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Should and can labour-surplus, middle-income economies pursue labour-intensive growth? The South African Challenge

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Should and can labour-surplus, middle-income economies pursue labour-intensive growth? The South African Challenge

Abstract

South Africa's industrial policy rests on Michael Porter's logic of raising productivity to promote dynamic competitive advantage. Given high unemployment, however, a more Arthur Lewis-like emphasis on labour-intensive development is also appropriate. Contrary to conventional wisdom, evidence from sectors such as clothing shows that South African producers remain sufficiently competitive as long as minimum wages are not raised in pursuit of a Porterian strategy. The South African case suggests that it is both desirable and feasible for an industrialised labour-surplus, middle-income economy like South Africa to pursue a mix of strategies including the promotion rather than destruction of labour-intensive jobs.

Introduction

Standard development theory suggests that governments should select strategies depending on where they are in the development process. The Caribbean economist Arthur Lewis famously argued that for developing countries with 'unlimited' supplies of labour absorbed in low-productivity agriculture, an appropriate development strategy entailed relatively low-wage, labour-intensive industrialisation (Lewis, 1954). As economies developed – or industrialised, in Lewis' model – labour markets became tighter. Michael Porter later emphasised the role that government intervention could play to promote 'dynamic competitive advantage', especially in the face of rising competition from low-wage countries (1985; 1990). But neither Lewis nor Porter imagined that an effectively unlimited supply of unskilled labour might persist in an upper middle-income country (in terms of GDP per capita) with a diversified economic base. South Africa is such a case.

By the end of the apartheid era, in the early 1990s, South Africa had an exceptionally high unemployment rate and an unusually low employment rate.

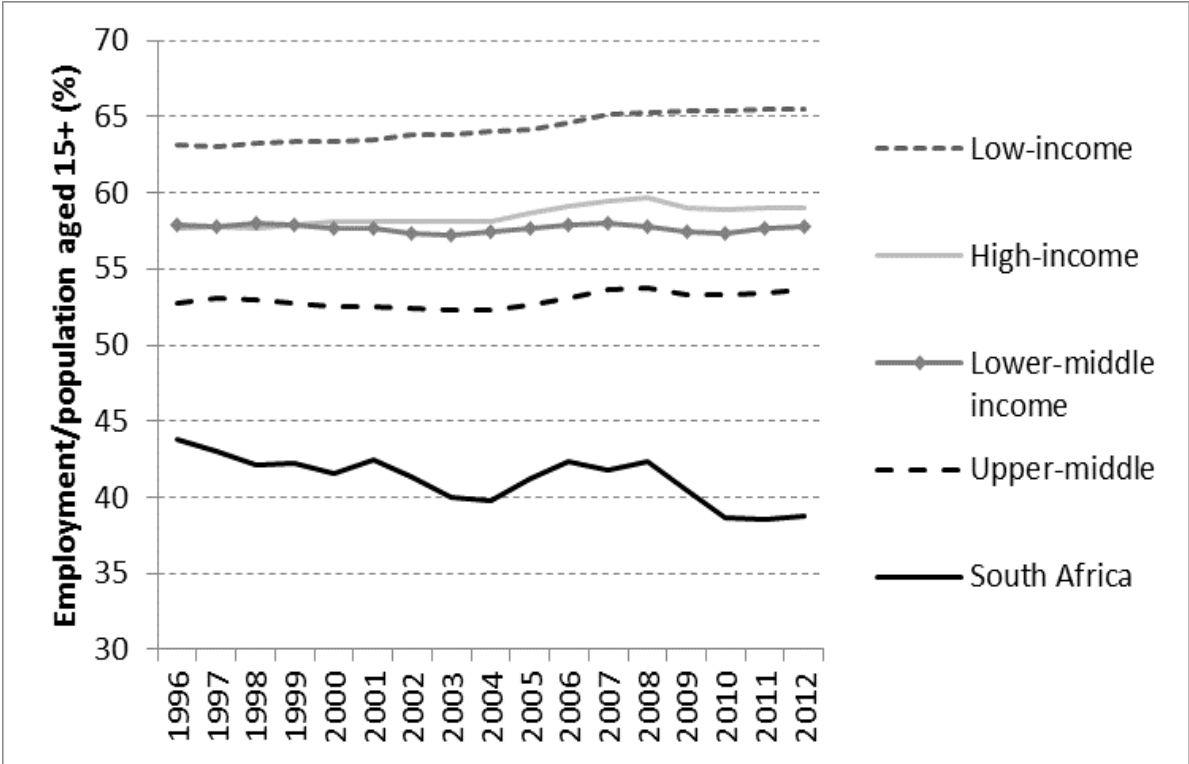
Despite this, post-apartheid governments pursued a broadly Porterian strategy, using labour market and industrial policies to raise labour productivity to support ‘decent work’. This contributed, over the two decades since the transition to democracy in 1994, to very modest employment growth. The employment elasticity of growth has been low, compared to other upper middle-income economies – despite South Africa’s exceptional unemployment. In this paper we argue that some labour-intensive production is not only desirable, but also feasible – despite globalisation and competition from lower-wage countries. Economies with a developed industrial sector and a serious unemployment problem can and should combine a Porterian productivity-raising strategy in some (established, advanced) sectors with a Lewisian labour-intensive strategy in others.

South Africa’s unemployment problem in comparative perspective

Creating income through employment has long been a development objective. The Preamble to Part XIII of the Treaty of Versailles, under which the International Labour Organisation (ILO) was established, includes the ‘prevention of unemployment’ and the ‘provision of an adequate living wage’ as some of the changes required for social justice and universal peace. The ILO’s convention 131 (1970) on minimum-wage setting advises policy-makers to balance social factors such as relative living standards and economic factors, including ‘the desirability of attaining and maintaining a high level of employment’ (Article 3).

Figure 1 shows that across the world as a whole, the employment rate in middle-income countries in the early 2000s remained steady at about 55 percent and in low-income countries rose to more than 65 percent in 2012. Figure 2 provides data on average unemployment rates, showing that they fluctuated globally within a narrow range of between 5 and 7 percent. South Africa is a spectacular contrast: An economy that, for about 40 years, failed to provide sufficient jobs for those who wanted them. This failure began in the 1970s as a combination of rising manufacturing wages (Hofmeyr, 1994) and lack-luster growth generated high and rising open unemployment (Seekings and Nattrass, 2005: Ch.5). The failure deepened in the final years of apartheid, and then persisted into the 1990s and 2000s. As shown in Figure 1, South Africa’s employment rate (employment / population aged 15 and above) was already, in 1996, very low relative to other

countries (at almost 45 percent),¹ but then worsened, to about 40 percent in the early 2000s. After a short-lived improvement, it fell even further – and behind the average for other countries – after the 2008 financial crisis. South Africa’s unemployment rate is similarly high by international standards (Figure 2). This, along with rising earnings inequality, is the key determinant of South Africa’s extremely high level of inequality (Leibbrandt *et al.*, 2012).



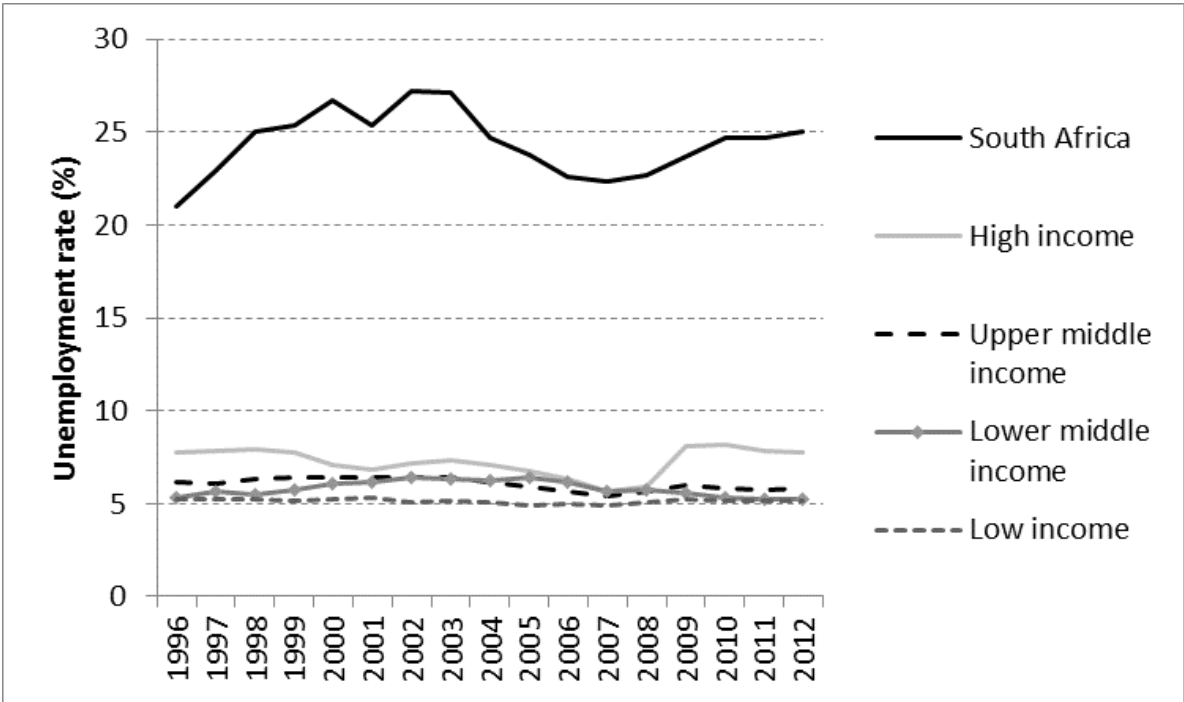
Source: World Development Indicators (data modelled by the International Labour Organisation. Available at: <http://data.worldbank.org/data-catalog/world-development-indicators>).

Figure 1: Employment rates (employment/ population aged 15 years and above)

Low employment rates imply that a country is not fully utilising its available human resources. But as not all people of working age are in the labour market, a better measure of social stress is the unemployment rate (unemployment/ labour force). Figure 3 plots employment and unemployment rates of 79 middle-income countries for which data are available. It shows that South Africa, together with its *de facto* satellites of Lesotho and Swaziland, have

¹ Data for employment and unemployment in South Africa prior to 1993 are suspect, and the standard data for 1995 are based on a survey subsequently shown to have sampling flaws (Wittenberg, 2014). We therefore report data from 1996.

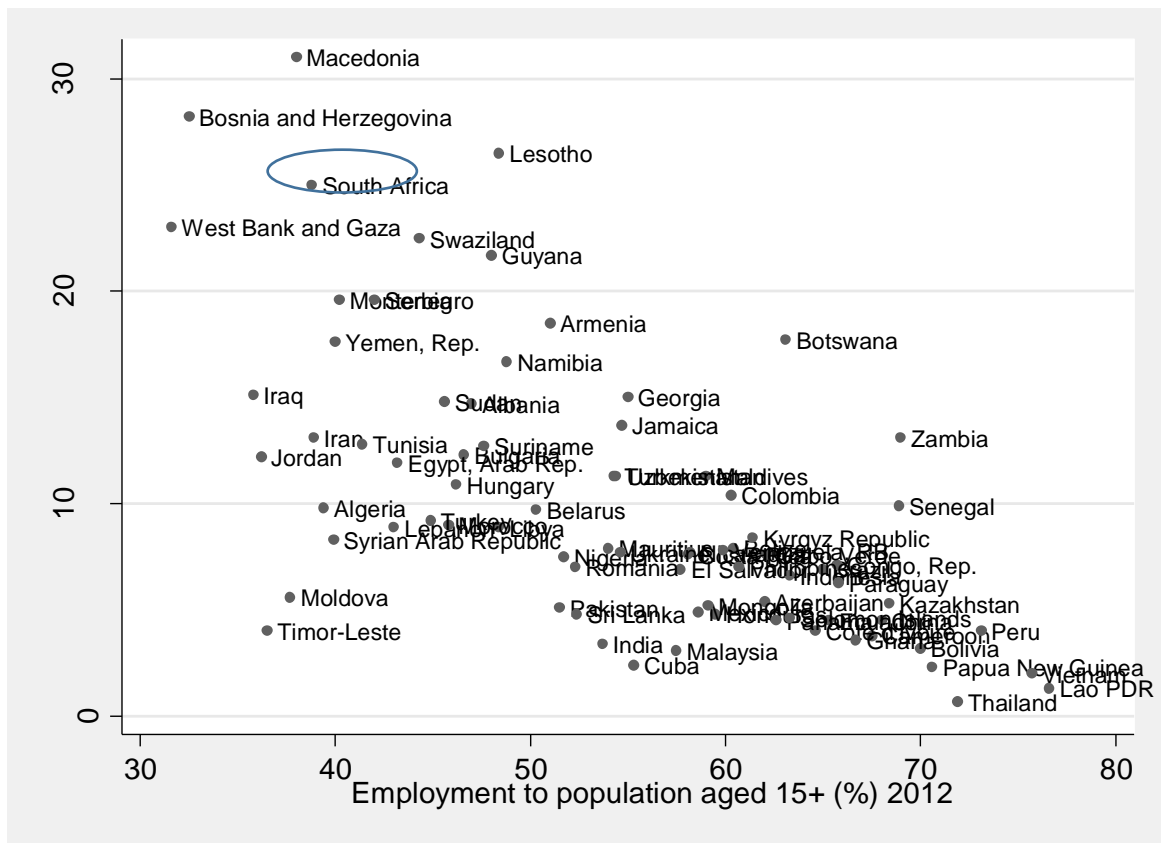
unemployment rates of about 25% and employment rates below 50%, placing them in a small group of otherwise war-torn countries that perform poorly on both measures. Economic growth is inhibited, and poverty persists. Boosting the employment rate is thus an urgent economic and social priority.



Source: World Development Indicators (data modelled by the International Labour Organisation. Available at: <http://data.worldbank.org/data-catalog/world-development-indicators>).

Figure 2: Unemployment Rates: South Africa in Comparative Perspective

All other things equal, employment rates are likely to be higher in countries with higher ratios of female to male labour force participation (as this increases the labour supply) and higher in countries with larger shares of agriculture in the GDP (because agriculture can absorb surplus labour especially where there is a large peasant sector). Employment rates are also likely to be higher when economic growth has been strong, but this effect will be muted if labour productivity (output/employment) rises at the same time. Table 1 explores these hypotheses using multivariate cross-country regression analysis. Model 1 accounts for 71% of global variation in 2012 employment rates. It finds that, controlling for the other variables in the model, an increase of one percentage point in annual real GDP growth between 2000 and 2012 was associated with a 4.1 percentage point higher employment rate. An increase in annual average labour productivity growth of 1 percentage point over the same period was associated with a 4 percentage point lower employment rate.



Source: World Development Indicators (Available at: <http://data.worldbank.org/data-catalog/world-development-indicators>).

Figure 3: Unemployment and employment rates for 79 middle income countries

The model predicts an employment rate of 56.5% for a country with South Africa’s characteristics. This is 18 percentage points higher than South Africa’s actual employment rate of 38% and is the largest regression residual in the sample. Model 2 includes a dummy variable for being a post-communist country (showing that such countries have a 3.6 percentage point lower employment rate) and in this model South Africa continues to have the highest residual, with a predicted employment rate 19% higher than actually achieved (Figure 4).

This suggests that there are important factors specific to South Africa at play. Its unique history is probably one of them. Like many other African countries with high land-to-labour ratios, industrialisation in South Africa was initially constrained by labour shortages (Karshenas, 2001). Colonial powers resorted to coercive measures such as forced labour to generate a labour supply, and in South Africa, apartheid policies destroyed the (‘black’) peasantry and created over-crowded reserves to supply migrant labour to the mines and farms (Feinstein, 2005). Such measures helped contain unskilled labour costs (although, in the early twentieth century, unskilled wages were no lower than in

much of Europe), but skilled labour shortages, exacerbated by racial discrimination, acted as a persistent constraint on growth (Seekings and Natrass, 2005). Despite the high ratio of skilled to unskilled wages, firms were encouraged to invest in capital-intensive processes by government subsidies and tax breaks as well as by racial restrictions on hiring. This resulted in inefficiently high rates of capital investment, falling capital productivity and falling profitability (Natrass, 2014c). By the time that open unemployment emerged in the 1970s as a large and persistent feature of the economic landscape, the South African economic growth path was unsuited for creating jobs for the millions of relatively unskilled people who wanted them (Seekings and Natrass, 2005).

Table 1: Exploring the determinants of employment rates in 2012

Explanatory variables (mean, minimum and maximum values for the sample, followed by the value for South Africa)	Model 1		Model 2	
	Unstandardized coefficient (standard error)	Beta	Unstandardized coefficient (standard error)	Beta
Female: male labour force participation rate (mean=0.72, min=0.21, max=1.04, SA=0.74)	0.44*** (0.03)	0.71	0.44*** (0.03)	0.71
Agricultural share of GDP (mean=10.8%, min=0%, max=49.6%, SA=2.5%)	0.17** (0.07)	0.16	0.16** (0.07)	0.15
Average annual real GDP growth 2000 to 2012 (mean=4.1%, min=-2.6%, max=12.5%, SA=3.5%)	4.1*** (0.47)	0.87	3.8*** (0.49)	0.81
Average annual labour productivity (real GDP per person employed) growth 2000 to 2012 (mean=2.4%, min=-2.6%, max=11.4%, SA=2%,)	-4.0*** (0.42)	- 0.89	-3.4*** (0.49)	- 0.76
Post-communist (mean=0.145, min=0, max=1, South Africa=0)			-3.6** (1.71)	- 0.14
Constant	17.64*** (2.81)			
Number of countries in the model (N)	111		111	
Adjusted R-squared	0.71		0.72	
Prob>F	0.000		000	

Note: *** p<0.01, ** p<0.05.

Source: World Development Indicators (Available at: <http://data.worldbank.org/data-catalog/world-development-indicators>).

Table 2 explores the global relationship between economic growth and employment during the 2000s. It shows that a one percentage point increase in economic growth was associated with a 0.29 percentage point increase in employment growth. If we include a control for being a post-communist country, then the employment elasticity of growth rises to 0.40. The models predict that given South Africa's average annual compound growth rate of 3.5% over the period 2000-2012, average annual employment growth should have

been 1.7% (model 1) or 2.2% (model 2) whereas its actual average rate of employment growth was only 1.5%. Under conditions of labour surplus in which you might expect that South African policy-makers would have encouraged the growth of employment at a rate *faster* than the typical international pattern so as to make fuller use of available labour and reduce poverty, the actual rate of employment growth was in fact *below* par by international standards.

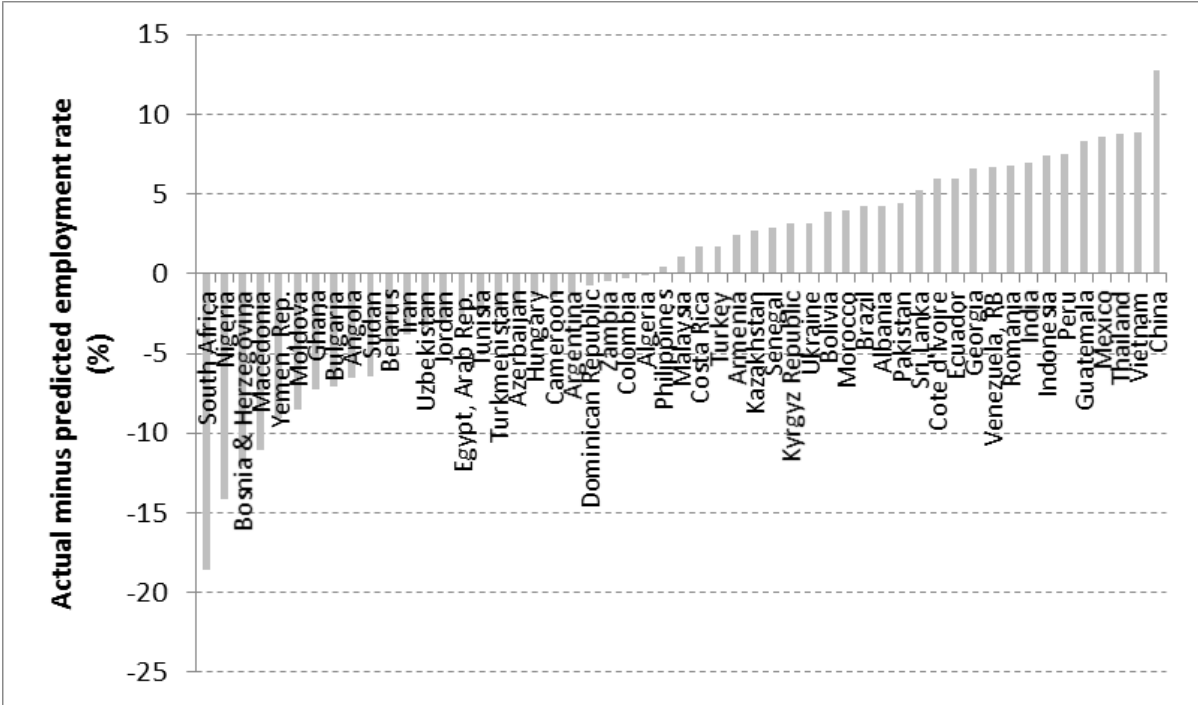


Figure 4: Regression residuals (model 2 in Table 1) for middle-income countries

Table 2: Regressing employment growth on output growth (2000 to 2012)

	Model 1	Model 2
Average annual compound growth in real GDP (2000 to 2012)	0.29**** (0.07)	0.40*** (0.06)
Post-communist countries		-2.51*** (0.33)
N	118	118
Adjusted R-squared	0.1321	0.4167
Prob>F	0.000	0.000

Note: Economic growth is the growth rate of real GDP; employment growth was estimated by subtracting the growth rate of GDP per person employed from the growth rate of GDP. *** p<0.01.

Source: World Development Indicators (Available at: <http://data.worldbank.org/data-catalog/world-development-indicators>).

Table 3: Employment elasticities and growth in upper middle-income countries

	Employment growth/output growth (2000-2012) <0.45	Employment growth/output growth (2000-2012) 0.45+
Unemployment rate (2000) <15%	Albania, Angola, Azerbaijan, Belarus, China, Dominican Rep, Hungary, Jordan, Kazakhstan, Peru, Romania, Thailand, Turkey, Turkmenistan, Venezuela,	Brazil, Costa Rica, Ecuador, Iran, Malaysia, Mexico
Unemployment rate (2000) 15%+	Bosnia and Herzegovina, Bulgaria, Iraq, South Africa	Argentina, Colombia, Macedonia, Tunisia

Note: Economic growth is the growth rate of real GDP; employment growth was estimated by subtracting the growth rate of GDP per person employed from the growth rate of GDP. *** p<0.01.

Source: World Development Indicators (Available at: <http://data.worldbank.org/data-catalog/world-development-indicators>).

In short, South Africa is not only an international outlier in terms of its high unemployment and low employment rates, but has also performed weakly in terms of generating jobs through economic growth. Table 3 situates South Africa and other upper middle-income countries in terms of combinations of employment elasticities of output (employment growth between 2000 and 2012 divided by real output growth over the same period) and unemployment rates. It shows that Bosnia and Herzegovina, Bulgaria, Iraq and South Africa share the dubious distinction of relatively high unemployment rates and relatively low employment elasticities. This means that in the absence of a fundamental change to the growth path, these countries are unlikely to grow their way out of their unemployment crisis any time soon.

South Africa and the Lewis Model

The post-apartheid government inherited an economy dominated by capital-intensive sectors and this has intensified over time. Table 4 shows that the most capital-intensive sectors (energy and mining, logistics and finance) grew collectively from 36% of value-added in 1990 to 42% in 2013 and their share of the capital stock rose from 38% to 55%. South Africa's capital-intensive character has been attributed to a specific cluster of activities dubbed the 'Minerals-Energy-Complex' or MEC (Rustomjee, 1992; Fine and Rustomjee, 1997; Fine, 2010). Following Rustomjee (1992), the MEC can be conceptualised as including the production of electricity and minerals and related manufacturing sectors such as chemicals, glass, plastics, basic iron and steel. Using 1988 input-output data, Rustomjee found that the MEC comprised about a quarter of value-

added and 63% of exports (1992: 327). Analysis of the 2011 input-output tables suggests that the MEC's contribution to value-added and exports has fallen since then, although it still remains an important generator of exports (Table 5).

Table 4: Changing Structure of Value-added and the Capital Stock: 1990-2013

	Ranking of capital intensity	Share of value-added in 1990	Share of value-added in 2013	Share of the real capital stock in 1990	Share of the real capital stock in 2013
Energy and Mining (electricity gas, water, mining and quarrying)	1	13%	8%	17%	19%
Logistics (transport, storage and communication)	2	7%	10%	16%	18%
Finance (finance, insurance, real estate and business services)	3	16%	24%	22%	21%
Community, social and personal services	4	25%	21%	22%	23%
Manufacturing	5	20%	17%	12%	11%
Other (Commerce, catering, accommodation and construction)	6	19%	20%	10%	8%

Source: South African Reserve Bank (Available at: <https://www.resbank.co.za/Research/Statistics/Pages/Statistics-Home.asp>)

Analyses of MEC-centred development usefully remind us of South Africa's origins as a minerals-dependent enclave economy and the role that this continues to play in supporting parts of the manufacturing industry and in generating export revenues. It also focuses attention on the legacy of South Africa's political-economic history in which powerful mining houses shaped the migrant labour system and diversified into manufacturing and finance, often behind protective tariff barriers and with the assistance of generous government subsidies (Feinstein, 2005). Yet whether it is a useful focus for understanding the core dynamics of capital accumulation in South Africa is a different matter (see also Bell and Farrell, 1996). Most obviously, other sectors have grown in importance, generating forward and backward linkages and growth dynamics beyond the MEC. One could, for example, just as easily identify a 'Logistics, Agriculture, Manufacturing and Energy' (LAME) cluster that is as integrated as the MEC and much larger (accounting for over quarter of value-added and gross profits, and about half of total employee remuneration). While it is true that LAME is a net user of foreign exchange and in this sense is dependent on export earnings from the MEC, it nevertheless represents a larger set of integrated economic activities and related political interests than the MEC and is also an important focus for government's industrial policies.

Table 5: The MEC and other clusters in the South African Economy, 2011

	MEC	LAME	FMEC	FLAME
% of outputs returned as inputs into the cluster	36%	36%	35%	38%
% of inputs coming from other firms in the cluster	59%	55%	65%	64%
contribution to total value-added	17%	26%	32%	44%
contribution to compensation of employees	15%	50%	39%	44%
contribution to gross operating profit	20%	27%	40%	51%
contribution to total exports	51%	37%	54%	40%
Contribution to total imports	35%	76%	35%	77%

Note: The MEC includes: coal and lignite, metal ores, other mining, coke oven manufacture, nuclear fuel, other chemicals, rubber, plastic, glass, non-metallic minerals, basic iron and steel, precious metals, structural metal and electricity gas and water. The LAME cluster includes: agriculture, forestry, fishing, food, beverages and tobacco, spinning and textiles, knitted fabrics, fur, leather and luggage, footwear, wood, paper, publishing, coke oven manufacture, nuclear fuel, other chemicals, rubber, plastic glass, furniture, general machinery, recycling, electrical machinery, electronic valves, medical appliances, motor vehicles, transport, telecommunications, renting of machinery, research and computer activities. The FMEC sector comprises the MEC and financial intermediation, insurance and pension, auxiliary financial and real estate activities. The FLAME sector comprises the LAME cluster and financial intermediation, insurance and pension, auxiliary financial and real estate activities.

Source: analysis of the 2011 input output tables (Available at: http://beta2.statssa.gov.za/?page_id=1854&PPN=Report-04-04-02&SCH=5769).

Recent neo-Marxist analyses have acknowledged the rapid growth of the financial sector (as shown in Table 4), but maintain that it remains strongly ‘linked’ to the MEC, and hence that the MEC remains the core feature of capital accumulation in South Africa (e.g. Ashman and Fine, 2013; Bond, 2013). But while there are historic connections between mining and finance, it is questionable whether this link is stronger with the MEC today than that between finance and other sectors of the economy. Table 5 shows that including finance in the MEC cluster (FMEC) increases the size and reach of the MEC, but that including finance in the LAME cluster (FLAME) has an even stronger impact.

What this suggests is that capital-intensity has risen in post-apartheid South Africa not because of the growth of the MEC cluster (with or without finance), but because there has been a general shift towards capital-intensity across *all* sectors, with faster growth in the historically capital-intensive sectors exacerbating the overall trend. South Africa’s labour-market and industrial policies which promote capital- and skill-intensive development, as well as significant support for capital-intensive mega projects (Black and Roberts, 2009) have contributed to this persistent bias against labour-intensive growth. It is only relatively recently that the DTI has started paying attention to more labour-intensive activities such as tourism, agriculture and small-scale enterprises (Black and Hasson, 2015 forthcoming).

In 1994, the African National Congress (ANC) won the first democratic election with an election manifesto, *The Reconstruction and Development Programme* (RDP), outlining an expansionary set of policies in which higher social spending would address poverty and fuel demand and hence growth (ANC, 1994). The RDP, which was written with the ANC's alliance partner, the Congress of South African Trade Unions (COSATU), also contained commitments about labour-market protection and achieving 'living wages'. It described collective bargaining over wages and working conditions as 'the basis for enhanced productivity in the economy' and endorsed the legal extension (by government gazette) of minimum wages set by unions and employer organisations in bargaining councils to 'all workplaces' in the country (ANC, 1994: par 4.2.10-1, pages 81-2, par. 4.8.8, p.114). The ILO's concern for living wages was clearly evident, but this was not seen as presenting any threat to job creation. No trade-off between wages and employment was envisaged, the assumption being that higher wages would compensate business by boosting demand whilst encouraging them to be more productive (Nattrass, 1994).

Unfortunately, once the ANC assumed power it became evident that the government was facing a debt crisis and that the prospects for demand-led growth were severely constrained (Nattrass, 2014a). In 1996 the government released a new economic vision, the 'Growth, Employment and Redistribution' policy framework subsequently referred to as GEAR, arguing that restrictive fiscal policy was required to stabilise government finances and the macroeconomy (DOF, 1996). More controversially, it proposed a set of labour-market reforms, notably that 'industrial agreements which reach across diverse firms, sectors or regions should be sufficiently flexible to avoid job losses and should be extended to non-parties only when this can reasonably be assured' (DOF, 1996: 19). The Presidential Labour Market Commission (LMC), reporting later that same year, came to a similar conclusion, recommending that the Minister of Labour exercise discretion before extending collective agreements to all firms so as to prevent job losses in the smaller, more labour-intensive firms that tend not to be adequately represented in bargaining councils (LMC, 1996). Predictably, COSATU objected to GEAR's macroeconomic policies and to the proposed labour-market reforms but was successful only in blocking the latter. The result was persistent wage pressure in the face of constrained demand and increasing competition: a toxic combination for job creation (Nattrass, 2014b).

Job creation has been, at least rhetorically, a key policy priority for the post-apartheid government. Yet the ANC has struggled to produce a coherent economic vision for achieving this and the three most recent development plans contain conflicting economic policies (Kaplan, 2013). What they share, however, is an underlying microeconomic assumption that international

competitiveness and industrial development has to be *driven* by labour productivity growth. This is testimony to the power of organised labour to maintain pressure on wages, to block labour-market reforms and to influence industrial policy. Put differently, with rising wages as a given, economic competitiveness in an open economy simply has to be based on rising labour productivity. South Africa's industrial policy accordingly concentrates on boosting productivity, helping firms upgrade (usually by mechanisation) and assisting capital-intensive sectors where labour-productivity and value-added is high (DTI, 2011; Lewis, 2001; Hirsch, 2005; Kaplan 2007; Zalk, 2014).

Productivity growth is important for sustainable economic development because it allows more output to be produced with fewer inputs, thereby raising living standards over the long term. But the extent to which labour productivity (output/employment) or capital productivity (output/capital stock) should be prioritised is an open question. In a developing country like South Africa where there is a large surplus of unemployed relatively unskilled labour and where finance for investment is relatively constrained, there is a strong economic case for a more labour-intensive growth path.

The relationship between industrialisation and job creation in labour-surplus countries was theorised by Lewis in the 1950s. The 'Lewis model' describes a trajectory in which relatively low-cost labour is drawn out of subsistence agriculture and into manufacturing, fuelling a process of labour-intensive industrialisation until wages rise as surplus labour is absorbed (Lewis, 1954; Fields, 2004). It has been criticized for focusing only on unskilled labour and neglecting the role of existing proto-industrialists (small weavers and the like) in Asian development (Sugihara, 2013: 27; Saito, 2016: 86). But it remains a useful heuristic for describing the potential for low-wage labour-intensive development to absorb unskilled labour, even if this is only one aspect of a broader development path. The Taiwanese experience of rapid employment growth at stable wages in the 1950s, followed by wage increases and a shift into higher productivity sectors in subsequent decades as the labour-market tightened, was a good example of Lewis-like growth subsequently transforming into a higher-wage, higher productivity growth dynamic after surplus labour has been absorbed (Fields, 2004: 730). Indeed, the pattern of moving into higher value-added economic activities (where wages and labour productivity are typically higher) *after* surplus labour-supplies have largely been exhausted is a stylised fact of Asian development (Chamon and Kremer, 2009: 20; Lin and Rosenblatt, 2012; Lin, 2012) and is evident most recently in China, where the labour market has tightened since the mid-2000s (Zhang *et al.*, 2011).

An example closer to South Africa is Mauritius, where the development of a local labour-intensive clothing industry spear-headed by entrepreneurs from

Hong Kong helped catapult the country from high unemployment in the early 1970s to such intense labour shortages by the end of the 1980s that workers had to be imported from China and elsewhere to fill the low-wage jobs Mauritians were no longer prepared to consider (see e.g. Subramanian, 2001; Bräutigam, 2003, 2009). As wages rose, the garment industry steadily declined and the Mauritian economy shifted more towards information technology and tourism. Some Chinese Mauritians moved their clothing factories out of the country, including to Lesotho in order to benefit from low-wage labour and access to the South African market. But whereas Lesotho is currently attempting a Lewis-like growth trajectory, post-apartheid South African policy, in effect, is seeking to maintain the economy's relatively high-wage, high-productivity character without mopping up unemployment through a prior or simultaneous process of labour-intensive growth.

This is partly a product of history in that Lewis-like labour-intensive development is strongly associated with labour coercion and racial oppression, particularly in the mining industry (Wilson, 1972; Feinstein, 2005). When large supplies of 'surplus' labour were revealed as open unemployment in the 1970s, the apartheid state responded by incentivising labour-intensive industry to set up in or near the impoverished reserves for the 'black' population. Some rural towns, like Newcastle in the Natal midlands, echoed the Mauritian approach by actively courting Taiwanese entrepreneurs to set up clothing enterprises there (Natrass and Seekings, 2014). Wages were much lower in such labour-intensive industries as they were either exempt from minimum wage setting altogether, or were part of regional wage-setting arrangements. For organised labour, they were a threat to 'decent work' in the towns and an engine for perpetuating racial wage inequality. The remaining incentives for decentralised industrial development were removed in the 1990s and the wage-setting machinery was expanded to cover the whole of South Africa and to encourage national, rather than regional wage agreements.

Globalisation and the rejection of Lewis-like growth in South Africa

Post-apartheid policy-makers faced a choice: to maintain and grow capacity in existing competitive industries whilst reigniting labour-intensive development to address unemployment directly; or concentrate only on improving productivity in the high-wage, high productivity sectors in the hope that this would be a strong enough source of competitiveness that it would address unemployment indirectly through rapid and sustained growth. This choice has never been resolved entirely, but in practice, given the absence of any significant reforms to

the wage-setting machinery and industrial policy, South Africa has opted for the latter. This was partly due to the apartheid baggage associated with labour-intensive development. But it was rooted also in an emerging development ideology, subsequently to become hegemonic, asserting that labour-intensive development in today's globalised world is a 'low-road' to growth promising little more than a 'race to the bottom' because of competition from low-wage countries.

The business economist Michael Porter argued influentially in the late 1980s and early 1990s that comparative advantage (based on the relative abundance of labour and capital) was no longer sufficient to guide policy and that national competitive advantage depends *inter alia* on active state involvement to support innovation, competition and strategic clustering of firms as well as to encourage structural change in favour of higher value-added activities (Porter, 1990). But, whereas Porter recommended that governments should avoid intervening in markets to lower labour costs as this was usually counter-productive and not conducive to encouraging upgrading (1990: 88), in South Africa his warning transmogrified into a stronger and more radical claim that rising wages are desirable as they would prompt firms to improve productivity and hence facilitate more dynamic growth. This notion appeared first in the RDP but was spelled out more systematically a year later by the COSATU-aligned Industrial Strategy Project (ISP). In a book that has influenced industrial policy for almost a decade, the ISP argued that South Africa should actively avoid any 'restructuring towards low-wage, low-productivity forms of production' (Joffe *et al.*, 1995: 213) and that labour and industrial policy should be 'premised on the need to move South African firms out of their low-wage, low-skill, low-productivity vicious circle in which they are out-competed by the second-tier newly industrialising countries' (1995: 214; Natrass, 2001).

In 2009 Ebrahim Patel was appointed to the newly created Ministry of Economic Development tasked with coordinating and planning the Government's economic policies (in effect taking these functions from the Treasury). Patel had been General Secretary of the South African Clothing and Textile Workers Union (SACTWU) from 1999 to 2009, national labour convener in the peak level National Economic, Development and Labour Council (Nedlac) and chief negotiator in the formation of the National Bargaining Council for the Clothing Industry, the Labour Relations Act and related legislation as well as in various government-sponsored employment summits. From the 1990s he was a strong advocate of using government resources and policies to promote high-wage, high value-added forms of production. As Minister of Economic Development, he incorporated this into a New Growth Path (NGP) strategy for the economy as a whole (Natrass, 2011).

The NGP proposed a ‘developmental state’ to support new productive activities, especially in light manufacturing, the mining and agricultural supply chains and in a range of knowledge- and skill-intensive activities (e.g. biotechnology) and in green technology (notably solar power). Resources were to come from progressive taxation and by boosting and ‘mobilising’ domestic savings, presumably by requiring pension funds to purchase ‘development bonds’ (2010: 27). Although the term ‘developmental state’ is evocative of the East Asian interventionist state, the NGP (2010) had a radically different approach to labour. Whereas wages and working conditions improved in East Asia only once the labour-market tightened after decades of strong growth, the NGP – like the ISP before it – proposed to advance the South African trade union agenda as an integral part of the growth strategy. Making this a labour-absorbing growth path was seen as the job of industrial policy (to identify and support economic activities which have the potential to create large numbers of well-paid formal jobs in which workers have contracts, access to benefits, training and a career path).

This task fell on the shoulders of Rob Davies, Minister of Trade and Industry since 2009 (and Deputy Minister 2005-2009) and long standing member of the South African Communist Party. Department of Trade and Industry (DTI) documents support the NGP vision and are replete with Porter-like discourse about the need for government to create and support ‘world class manufacturing’ – as if there is only one ‘best practice’ way of producing in an industry, and that ‘sustainable’ production inevitably requires a movement ‘up the value-chain’. For example, the economic rationale for the DTI’s support program for clothing (which primarily supports capital intensification and skills development) – is that ‘the sector lags behind its international competitors in terms of conversion efficiencies and other key indicators of world-class manufacturing principles, of which quality cost and delivery are the main drivers’ (DTI, 2011: 144). It talks about ‘competitiveness challenges’ but does not mention wages (2011: 142), which accordingly, appear to be off the agenda. Its stance is primarily one of supporting more long-term partnerships between producers and retailers (through the formation of ‘clusters’), upgrading machinery, reducing costs through lean production, subsidising training programs and otherwise assisting firms to cope with wage pressure by improving labour productivity.

South Africa’s latest development strategy, the 2012 National Development Plan (NDP), reinforces this anti labour-intensive stance by characterising the country as being caught in a ‘middle-income trap’ with no real prospects of competing internationally in labour-intensive activities and hence facing no real alternative other than to compete in niche markets and move into higher value added

activities (NPC, 2012: 115). Indeed, the NDP appears to have given up on labour-intensive manufacturing altogether, declaring:

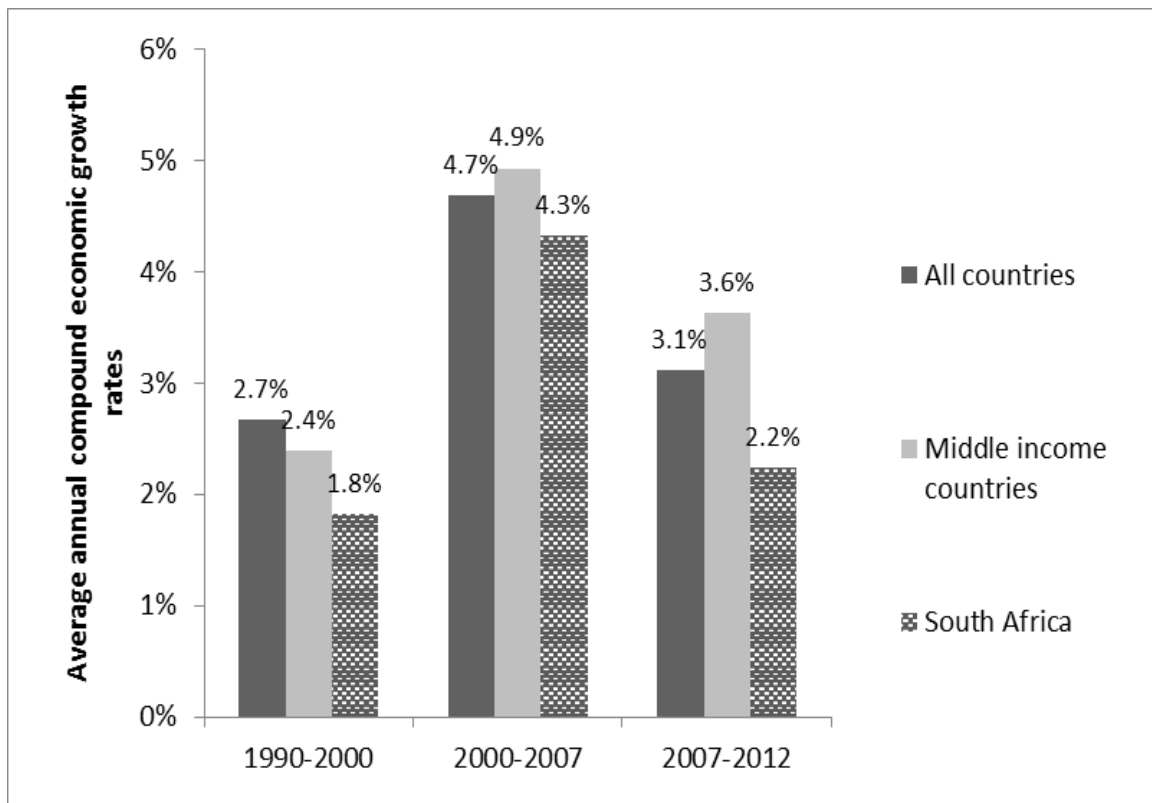
‘South Africa’s manufacturing strength lies in capital-intensive industries. In the context of high unemployment, growth would ideally be sourced through expanded contribution of labour. However, to compete, the country’s cost structure requires an emphasis on productivity, products and logistics’ (NPC, 2012: 147–148).

In other words, because wages and other costs are already high, tradable sectors are not seen as a source of significant direct job creation. This is left to small-holder agriculture and domestically-oriented small- and medium-firms (NPC, 2012: 115). Some regulatory reforms are proposed to assist such firms including entry-level wage flexibility and simplifying dismissals procedures (NPC, 2012: 131-2; 134-5, 143). This, coupled with projected growth of 5.4% per annum until 2030, is assumed sufficient to boost the employment rate by 20 percentage points.²

This, however, is over-optimistic. Annual growth of 5.4% is 25% faster than during the global economic boom of the 2000s and over twice that achieved since the 2007/8 global crisis (see Figure 5). It is also faster than average middle-income country growth between 2000 and 2007 – something South Africa has never achieved. According to recent projections by the International Monetary Fund (IMF, 2014), South Africa is likely to grow at only 1.7% in 2014 and 2.7% in 2015 and the South African Reserve Bank now calculates South Africa’s potential economic growth as no more than 2.5% (Anvari *et al.*, 2014). Furthermore, even in the unlikely event that economic growth of 5.4% could be achieved, the international model in Table 1 suggests that for a country with South Africa’s characteristics, boosting the employment rate by 20 percentage points would require an even higher growth rate or sharply falling labour productivity³ – i.e. a substantially more labour-intensive growth path.

² Calculated from data in NPC (2012: 118).

³ The NDP did not publish its underlying economic model. According to the international trends summarised by the cross-country regression in Table 1, for a country with South Africa’s characteristics, a 20 percentage point increase in the employment rate would have required either annual growth of 8.4%, or annual growth of 5.4% accompanied by a 3% annual decline in labour productivity.



Source: *World Development Indicators* (Available at: <http://data.worldbank.org/data-catalog/world-development-indicators>).

Figure 5: South Africa's GDP growth rates in comparative perspective

Are there labour-intensive options for South Africa in today's globalised world? In the 70 years since Lewis formulated his model, production has become increasingly fragmented in global value chains (GVCs) as communications technology and falling transport costs enable countries to specialise in tasks rather than products or entire industries (OECD, 2013; Cattaneo *et al.*, 2013; Baldwin, 2014). Over half of global manufactured imports are intermediate goods (primary goods, parts and components and semi-finished products) and more than half of the value of exports is made up of products traded through GVCs (Backer and Miroudot, 2013). As Gawande *et al.* put it, 'the iPhone's supply chain, which traverses more than ten countries for eventual assembly in China is the new "new"' (2014: 3). Even simple products, like the t-shirt, are caught up in GVCs, with cotton grown in the US, exported to China for the manufacturing of clothing and then shipped back to the US for imprinting with logos and marketing, and then shipped to Tanzania (as used garments) for resale or to be used as furniture padding (OECD, 2013: 10).

Table 6: Indicators of domestic and global inter-connectedness for manufacturing, mining and agriculture in the major emerging markets (2009)

	Brazil	China	India	Mexico	Turkey	South Africa
Exports as % GDP	11.0%	26.7%	20.1%	27.3%	23.3%	27.3%
Average applied tariff	13.3	8.0	9.3	4.8	2.9	7.4
Intra-industry trade*	0.104	0.197	0.181	0.079	0.132	0.085
% intermediates use **	0.638	0.771	0.604	0.777	0.757	0.684
Vertical specialisation***	0.166	0.266	0.257	0.266	0.291	0.192
Forward participation in GVCs ****	27.2	13.4	20.3	11.5	15.9	17.3
Backward participation in GVCs *****	9.0	32.6	21.9	30.3	28.5	16.5
Global value chain participation *****	36.2	46.1	42.3	41.8	37.7	33.8

Note: *|imports-exports|/(imports+exports) HS 6 digits; ** Fraction of output used as intermediates inputs by all other sectors; *** Percentage of output used as intermediates by exporters in the same country; ****forward participation (domestically produced inputs used in third country exports) as a share of exports; ***** backward participation (import content of exports); *****Share of exported inputs in exports plus share of foreign value added in exports. This is the sum of forward and backward participation in GVCs.

Source: Gawande *et al.*, 2014: 3, 12; Koopman *et al.*, 2010: 35-36; OECD global value chains indicators May 2013 (Available at: http://stats.oecd.org/Index.aspx?DataSetCode=TIVA_OECD_WTO#); World Development Indicators (Available at: <http://databank.worldbank.org/data/views/variableSelection/selectvariables.aspx?source=world-development-indicators>).

Table 6 provides indicators of domestic and global inter-connectedness for South Africa and other major emerging markets. It shows that South Africa's economic structure is fairly typical in that over two thirds of output is used as inputs into other products and that about a fifth of its output is absorbed as inputs by exporters. Its forward participation in GVCs (selling inputs to export producers in other countries) is relatively high reflecting the important role of commodity exports. Backward participation (buying foreign components for use in export production) is relatively low.

Participation in GVCs can benefit developing countries by allowing them to embark on a Lewis-like trajectory on the basis of tasks rather than entire industries. According to Hausmann, this development can be likened to changing the rules in the game of Scrabble: initially only those countries with the most 'letters' (technologies, capabilities, infrastructure, and domestic supply chains) could form the most 'words' (products), whereas contemporary globalisation has:

‘split up value chains, allowing trade to move from words to syllables. Now, countries can get into business with fewer letters and add letters more parsimoniously.... Countries that started in garments – for example, South Korea, Mexico, and China – ended up reusing the accumulated letters (industrial and logistical capabilities) while adding others to move into the production of electronics, cars, and medical equipment’ (2014, npn).

However, there are also risks involved in pursuing Lewis-like labour-intensive development through GVCs. As UNCTAD warns:

‘participation in international production networks runs the risk of generating adverse terms-of-trade effects on countries, particularly those at the lower ends of production chains, and it creates few domestic linkages and technology spillovers. Moreover, developing countries at an early stage of industrialisation may become locked into low-value-added activities due to stiff competition from other suppliers to keep labour costs low, and because the tight control over intellectual property and expensive branding strategies of the lead firm block them from moving up the value chain. Even relatively successful middle-income countries do not face a level playing field in many of these networks’ (UNCTAD, 2014: x; 104-105; OECD, 2013: 14).

This concern resonates with South African policy makers and within a sub-set of the GVC literature arguing that countries should avoid the bottom (labour-intensive, low-value added) end of GVCs and direct industrial policy towards moving firms into higher-value added segments (Fernandez-Stark *et al.*, 2011; Gereffi, 2013; Gereffi and Fernandez-Stark, 2011). Countries are accordingly advised to help firms position themselves more favourably within GVCs by *inter alia* moving into more sophisticated product lines (product upgrading), using superior technologies (process upgrading) and increasing the skills content of operations (functional upgrading) (Kaplinsky *et al.*, 2003; Gereffi and Fernandez-Stark, 2011; Gereffi, 2013: 18-19; Cattaneo *et al.*, 2013). In this perspective, ‘upgrading is imperative, not only to capture increasing value within these global industries, but ultimately to survive within the industry’ (Psilos and Gereffi, 2011: 3). South Africa’s industrial policy stance towards the clothing industry is in precisely this vein: substantial resources have been channeled to the larger, mostly capital-intensive firms to upgrade their machinery and move into higher value-added segments (Nattrass and Seekings, 2014).

The ‘upgrade or die’ approach, however, rests on an overly static notion of competitiveness and assumes that there is a one-to-one correlation between higher value-added and profitability. For example, value-added in the garment GVC is assumed to be captured by large retailers and branded marketers who design and sell clothing, sometimes engaging in full-package production of the more sophisticated garments but mostly outsourcing mass production to low-wage countries (Gereffi, 1994; OECD, 2013: 13). Yet as Tokatli (2013) has shown, even highly successful international apparel producers with design, manufacturing and retail capacity sometimes ‘downgrade’ by moving in and out of sub-contracted manufacturing for other firms if profitable opportunities arise. There is thus no necessary link between targeting higher value-added activities and economic dynamism; profitability matters and this is not always coincident with higher-value added production.

Producing in the lower-value added segments can generate significant income for labour and capital, especially where there are scale advantages – as the Chinese assembly industry illustrates – thereby creating a strong developmental dynamic. As Kowalski (for the Working Party of the OECD Trade Committee) observes:

‘Recently, and perhaps mistakenly, the concept of upgrading has been seen as the need to capture a growing share of domestic value added in exports or to targeting specific “sophisticated” products or production stages. This however misses the point that the *volume of the activity may matter as much as domestic content or sophistication*; important benefits can be derived from specializing in less sophisticated assembly activities and performing them on a large scale. Our empirical results show indeed that engaging more widely in GVCs, whether by using more foreign value added embodied in imported intermediates or importing more sophisticated intermediates, does appear to correlate with positive outcomes, such as productivity, sophistication and diversification of exports, even if there is a large heterogeneity across income groups’ (emphasis in the original) (2014: 7).

In other words, a diversified economic strategy which promotes a ‘wide’ participation in GVCs can diversify exports and promote productivity growth in key areas whilst also accommodating more labour-intensive, lower-value added production. Industrial policy should prepare for and accommodate structural change, even taking a leaf out of the East Asian playbook by generating new industrial capacity prior to the exhaustion of cheap labour supplies from agriculture (Porter, 1990; Wade, 1990; Chang, 2002). But it could do this whilst simultaneously sustaining and generating new job creation in labour-intensive

activities. There is no reason why countries have to choose one path or another: the global environment is flexible enough to accommodate a range of competitive strategies – but only if domestic labour-market policy is sufficiently accommodating. South Africa's is not.

Wage-setting and the destruction of labour-intensive jobs in South Africa

South Africa's wage-setting machinery was introduced in the 1920s for 'white' workers and extended to 'black' workers after 1979. Devised at a time of import-substituting industrialisation, it rested on the assumption that product and process differentiation was limited. Both the institutions themselves and the minimum wages then set were shaped by the British experience, itself rooted in Britain's high wages. In this context, setting minimum wages across the industry protected firms from unfair competition in the same product market and tariffs protected them from foreign imports. After the transition to democracy in 1994, the Labour Relations Act was rewritten not only to cover all South African workers but also to consolidate industrial-level bargaining and to require the Minister of Labour to extend collective agreements to all firms (whether unionised or represented in bargaining councils or not) where bargaining councils were deemed to be sufficiently representative. The ICTWSS database on Institutional Characteristics of Trade Unions, W-setting, State Intervention and Social Pacts⁴ accordingly upgraded South Africa's score for 'mandatory extensions of collective agreements by public law to non-organised firms' from 1 (exceptional, applying to less than 10 percent of the labour force) to 2 (used regularly, and affecting more than 10 percent of workers) when South Africa transitioned to democracy (see also Visser, 2011: 8). In this database of 49 countries, only one country besides South Africa (Switzerland) increased the scope of extensions in the 1990s whereas three countries reduced the scope of extensions: Australia from 3 (extensions virtually automatic and general) to 2 in 1992; New Zealand from 3 to 0 in 1992; and Slovakia from 2 to 1 in 2004. South Africa's expanded use of extensions thus went against global trends, institutionally and economically. This is problematic for employment because in today's globalised world, there is a greater degree of product and process differentiation and competition from foreign imports is much more intensive. Extending wages across the industry has a potentially far greater impact on employment today because sometimes firms in non-competing product markets are driven out of business and, whether or not they are in the same product

⁴ ICTWSS data base version 4 available at: <http://www.uva-aias.net/208>

market, their place is quickly filled with foreign imports.

Consider the case of the clothing industry where since 2003, minimum wages have been set in the National Bargaining Council for the Clothing Manufacturing Industry (NBC) through collective agreements between SACTWU and various regionally-based employer organisations. As SACTWU has 50 percent of the votes (it is the only union) on the NBC, it needs the agreement of only a single employer association to obtain a ‘collective agreement’ in the NBC. Agreements are dominated by metro-based employers who can pay higher wages, in part because they produce for niche markets (such as government or top-end consumers) and in part because their production is more capital- (and skill-) intensive. Since 2003 the NBC’s collective agreements have routinely been extended by the Minister of Labour to all firms, whether represented in the NBC or not. Minimum wages for labour-intensive firms outside of urban areas (including in the old apartheid-era industrial decentralisation zones) tripled in dollar terms between 2002 and 2010. Many firms shut down whereas others continued to operate at wages below the minimum until pursued through the courts by the NBC and shut down by the local sheriff (Nattrass and Seekings, 2014).

Falling effective rates of protection in the clothing industry between 1994 and 2004 certainly increased competitive pressures on the clothing industry (Edwards, 2005: 768) but it was the combination of increased international competition from China and the advent of national wage setting from 2003 that drove job losses: between 2003 and 2013 the clothing industry shrunk by 50%, especially in labour-intensive firms in relatively poor non-metro areas (Nattrass and Seekings, 2012a; 2014). The result has been rising average labour productivity (as average capital-intensity increased) but at the cost of the destruction of the ultra-labour-intensive segments of South Africa’s last remaining labour-intensive manufacturing industry.

The destruction of jobs in the South African clothing industry is a dramatic illustration of how labour-market and industrial policy can shape the dynamic of capital accumulation. Elsewhere the impact is more subtle as wage pressure simply encourages firms to become more capital-intensive, to shift out of labour-intensive sectors or avoid entering labour-intensive sectors in the first place. It is thus difficult to estimate the impact of wage-setting machinery on the economy because we do not have data on how the economy would have developed in its absence (see discussion in Nattrass and Seekings, 2012b). Borat *et al* (2009) find that the wage premium for workers covered by bargaining councils is higher at the bottom end of the wage distribution, providing suggestive evidence that bargaining council agreements discourage low-wage labour-intensive production. Rather than South Africa not being able

to compete with countries like China, the experience of job destruction in the South African clothing industry reveals that labour-intensive producers *were* competing successfully (albeit by failing to pay legislated minimum wages) until they were driven out of business by the bargaining council.

The history of South Africa's clothing industry also demonstrates the falsity of the assumption that without industry-wide minimum wages, there will be a 'race to the bottom'. It is simply not the case that low-wage, labour-intensive firms necessarily drive higher-wage, higher productivity firms producing more sophisticated products out of business. Relatively high-wage clothing firms in urban areas co-existed with low-wage clothing firms in non-metro areas in South Africa (including in the highly subsidised industrial development zones) for over a century because they use different technologies and compete in different product markets - formal attire and pajamas, for example (Nattrass and Seekings, 2012a). If there was going to be a race to the bottom it would have happened already. Rather, there is room for a range of job opportunities at different combinations of wages and productivity, if the minimum-wage setting machinery allowed it.

The extension of collective agreements to non-parties has also been the subject of contestation in the Metal and Engineering Industry Bargaining Council where smaller firms complain about unaffordable wage increases negotiated between large employers and the dominant trade union.⁵ Lower-wage, labour-intensive firms in South Africa are driven out of business not by being caught in some existential middle income trap, but by a wage setting system that allows higher-end, unionised firms to set wages too high for labour-intensive businesses producing at the lower end of the market. The problem is not collective bargaining *per se*, but rather the extension of these agreements across the entire country by a Minister of Labour not charged with having to consider any adverse effects on employment.

The wage-setting machinery in post-Apartheid South Africa strengthened the power of organised labour and (big) business and in the process weakened the power of government by removing any discretion to take other factors (including employment effects) into account before converting collective agreements into legally binding minimum wages. Most countries set minimum wages, but through different processes and with more or less power in the hands of government. The ICTWSS data set includes a scale of government power to set national minimum wages that runs from 1 (set entirely by collective

⁵ Details are available at: <http://www.neasa.co.za/Home.aspx> and: <http://www.meibc.co.za/>.

agreements with no government discretion) to 8 (government set minimum wages with no fixed rules). South Africa's classification is a 3 on this scale (national minimum wages as set mostly through collective agreements which are extended by government). The dataset has scores for 46 countries and no other middle-income country has a score for government power/discretion as low as South Africa's (or an unemployment rate as high). Table 7 reports the results of a simple regression of the 2012 unemployment rate for these 46 countries on (log) per capita GDP, share of agriculture in value-added and a dummy variable taking a value of 1 if government or an expert panel set national minimum wages, and a value of 0 if unions and employers are involved. The regression shows that controlling for the capacity of the agricultural sector to absorb surplus labour and for the level of development, having national minimum wages set by government (as opposed to business and labour) reduces the unemployment rate by 3 percentage points. This suggests that the institutional space for government to ensure that national minimum wages are set after taking into account a broader range of interests than those represented in collective bargaining institutions, matters for reducing unemployment.

Table 7: Determinants of unemployment rates in 2012

Explanatory variables (mean, minimum and maximum values for the sample, followed by the value for South Africa)	Unstandardized coefficient (standard error)	Beta
Log of real GDP per capita in 2012, in 2001 dollars (mean=10.19, min=8.53, max=11.37, South Africa=9.40)	-7.271*** (2.215)	- 0.78
Agricultural share of GDP (mean=3.8%, min=0.3%, max=17.5%, South Africa=2.5%)	-1.055*** (0.343)	-0.73
National minimum wages mostly set by government or an expert panel with no participation by unions or employers (mean=0.63, min=0. max=1, South Africa=0)	-3.21** (1.478)	- 0.30
Constant	89.173*** (23.827)	
Number of countries in the model (N)	46	
Adjusted R-squared	0.206	
Prob>F	0.005	

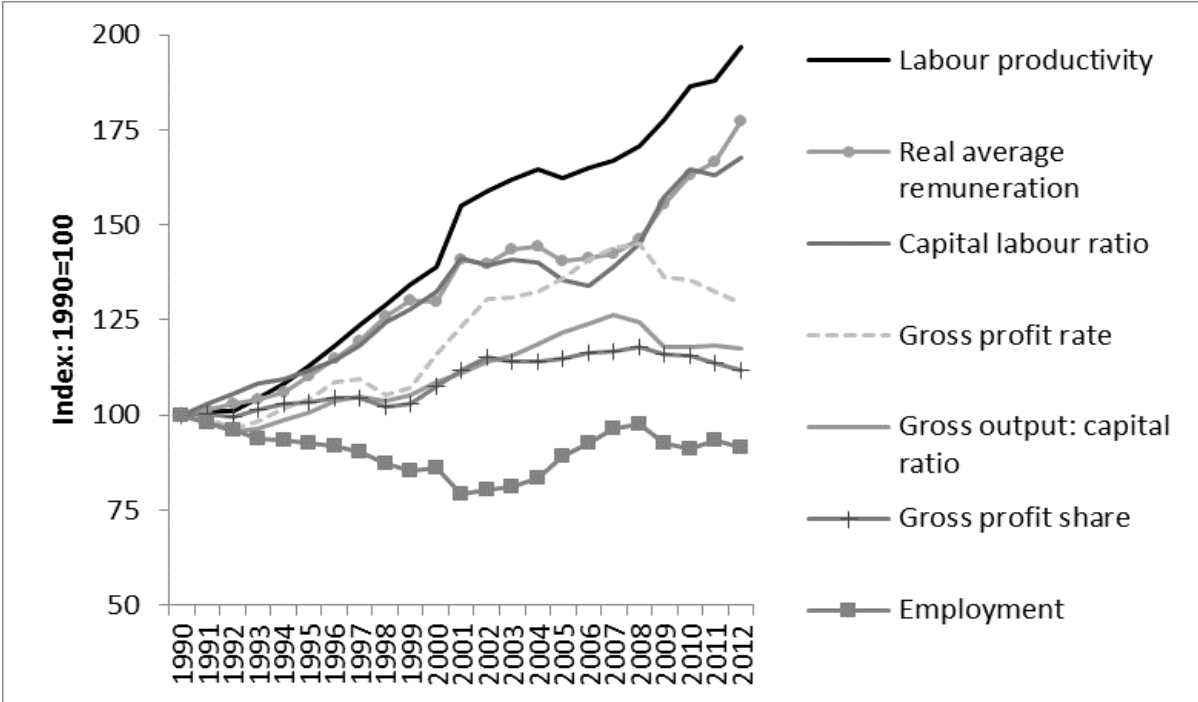
Note: *** p<0.01, ** p<0.05.

Source: World Development Indicators (Available at: <http://data.worldbank.org/data-catalog/world-development-indicators>).

The political-economy of growth and policy reform

The post-apartheid growth path has generated winners and losers. As shown in Figure 6, real average remuneration has been on an upward trend alongside

rising capital-labour ratios (capital-intensity). But because average labour productivity grew faster than real wages, the overall share of income going to labour fell, and the profit share rose. Capital productivity also rose as the economy became more skill- and capital-intensive, contributing further to rising profit rates. In short, firms that were able to improve their labour and capital productivity or expand into relatively high-wage, high-productivity sectors, were the beneficiaries of the growth path. Labour-intensive firms who were pushed out of business by rising wage costs and increased international competition were the losers. Rising average remuneration indicates that labour as a whole also benefited. Note, however, that the benefits were unevenly spread, with incomes rising faster at the upper end and with some compression at the bottom (Wittenberg, 2014).



Source: South African Reserve Bank, Statistics South Africa (Quarterly Labour Force Survey) and the Post-Apartheid Labour Market Series (PALMS) from Data First, University of Cape Town.

Figure 6: Productivity, profitability and average remuneration in South Africa

The NDP calls for a ‘social contract that will enable South Africa to achieve higher growth and employment’ (NPC, 2012: 475). It is vague on details, but calls for workers (except the very low paid) to agree to accept wage increases lower than their productivity gains would dictate, and for business to reinvest profits in job-creating ways and not to fuel the growth in executive remuneration. In other words, the NDP is actually calling for a rising profit

share. This is presumably to finance investment given that corporate saving out of profits has been the only domestic source of financing gross capital formation since the global economic crisis (Nattrass, 2014a). The NDP proposes to compensate workers by lowering the cost of living (notably by keeping inflation and import tariffs low) and continuing to support skill development and productivity growth in higher-value added activities where there is more space for wage growth (NPC, 2012: 475-6). Organised labour, however, remains suspicious of anti-inflationary policies and any call for wage restraint, seeing this as an affront to the agenda of getting rid of the apartheid wage gap (COSATU, 2010; 2012). The prospects for the envisaged social contract are thus poor.

COSATU's 'high-wage, high productivity' strategy in support of 'decent work' is in effect at the centre of the government's growth strategy. But there are signs that it is not necessarily a hegemonic position. For example, the then Minister of Finance, Pravin Gordhan, suggested in 2011 that changes to South Africa's labour dispensation may be necessary to prevent further job losses in the clothing sector – a view subsequently endorsed by Trevor Manuel, a previous minister of Finance and currently the head of South Africa's Planning Commission.⁶ Yet this has not resulted in any serious proposals to reform the extension of collective agreements across industries.

Trade-union aligned intellectuals have justified continued wage pressure by pointing to the so-called 'Lula moment' in Brazil (Coleman, 2012) when President Ignacio Lula da Silva increased minimum wages and social security payments in the mid-2000s. This contributed to economic growth and poverty alleviation (ILO, 2011; Serrano and Suma, 2011). However, Brazil was further down the Lewis trajectory than South Africa when this policy was introduced. It had already redistributed its surplus labour from agriculture into urban work – informal and formal – in the second half of the twentieth century and by the mid-2000s the labour market had tightened. Unemployment rates were a third of that of South Africa and wealthy residents in Rio and elsewhere complained about the difficulties finding domestic workers. The combination of global boom, a tight labour market and strong domestic savings provided the ideal opportunity – or moment – to raise minimum wages and social security payments. South Africa is not in such an enviable position. With consumption already accounting for over four fifths of GDP and given persistent balance of payments problems (Nattrass, 2014a), the prospects for demand-led growth remain limited.

⁶ A newspaper report on this is available at: <http://mg.co.za/article/2011-08-25-cabinet-no-pravin-we-wont-relax-sas-labour-laws>.

According to the 2008 ‘Spence Commission’ on growth and development, countries which achieved strong growth in the post-war period shared a set of common features: they fully exploited the world economy; they maintained macroeconomic stability; they mustered high rates of saving and investment; they relied primarily on markets to allocate resources; and they had committed, credible and capable governments (Spence Commission, 2008: 21). But the Commission emphasised that there is no single recipe and that countries are best advised to move forward cautiously and with sensitivity to political-economic constraints: ‘the principle is expressed well by Deng Xiaoping’s oft-quoted dictum to “cross the river by feeling for the stones”’ (Spence Commission, 2008: 4).

South Africa already has a diverse economic base. The key challenge is to devise an appropriately diverse set of industrial and labour-market policies to support existing high-productivity activities whilst avoiding the kind of job destruction within labour-intensive firms witnessed in the clothing industry. Mechanisms ought to be explored to ensure that minimum wage setting does not prejudice labour-intensive firms. But what are the relevant stones involved in crossing this particular river? Organised labour has successfully resisted any adaptations to the labour legislation requiring the Minister of Labour to consider adverse employment effects before extending collective agreements. However, the Employment Conditions Commission, which sets minimum wages in sectors without bargaining councils, *is* required to consider employment effects, so there is a political and institutional precedent in this regard. Furthermore, COSATU’s own ‘September Commission’ of 1997 called for a labour-intensive orientation for industrial policy:

‘Our overwhelming need in the short to medium term is to develop labour-intensive industry which is able to employ massive numbers of unskilled and semi-skilled workers. This suggests a focus on sectors such as clothing and footwear, furniture, plastics, electronics/electronic consumer goods, metal products, agribusiness/food processing, construction and tourism.’⁷

Much of COSATU’s economic thinking was solidified in the 1990s before the entry of China into the global economy and the associated dramatic expansion of GVCs. If space can be created, perhaps through the social accord processes favoured by the NDP, for constructive reflection on the implications of today’s globalised world for labour-market policy and job creation, it is possible that

⁷ Available on: <http://www.cosatu.org.za/show.php?ID=5120>

COSATU may agree to policy reforms designed to foster the kind of labour-intensive growth it once demanded. It may agree to the creation of export processing zones in which previously employed clothing workers negotiate wages directly with firms (and at below minimum wages) on the proviso that all production is exported (Kaplan, 2014).

But such measures will probably have to be accompanied by other concessions to reduce inequality such as measures to restrain excessively high executive pay (which fuels resentment among low paid workers, particularly when they are being asked for wage restraint) as well as welfare policies to get income into the hands of the unemployed as fast as possible. South Africa already has an exceptionally pro-poor welfare regime in terms of its pro-poor social assistance policies (Seekings, 2002; 2014; World Bank, 2014) yet the scale of the unemployment problem is such that further measures should be considered such as an employment guarantee scheme (Philip, 2012) or even a basic income grant (Standing and Samson, 2003). This will require additional taxation and consideration should be given to new wealth taxes (notably on financial assets) and to an appropriate mix of new consumption and income taxes on all earners.

Conclusion

In a globalised world, a very low employment rate and high unemployment rate in an upper middle-income economy pose a severe challenge to both policy-makers and development theorists. Policy-makers face not only strong pressure to create jobs, but also powerful trade unions representing mostly skilled workers, widespread expectations of ‘proper’ or ‘decent jobs’ paying high wages, and inherited institutions that sustain a high-wage, high-productivity growth path. Most development theory is of little help in the case of South Africa. Standard theory suggests that economies at low levels of development (or industrialisation) should go down a labour-intensive growth path, but economies at higher levels of development (or industrialisation) should emphasise raising productivity. Existing theory provides little guidance on how to tackle high unemployment in an economy that is already industrialised.

The South African case confirms that, under these circumstances, the single-minded resort to a Porterian strategy of raising productivity results in low employment growth, persisting unemployment and ‘exclusive’ rather than ‘inclusive’ growth. Social welfare programs can, at most, mitigate these outcomes. In cases such as South Africa, Lewis’s proposals for surplus-labour economies remain relevant: Labour-intensive growth needs to be pursued, in appropriate sectors, generally alongside efforts to raise productivity in other sectors.

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