income tax (and future

capital-gains tax) is paid by the very top end of the income distribution, talking in terms of average tax rates is not very helpful. South Africa's top income earners are already highly burdened, and it is thus likely that significant and sustainable increases in tax revenues could only come about through either adding to the income tax burden of households in, especially, the seventh and eighth deciles (i.e., the labor movement's chief constituency) or increasing value-added tax. If the burden falls mainly to value-added tax, then the redistributive impact of the basic income grant will be reduced, as the poor will be paying for part of it every time they spend on goods and services. At present both the trade-union movement and the Democratic Party (representing most of the rich) profess support for a basic income grant, but both seem to anticipate that their constituencies will not shoulder the financial burden.

Nonetheless, the basic income grant proposal is important as it highlights a central policy dilemma in South Africa today: how to provide basic income support in a middle-income labor-surplus society. Given that wage earners are protected relative to the unemployed, the moral and political *quid pro quo* is higher taxation in order to finance a basic income grant for the unemployed. The attraction is that the deal does not entail any erosion of labor standards or hard-won rights. But it does entail higher taxation, and there is little indication that the organized working class is any more prepared to countenance higher taxation than it is to agree to greater labor-market flexibility. There remain major political obstacles to crucial redistributive reforms.<sup>52</sup>

## CONCLUSION

The image of a divided nation is important in highlighting the extreme level of inequality in post-apartheid South Africa. But Mbeki's portrayal of "two nations" is inadequate. South African inequality is not simply or even primarily interracial. Declining *interracial* inequality has not reduced overall inequality, and will not do so in the future, because the factors that drive inequality have become increasingly significant at the *intraracial* level. In a society that has become dependent on wages and

salaries, a reduction in inequality requires a more egalitarian educational system, broader access to employment (through job creation), and, perhaps, reforms to the welfare system that direct more resources to the poor, whether elderly or not. Insofar as South Africa comprises a divided nation, it is perhaps most accurate to see it in terms of three broad classes, not two racially defined nations: an increasingly multiracial upper class, comprising not just high-profile corporate figures but much more broadly the professional, managerial, and business classes; a “middle” class of mostly urban, employed workers; and a marginalized class of outsiders, comprising many of the unemployed as well as workers in agricultural and domestic employment.

## ENDNOTES

<sup>1</sup>*Hansard*, 29 May 1998, col. 3378.

<sup>2</sup>This data is from the 1993 survey of the Southern African Labour and Development Research Unit (SALDRU) at the University of Cape Town. See also the 1999 survey funded by the Kaiser Foundation and widely reported in the press in April/May of 1999.

<sup>3</sup>Benjamin Disraeli, *Sybil, or The Two Nations* (London: Macmillan, 1845/1930), 74.

<sup>4</sup>Jeffrey Williamson, *Did British Capitalism Breed Inequality?* (London: George Allen and Unwin, 1985); Jeffrey Williamson, “British Inequality during the Industrial Revolution: Accounting for the Kuznets Curve,” in Y. S. Brenner, Hartmut Kaelble, and Mark Thomas, eds., *Income Distribution in Historical Perspective* (Cambridge: Cambridge University Press, 1991); and W. D. Rubinstein, *Wealth and Inequality in Britain* (London: Faber and Faber, 1986).

<sup>5</sup>Andrew Hacker, *Two Nations: Black and White, Separate, Hostile, Unequal* (New York: Charles Scribner’s Sons, 1992).

<sup>6</sup>There is a further irony in the origins of the “two nations” imagery: Disraeli, later the prime minister of Britain, was a key figure in social Toryism, the reformist wing of British conservatism that sought to rebuild the party on a multiclass basis. Disraeli was a strong exponent of the expanded franchise and the need for a *cross-class* alliance. He stood for amelioration, not redistribution; patrician responsibility rather than radicalism. His One Nation conservatism entailed responsible patrician leadership rising above class loyalties in the national interest. See, e.g., John K. Walton, *Disraeli* (London: Routledge, 1990).



- <sup>7</sup>Quoted in Claude S. Fischer et al., *Inequality by Design: Cracking the Bell Curve Myth* (Princeton, N.J.: Princeton University Press, 1996), 3.
- <sup>8</sup>Andrew Whiteford and Dirk Van Seventer, "Winners and Losers: South Africa's Changing Income Distribution in the 1990s," WEFA Southern Africa, Pretoria, 1999; and Michael Carter and Julian May, "One Kind of Freedom: Poverty Dynamics in Post-Apartheid South Africa," unpublished paper, University of Wisconsin, December 1999.
- <sup>9</sup>Whiteford and Van Seventer, "Winners and Losers: South Africa's Changing Income Distribution in the 1990s," 9.
- <sup>10</sup>*Ibid.*, 14.
- <sup>11</sup>*Ibid.*, 44.
- <sup>12</sup>Murray Leibbrandt, Haroon Borat, and Ingrid Woolard, "Understanding Contemporary Household Inequality in South Africa," DPRU Working Papers No. 99/25, Development Policy Research Unit, University of Cape Town, May 1999, have shown that such estimates vary according to the statistical technique and data source used.
- <sup>13</sup>Shula Marks, *Divided Sisterhood* (New York: St. Martin's Press, 1994), 173–174.
- <sup>14</sup>*Ibid.*, 173; John Knight and Michael McGrath, "An Analysis of Racial Wage Discrimination in South Africa," *Oxford Bulletin of Economics and Statistics* 39 (1977): 258.
- <sup>15</sup>Peter Moll, "Discrimination is Declining in South Africa but Inequality is Not," SANER Working Paper no. 5, South African Network for Economic Research, Cape Town, 1998.
- <sup>16</sup>T. P. Schultz and G. Mwabu, "Wage Premia for Education and Location, by Gender and Race in South Africa," Economic Growth Center, Discussion Paper no. 785, Yale University, February 1998; Schultz and Mwabu, "Labor Unions and the Distribution of Wages and Employment in South Africa," *Industrial and Labour Relations Review* 51 (4) (1998): 680–703; Moll, "Discrimination is Declining in South Africa but Inequality is Not"; and David Lam, "Generating Extreme Inequality: Schooling, Earnings, and Intergenerational Transmission of Human Capital in South African and Brazil," *Research Report* no. 99–439, Population Studies Center at the Institute for Social Research, University of Michigan, 1999.
- <sup>17</sup>Schultz and Mwabu, "Wage Premia for Education and Location, by Gender and Race in South Africa."
- <sup>18</sup>Julian Hofmeyr, *An Analysis of African Wage Movements in South Africa*, Research Monograph No. 9, Economic Research Unit, University of Natal, 1994; and Owen Crankshaw, *Race, Class and the Changing Division of Labour under Apartheid* (London: Routledge, 1997).
- <sup>19</sup>Schultz and Mwabu, "Labor Unions and the Distribution of Wages and Employment in South Africa," 700.
- <sup>20</sup>According to Schultz and Mwabu, if the union relative wage effect were cut in half, then black employment would increase by about 2 percent: "There



would be a redistribution of wage payments from the upper-middle class African union workers to lower-wage nonunion workers and the marginalised poor who are often now not actively participating in the labour market." *Ibid.*, 701.

- <sup>21</sup>Jeremy Seekings, "Visions of Society: Peasants, Workers and the Unemployed in a Changing South Africa," *Journal for Studies in Economics and Econometrics* 24 (3) (November 2000).
- <sup>22</sup>OECD, "Recent Labour Market Developments and Prospects: Special Focus on the Patterns of Employment and Joblessness from a Household Perspective," *Employment Outlook* (June 1998): 24.
- <sup>23</sup>See also Gita Kingdon and John Knight, "What is the Appropriate Definition of Unemployment?" presented to the Seminar on Unemployment in South Africa, Institute for Economics and Statistics, Oxford University, 10 November 1999.
- <sup>24</sup>Steffen Schneier, "Occupational Mobility among Blacks in South Africa," working paper no. 58, South African Labor and Development Research Unit, University of Cape Town, 1983.
- <sup>25</sup>Michael McGrath, C. Janisch, and C. Horner, "Redistribution through the Fiscal System in the South African Economy," paper presented to the Economics Society of South Africa conference, Potchefstroom, 1997. See also Servaas Van der Berg, "Trends in Racial Fiscal Incidence in South Africa," unpublished paper, 1998.
- <sup>26</sup>See Inter-American Development Bank (IADB), *Facing Up to Inequality in Latin America* (Washington, D.C.: IADB, 1999); Branko Milanovic, "Do More Unequal Countries Redistribute More?" unpublished paper, World Bank, Washington, D.C., 1999.
- <sup>27</sup>Elizabeth Ardington and Francie Lund, "Pensions and Development: Social Security as Complementary to Programmes of Reconstruction and Development," *Development Southern Africa* 12 (4) (1995).
- <sup>28</sup>Lam, "Generating Extreme Inequality."
- <sup>29</sup>F. Castro-Leal, J. Dayton, and K. Metra, "Public Social Spending in Africa: Do the Poor Benefit?" *World Bank Research Observer* 14 (1999).
- <sup>30</sup>On the basis of calculations by Van der Berg; Department of Finance, *Budget Review 2000* (Pretoria: Government Printer, 2000), 15.
- <sup>31</sup>Servaas Van der Berg, "An Analysis of Fiscal Incidence of Social Spending in South Africa, 1993–97," report to the Department of Finance, South Africa, 2000.
- <sup>32</sup>It is possible that take-up rates among poor elderly people improved (*ibid.*), but other studies (such as Ann Case and Angus Deaton, "Large Cash Transfers to the Elderly in South Africa," *Economic Journal* 108 [450] [1998]: 1330–1361) found that take-up rates were very high by 1993.
- <sup>33</sup>IDASA, *Poverty Profile, Special Edition on Child Maintenance Reforms* (Cape Town: IDASA Poverty Monitoring Service, April 1994); IDASA, "Submis-

sion to the Portfolio Committee on Finance on the 2000/2001 Budget," 3 March 2000.

- <sup>34</sup>Van der Berg, "An Analysis of Fiscal Incidence of Social Spending in South Africa, 1993-97"; Van der Berg, "An Analysis of 1997 School Data Flowing From Work on the Fiscal Incidence of Social Spending in South Africa," report to the Department of Finance, South Africa, 2000.
- <sup>35</sup>Marius Olivier et al., "Social Insurance and Social Assistance: Towards a Coherent Approach," report for the Department of Welfare, South Africa, 1999, 152.
- <sup>36</sup>Department of Finance, *Growth, Employment and Redistribution* (Pretoria: Government Printer, 1996).
- <sup>37</sup>See, e.g., John Weeks, "Stuck in Low GEAR? Macroeconomic Policy in South Africa, 1996-98," *Cambridge Journal of Economics* 23 (4) (1999).
- <sup>38</sup>Joseph Stiglitz, "More Instruments and Broader Goals: Moving Towards the Post-Washington Consensus," WIDER Annual Lectures 2, UNU World Institute for Development Economics Research, Helsinki, 1998.
- <sup>39</sup>Nicoli Nattrass, "Globalisation and the South African Labour Market," *Journal for Studies in Economics and Econometrics* 22 (3) (1998).
- <sup>40</sup>This is not to say that the net impact of trade liberalization has been to reduce jobs. Indeed, there is evidence that the overall impact has been marginally positive as export industries have helped boost labor-intensive down-stream industries like transport and services. Lawrence Edwards, "Globalisation and the Skill Bias of Occupational Employment in South Africa," unpublished paper, School of Economics, University of Cape Town, 2000. The point is simply that a more flexible labor market would probably have reduced the negative impact of trade liberalization. Trevor Bell and N. Cattaneo, *Foreign Trade and Employment in South African Manufacturing Industry*, occasional report no. 4 (Geneva: Employment and Training Department, International Labor Office, 1997); ILO (drafted by S. Hayter, G. Reinecke, and R. Torres), *South Africa: Studies on the Social Dimensions of Globalisation*, final draft, February 1999, Task Force on Country Studies on Globalization, International Labor Office, Geneva.
- <sup>41</sup>Most calculations of employment elasticity in South Africa indicate that the labor demand curve is relatively elastic. Estimates range from -0.66 to -0.85, which suggests that a 10 percent increase in wages will result in a drop in employment of between 6.6 percent and 8.5 percent (reported in the EAGER Report [10] [Spring 1999]: 7). F. Barker, "On South Africa's Labour Policies," *South African Journal of Economics* 67 (1) (March 1999): 1-33.
- <sup>42</sup>Peter Moll, "Compulsory Centralisation of Collective Bargaining in South Africa," *American Economic Review: Papers and Proceedings* 82 (2) (1996): 326-329; Nicoli Nattrass, "Inequality, Unemployment and Wage-Setting Institutions in South Africa," *Journal for Studies in Economics and Econometrics* 24 (3) (November 2000).
- <sup>43</sup>Department of Finance, *Growth, Employment and Redistribution*, 18.
- <sup>44</sup>Barker, "On South Africa's Labour Policies."

<sup>45</sup>ILO, *South Africa: Studies on the Social Dimensions of Globalisation*, 25.

<sup>46</sup>Tom Hertz, *The Relationship between Poverty, Inequality and Unemployment in South Africa*, SANER Working Paper no. 9, South African Network for Economic Research, Cape Town, 1998.

<sup>47</sup>Gosta Esping-Andersen, *The Three Worlds of Welfare Capitalism* (Princeton: Princeton University Press, 1990).

<sup>48</sup>Nicoli Natrass and Jeremy Seekings, "Citizenship and Welfare in South Africa: Deracialisation and Inequality in a Labour-Surplus Economy," *Canadian Journal of African Studies* (1997): 452–481.

<sup>49</sup>Michael Samson et al., "The Macroeconomic Implications of Poverty-reducing Income Transfers," paper presented to the conference Towards a Sustainable and Comprehensive Social Security System, hosted by the Institute for Social Development, University of the Western Cape, 2000.

<sup>50</sup>Department of Finance, *Budget Review 2000*, 17.

<sup>51</sup>V. Peterson, "The Payment of Pensions," paper presented to the conference Towards a Sustainable and Comprehensive Social Security System.

<sup>52</sup>See, in general, Nicoli Natrass and Jeremy Seekings, "Democracy and Distribution in Highly Unequal Economies: The Case of South Africa," paper presented at a conference on Democracy and Distribution, Yale University, 1999.