Action Needed to Halve Poverty and Unemployment by 2014

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It has become clear to everybody that, if we are to make progress towards an equitable and peaceful society, we need to act urgently to meet the needs of the poor and the unemployed. Recognising this, the government has promised to halve poverty and unemployment rates by 2014. The question is: how are we to reach these goals?

Last month, the Alliance Economic Summit concluded that there is a need for: (a) a major shift and upscaling of industrial policy to transform the economy so that it creates decent jobs for all South Africans; (b) the establishment of a comprehensive social security protection system to help the poor and vulnerable, and (c) macroeconomic policy to support economic development and employment creation.

The scenarios that follow are based on a macro-micro linked model developed especially for South Africa. Using this, we can capture the link between government policy and household welfare and examine our policy options in relation to the above goals. The process involves positing a series of alternative scenarios that capture government's policy choices and their likely outcomes. The scenarios are progressive: that is, each is followed by another that includes additional interventions designed to overcome the previous scenario's shortcomings. The scenarios are: the current 'no change' scenario; the industrial policy scenario; the guaranteed public employment (GPE) scenario, and the expanded social security scenario.

Policy scenario 1: Current 'no change' scenario

Scenario 1 reflects current macroeconomic policy and a relatively weak industrial policy framework. It is based on the existing medium-term plan for public investment expenditure and extends that to 2014. The scenario produces an average annual growth rate for the period 2009 to 2014 – about 1.3 percent higher than a scenario with no increase in public investment. Yet, although the economy is projected to grow at a moderate level, the estimated unemployment rate for 2014 is only a few percentages lower than current levels. This outcome reflects structural problems with the South African economy, where the employment intensity of growth is low.

Without increased public investment, the poverty rate, estimated at 40 percent for 2008, will increase to 44.2 percent by 2014. Increased public investment improves the average growth rate, but the poverty rate will worsen. Thus the rise in public investment is not expected to change the overall developmental characteristics of the underlying growth path. This scenario will benefit the non-poor more than the poor.

Policy scenario 2: Industrial policy scenario

If Scenario 1 fails to halve unemployment and poverty rates, will an industrial policy that targets employment creation help? That is, what will happen if the rise in public investment is coupled with a set of industrial policy measures that successfully double the sector-specific employment elasticity of growth in the next six years? How will this impact poverty and inequality? How will the macroeconomic balance be affected?

The average annual growth rate generated under Scenario 2 will be slightly higher than for the previous scenario. The increased employment intensity of growth will gradually bring about modest changes in the distribution of economic output. Consequently, relative to Scenario 1, the GDP share of wages and salaries will be higher by 2 percent. This engenders changes in the components of aggregate demand, leading to changes in sector outputs and aggregate supply.

As expected, the gradual increase in the employment intensity of growth means Scenario 2 will generate higher levels of employment than Scenario 1; by 2014, the estimated unemployment rate will drop by almost 5 percent. However, the projected unemployment rate will still be much higher than the target, and the total number of unemployed is estimated at 4.3 million.

The increased job-creation potential of the economy also widens the income channels linking economic growth and poverty. This contributes to a decline in income inequality and produces pro-poor results. Moreover, it produces trade, fiscal, financial and real indicators that satisfy basic sustainability criteria.

Despite relatively better developmental outcomes, the results show that even measures to double the employment intensity of growth will be insufficient to halve unemployment and poverty by 2014.

If industrial policy that targets employment creation helps address poverty and inequality to some measure, what will result if the current public works programme is significantly expanded?

Policy scenario 3: Guaranteed public employment (GPE)

Scenario 3 examines the feasibility and impact of implementing a large part time GPE programme to combat unemployment and poverty. The model simulations show that adding GPE raises the average annual growth rate of the previous scenario.

These results reflect two key yet inter-related dynamics. GPE programmes help raise the income of millions of families, exerting positive pressure on demand as a whole. At the same time, greater employment and more people producing increases the supply of goods and services on the market.

The simulation results show that, by 2014, GPE will add the equivalent of full-time employment for 1.5 million people, with knock-on effects that increase employment in the private sector as well. The model estimates that the unemployment rate will drop to 14.2 percent.

This scenario also demonstrates a significant impact on poverty and inequality. Scenario 3 is pro-poor, since the underlying growth paths benefit the poor more than the non-poor.

How then will the South African economy react to and absorb an expanded guaranteed public employment programme?

A programme that targets 3 million unemployed is expected to reduce the dependency of many families on social security. Consequently, relative to Scenario 2, the total number of persons eligible for social grants is expected to decline by 1.1 million, which translates into a R5.6 billion saving in the social security budget. Scenario 3 is also expected to generate R12.4 billion more tax revenue than Scenario 2.

Therefore, a combination of government saving on the social security budget and the rise in tax revenue reduces the net cost of the GPE to an equivalent of 0.7 percent of the estimated nominal GDP for the same year. When taking into account the positive impacts on growth, employment, poverty and distribution, the inclusion of a GPE programme in the public investment and employment policy scenario will not threaten the country's fiscal position negatively. At the same time, the trade deficit relative to GDP will be manageable and the average annual inflation rate will only be slightly higher than for Scenarios 2.

Overall, Scenario 3, which combines public investment, industrial policy and public employment, successfully halves the unemployment rate. However, although the poverty rate drops 11 percent lower than for Scenario 2, it falls short of the government target for 2014.

Policy scenario 4: Expanded social security scenario

Given the links between social welfare programmes and reductions in poverty and inequality, how can the social security system help halve the poverty rate by 2014?

Currently, the child support grant programme covers children from poor families aged up to 14. Moreover, the social security programme does not include financial support for those providing care to children living in poor households.

Scenario 4 explores the implications of expanding the coverage of the current social protection system. The scenario extends the child support grant to poor children up to 18 years old. It also introduces a new caregiver grant programme, providing financial support to those who care for recipients of social grants, limited to one grant per eligible family.

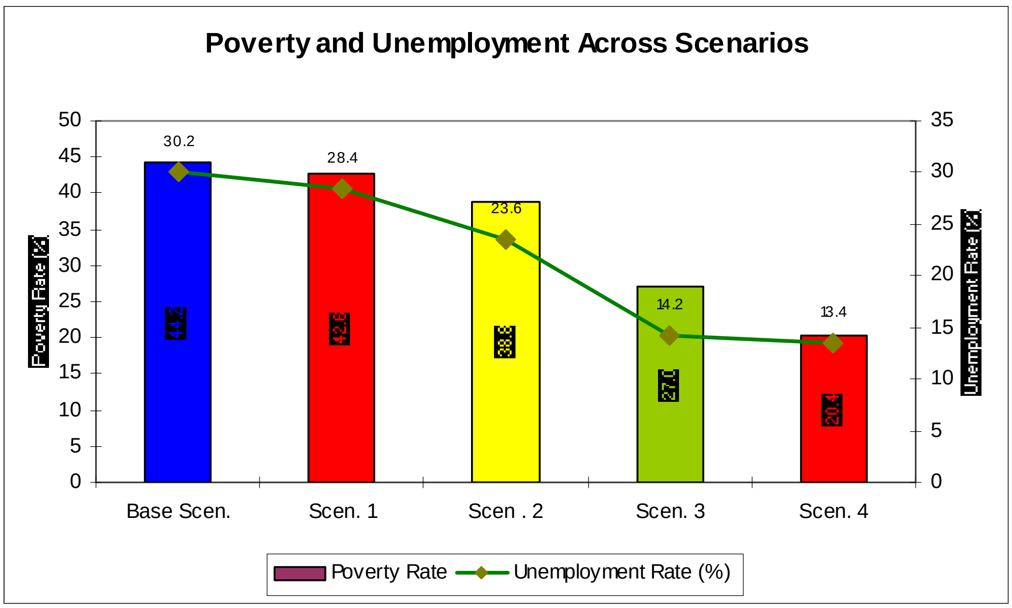
Scenario 4 helps increase the average income of poor families, reduces overall income inequality and helps reach the target for the poverty rate by 2014. At the same time, relative to Scenario 3, even though average real GDP growth remains the same, changes in the sector composition of output help further reduce the unemployment rate. At the same time, the scenario results for fiscal, financial, trade, and real indicators satisfy the basic sustainability criteria.

Conclusion

The scenarios underscore the importance of the government's role in the economy's future path. The growth path depends on a strategy and policy framework that guides government with respect of how, to what extent and for what purpose it uses the policy tools at its disposal. As shown, increased public investment can raise the average growth rate of the economy, but the outcome will not be automatically pro-poor. Although the economy is capable of producing sustainable pro-poor outcomes, additional policy interventions are needed to complement public investment and form a complete set of integrated policies for growth, together with accelerated reductions in unemployment, poverty and economic inequality.

Overall, the scenarios point to the importance of: a strong public investment programme to support growth and economic development; an industrial policy aimed at directly increasing the employment-creating thrust of the growth process; a public employment policy that will systematically help the unemployed, a more responsible social security system, and accommodating macroeconomic policies to help bring about these changes and achieve a growth path that embodies progress towards minimising income inequality and achieving full employment.

South Africa cannot afford to tolerate a scenario that leaves almost half its population in poverty and at least a quarter of its labour force unemployed. Nor can the country be allowed to remain the most unequal in the world.



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