

**Income and Non-Income Inequality in Post-Apartheid
South Africa: What are the Drivers and Possible
Policy Interventions**

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1. Introduction

South Africa has historically been ranked as one of the most unequal societies in the world, and while the country has experienced sustained positive economic growth since 1994, besides the 18 months ending December 2009 which showed a negative growth. The impact of this growth on poverty, and particularly inequality, has been disappointing.

- **Analysis using data from the 1995 and 2000 Income and Expenditure Surveys** has found, for example, a significant increase in income inequality over the period and, further, that this increase in inequality eroded any significant poverty-reduction gains from higher economic growth.
- **The release of the Income and Expenditure Survey 2005** has enabled us to now examine changes in inequality over the 10-year period between 1995 and 2005.

This Policy Brief excludes a number of aspects that are covered in great detail within the paper, as it attempts to only highlight the significant data that has affected inequality generally.

Some preliminary analysis, however, shows a further increase in inequality over the second half of the period. This new result would possibly suggest that South Africa is now the most consistently unequal economy in the world. Critically, the persistent and increasing levels of inequality have been acting as a constraint to ensuring that South Africa's economic growth results in significant declines in household poverty levels.

There are two main objectives stipulated in the paper:

- The **first objective** is to provide a comprehensive overview of the changing levels of inequality in the post-apartheid South Africa and to identify the drivers of these changes. This also includes examining the relationship between economic growth, poverty and inequality over the period.
- The **second objective** is to evaluate the increased provision of social grants as a policy option to alleviate the impact of increasing inequality in South Africa.

The last section of the paper reviews the impact of Government's provision of social grants on income inequality. While the results from the decomposition of income inequality in the first section of the paper suggest that social grants as a source of income did not serve to reduce income inequality, **further analysis do show that social grant income made a significant contribution to total income across the income distribution, particularly in 2005.**

2. Shifts in Inequality in Post-Apartheid South Africa

The methodologies of data collection as well as the questions themselves differ slightly between the two surveys and for the purposes of our analysis **the paper looks at carefully constructed total household income aggregates for 1995 and 2005. Only those sources of income that were included in both datasets were used to estimate total income.** The paper shows a match of the majority of income sources for the two years and only a very small share of income was excluded from the final total income aggregates with negligible implication for our inequality estimates.

- **All individuals**, irrespective of race and the gender of the household head, **experienced statistically significant increases in their nominal per capita household incomes between 1995 and 2005.**
- **At the aggregate level, nominal incomes more than doubled over the decade**, with slightly lower growth experienced by African and Asian individuals.

When the impact of inflation over the period is taken into account, the increase in real income at the aggregate level was only about 11.5 percent. White individuals, followed by Coloured individuals, experienced the largest increases in their real income, with increases of 40.5 and 35.2 percent respectively. Individuals living in male headed households experienced an increase of about 24 percent in their real incomes over the decade. However, **in real terms, Africans, Asians and individuals living in households headed by females, did not experience any statistically significant change in their incomes over the period.**

The South African society has historically been characterised by high levels of income inequality and **the paper gives an overview of the changes in income inequality between 1995 and 2005.**

Three standard measures are utilised namely:

- **the Gini coefficient,**
- **the Lorenz Curve** and
- **the Theil index**

These measures are complementary to each other as they are able to describe the extent and nature of inequality in different ways. **The Gini coefficient is derived from the Lorenz Curve, which is a graphical depiction of income distribution.** In contrast to the Gini coefficient, **the Theil index is neither intuitive nor easy to interpret.** However, its one advantage is that it has the ability to decompose overall inequality into a proportion originating between subgroups and a proportion originating within subgroups. Thus, for example, overall inequality can be decomposed by race, with a certain proportion of overall inequality being explained by inequality between the race groups, and the remainder being explained by within race groups.

Generally the inequality measures show that income inequality has increased considerably across race groups over the period under consideration.

The paper may suggest that **the provision of social grants has not been as well-targeted as previously thought,** it is important to remember that even in the lowest income group (shown in detail in the paper), mean per capita incomes can be very low. In fact, in 2005:

- **the annual mean per capita income was only around R8 800 and in the same year,**
- **the value of the Old Age Pension was R780 a month (National Treasury, 2005) or R9 360 a year – which is more than the mean income in the lower and lowest household earnings.**

2.1 Wage Income as a Driver of Income Inequality

The analysis of income inequality in the paper has made it clear that

- **wage income is the leading contributing factor to income inequality.** In addition,
- **its contribution to income inequality has increased between 1995 and 2005.**

Hence, it is unmistakable that wages remain the factor explaining income inequality, but its importance in explaining that income inequality has been further entrenched over the years. If we can understand what factors are driving wage income, and which portion of the distribution of households have access to wage income, then it may then be possible to improve our understanding of income inequality.

Since wage inequality is the most important contributing factor to income inequality, a more detailed analysis into wage inequality is warranted. Given the limitations of the IES, a more detailed analysis of wage distribution using these datasets is not possible. So the paper draws on existing evidence from studies using other datasets to explain the inequality found within wages. Borhat and Goga (2008) investigate wage inequality using the 2001 and 2006 Labour Force Survey of South Africa.

- **Wage inequality is first measured by estimating the Gini coefficient for real wages and secondly by analysing the differences in the distribution of real wages.**
- **While they find that the Gini coefficient has remained relatively stable between 2001 and 2006, their analysis of changes in the wage differential shows that there has been a decrease in the overall wage inequality.**
- **But this was only because of the social grants going to lower-, middle- and upper-income groups which contributes as much as 20 percent to household income across the board.**

The only significant decrease in inequality was noticed in the sector of self-employment.

- **By 2005, the relative contribution of income from self-employment to total income had declined by almost 50 percent in lower- to middle-income groups,**

- **while all upper-income groups show an increase in the share of total income attributed to self-employment.**

In fact, it appears as if the average contribution of this income source was between five and ten percent in the bottom incomes, with a larger share in the upper-income bracket. This relatively larger share in the upper-income groups accounted for the positive contribution of this source to total income inequality.

2..2 Changes in Non-income Inequality

The evidence presented in the previous section has shown that South Africa's levels of income inequality have increased between 1995 and 2005. With a few minor exceptions, this trend was observed to be invariant with respect to race, location and the gender of the household head. The paper also finds that the increase in income inequality was driven by increasing levels of wage inequality. Importantly, however, it would be imprudent to ignore other indicators of living standards, such as access to basic services and private assets. Access to basic services is an important measure of living standards as it has a direct impact on the quality of life of the population (Leibbrandt et al 2006).

Aggregate non-income inequality has decreased significantly between 1993 and 2005 and this decline in non-income inequality stands in direct contrast to the substantial increase in income inequality between 1995 and 2005.

- **The improvement in the levels of non-income inequality is largely the result of the increased access to public services** (see Bhorat et al 2007 for a more detailed discussion), especially in **the lower household expenditure bracket.**

The African population also experienced a significant decrease in non-income inequality. Importantly,

- **non-income inequality for the African population remains higher than non-income inequality at the aggregate level and for the other race**

groups. (The changes in non-income inequality for the other race groups are not statistically significant).

- **While the African population has benefited significantly from the increase in the provision of basic services since 1994, a large share of the African**

population remains without access to water, electricity, housing and sanitation.

- Addressing these major backlogs in the delivery of basic services will serve to further reduce non-income inequality in the country.

Overall then, the evidence presented in this section has shown that,

- **in contrast to the shifts in income inequality, non-income inequality – as measured using a basic services index – has decreased at the aggregate, for African households, in most provinces and for both male and female headed households.**
- However, **significant backlogs still exist.** This highlights **the opportunity for government to further impact on the levels of non-income inequality by targeting the delivery of basic services to those households that still do not have access to basic housing, water, electricity and sanitation.**

3. The Relationship between Economic Growth, Poverty and Inequality: 1995 – 2005

There is very little debate, if any, amongst economists around the notion that

- **a high level of economic growth is essential for poverty reduction.**
- Indeed, increased growth rates, effectively measured by rising per capita incomes, would appear to make this link clear and simple:
 - if you increase economic growth, poverty levels will fall in the society.
 - As incomes grow, there is a high likelihood that this will also affect the distribution of that income.
 - Put differently, economic growth often brings with it, some change in the levels of income inequality.
 - When this occurs and if the result is an increase in inequality, the gains from growth to the poor may in fact be reduced.
- **Higher inequality levels from growth ‘stretch’ the distribution of income** and in so doing dilute the impact of economic growth on poverty.

Given these two caveats to the growth-poverty nexus then, the critical insight is that economic growth may be necessary, but it is certainly not a sufficient condition for poverty reduction in a society.

The evidence presented in the paper also shows that over the same period,

- **all South Africans experienced rising income inequality.** The objective of this section is therefore to **examine the relationship between economic growth, inequality and poverty between 1995 and 2005 and particularly the impact of the increasing income inequality on poverty levels.**
- It is clear that **the growth in per capita income was not pro-poor in the relative sense.** While the GIC may be above zero and thus meets the weaker criterion of pro-poor growth, it is upward sloping and confirms the results from the previous section which showed that inequality has increased significantly over the period, with the rich experiencing faster growth in their per capita incomes than the poor.
- Growth may be considered pro-poor in a relative sense if the change in the income levels of the poor is larger than the change in the income levels of the non-poor
- **However, none of the individuals in the bottom 30 percent of the distribution experienced growth in per capita income higher than the mean growth rate.**
- **The White population generally experienced higher growth rates in per capita income than other race groups, with the African population exhibiting the lowest growth rates when compared to their White and Coloured counterparts.**
- **Asians at the bottom of the income distribution experienced negative growth rates over the period.**

Specifically, the wage premium paid to highly skilled workers is one of the main contributing factors to wage inequality. The result presented may reflect the fact that highly skilled and highly paid workers generally reside in urban areas.

To summarise then, while all individuals experienced absolute pro-poor growth in South Africa between 1995 and 2005, those at the top end of the distribution experienced higher growth rates than those at the bottom. This result holds true across race, location and gender of the household head and confirms a growth

trajectory marked by a decrease in poverty levels, but sharply rising income inequality.

4. Policy Interventions to Mitigate the Impact of Rising Inequality in South Africa

The evidence presented has clearly shown that **wage inequality** is undoubtedly the **leading cause of income inequality**. Not only is

- **wage income the greatest source of income**, but
- **the distribution of it is highly skewed**, with labour market participants being rewarded for the type (or level) of skill owned.

While little can be done in the short-term to dampen the effect of wage inequality on income inequality, **government can redistribute income via other means such as the provision of social grant income to poor households**.

4.1 *The Impact of the Increased Provision of Social Grants*

One of the policies that government has implemented quite successfully is the provision of social grants. These grants are generally well targeted and mostly reach the poorest of the poor. Grants are targeted at **the most vulnerable members of society**, specifically **the disabled, the aged and children**. **Grant income has been found to make a substantial contribution to total income**, and is often used to support an entire household.

- **The provision of grants accelerated after 2000.**
- **Grant expenditure increased from R20 553 million in 2001/02 to R51 927 million in 2005/06**, which represents a 26.1 percent growth in social assistance expenditure by the government.
- **The number of grant beneficiaries increased significantly over this relatively short period, from 3.61 million to 9.40 million.**

While all grants experienced a significant increase in the number of beneficiaries between 2001 and 2005, **the number of Child Support Grant recipients increased from 975 000 in 2001 to 5.6 million in 2005**. This surge was due to both the

increased public awareness of the grants and the extension of the grant to children up to the age of 14 years (Pauw & Mncube 2007).

A key aspect of the post-apartheid fiscal expenditure patterns has therefore been a widening and deepening of South Africa's social security system.

- The paper shows **per capita grant income as a proportion of total per capita household income for South Africa between 1995 and 2005.**
- **It also shows that grant income has contributed significantly to total per capita income in particularly in 2005.**

This confirms that not only has grant income been an important source of income for the poor, but that the share of grant income in total household income has increased significantly over the period. In 1995 the share of grant income in total per capita income was relatively low. This reflects the relatively limited number of South Africans who were grant recipients over that period. **Even in the low -to no-income households, grant income only contributed about 35 percent to total income in 1995.** The number of grant beneficiaries and therefore the contribution of grant income to total income increased significantly between 1995 and 2005.

Furthermore, we observe that grant income has become an important contributing source to total income in all the lower-income households. For example, grant income accounted for almost 40 percent of total income for the lower- to middle-income households and ten percent for the middle- to upper-income households. This result is driven by the fact that individuals in this income bracket had such low levels of income in the absence of grants that they qualified to receive social grants.

4.2 Social Grants as a Suppressor of Income Inequality

The paper

- **compares two GICs (Growth Incidence Curve), with grant income included and excluded respectively.**
- **It also shows the impact of the provision of social grants on the growth rates at different percentiles of the income distribution.**

The results are quite striking, as the average annual growth rates for those at the bottom of the income distributing becomes negative in the absence of social grants. In fact, the percentile growth rates are negative up to about the upper-income percentile of the distribution. Hence, in the absence of the provision of grant income growth would not have been pro-poor even in the absolute sense over the period.

The mean percentile growth rate is also significantly lower at 1.7 percent when grant income is excluded, compared to 4.8 per cent when grants are included as a source of income. These results confirm the critical role of the provision of social grants specifically in the African population sub-group in rural areas. **The growth rates at the aggregate and for rural areas are quite similar when total income, including grants, is considered.** In the absence of social grants, the rural poor would have experienced severe negative growth rates. This result reflects the significance of social grants in the government's **fight against poverty and inequality in rural areas**, which generally have higher unemployment rates and more limited employment opportunities when compared to urban areas.

The importance of grant income, especially for individuals residing in rural areas, raises many questions around the policy options available in the fight against the impact of rising inequality. The rate at which grants are rolled out is unsustainable, and it would be imprudent for the state to increase the number of grant beneficiaries at the same rate as in the past. The state should consider implementing complimentary policy measures to the roll out of grant income, such as strengthening labour market policies and the education system. This would make it easier for labour market entrants to secure employment which would make it easier to wean the South African society off the social security system that we so desperately depend on.

5. Conclusion

The results from the paper confirm the perception that South Africa is one of the most unequal societies in the world as income inequality increased significantly between 1995 and 2005, irrespective of race, gender of household head and location. **An unexpected result was that income inequality *between* race groups, rather than income inequality *within* race groups was the leading cause of the increasing levels of income inequality.** The result was unexpected, since previous research using data from a shorter time period, suggested that it was income inequality within race groups (driven by higher levels of African inequality) that was causing the increase in income inequality.

The paper also found that most of the potential poverty gains of economic growth were eroded by the rising levels of income inequality within South Africa. In addition, economic growth became less pro-poor over time. **Higher growth rates are therefore needed to compensate for the rising inequality.** It is unlikely that South Africa would be able to sustain higher growth rates, and so alternative policies are needed which would aid poverty reduction.

One such policy that the South African Government has successfully implemented is **the increased provision of social grants.** Not only did more individuals have access to grant income, but grant income also accounted for a greater proportion of total income over time. **The increased provision of grant income has helped to suppress the increase in income inequality as shown by the large differences in the Gini coefficient and the GIC curve, when grant income is included and excluded as a source of income.** This is especially true for individuals living in rural areas, as their heavy reliance on grant income explains why rural areas were better off than their urban counterparts when their GICs including grant income were compared.