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The Inconsequentiality of Employment Disincentives: Basic Income in South Africa

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In most societies, some poor people are seen as deserving of public or other assistance, generally because they are poor for reasons beyond their control, while others are regarded as undeserving, typically because their own behaviour or choices (for example, laziness) are seen as contributing to their poverty. South Africa, a country with a population of only 45 million, paid more than 10 million monthly grants to some categories of the deserving poor as of early 2006: about 2 million seniors received old-age pensions, more than 1 million people received disability grants (many due to HIV and AIDS), and more than 6 million children received child-support grants. A substantial proportion of poor households are lifted out of poverty by these grants. But there are many other poor people who are considered deserving yet are *not* provided for by the present system.

Many working-age poor are considered deserving of assistance because of the high unemployment rates. South Africans recognize that many of their working-age fellow citizens are poor despite being in good health, and are poor not because of laziness, but because they have too few opportunities for employment or earning a living. South Africa has an unemployment rate of almost 40 percent of the labour force, using the most appropriate measure of

unemployment. This measure includes people who want work but are not looking for work actively. Many unemployed have given up looking for work “actively”, in part because people get jobs in South Africa primarily through word of mouth, not through “active” forms of job search, and in part because in many areas, especially rural areas, there are just no jobs to be had.

The unemployment rate is so high in South Africa in part because of the absence of opportunities in the informal sector or smallholder agriculture, relative to many other developing economies. The apartheid state destroyed the peasantry through forced removals from large farms owned by white people, which led to overcrowding in those rural areas where poor African people retained access to land. The apartheid state also destroyed the informal sector through repressive regulation. Since the end of apartheid, the informal sector has grown but remains small; smallholder agriculture has not re-emerged at all. Unemployed people in South Africa are not simply without a job in the formal sector. They are without paid work of any kind, including even informal self-employment. Public support for the unemployed, able-bodied, working-age poor is limited to modest public works programmes. Therefore, they rely on support from kin who are working, or who receive pensions or another form of social assistance. Thus, many working-age unemployed are dependents of seniors or of disabled people who receive social assistance.

The current combination of a strong social-assistance system (3.5 percent of GDP) and large numbers of uncovered, but deserving, poor provides unusually fertile ground for basic income grant (BIG) advocates. The combination is also unusual: in most countries of the global South, public welfare systems grew from contributory social insurance rather than non-contributory social assistance, for workers in formal employment who are relatively rich rather than the extremely poor. Impoverished seniors receive a pension by right in just a few countries, and in even fewer countries do the sick or disabled, or poor children, receive benefits from broad welfare programmes. Similarly, South Africa’s unemployment rate is rivaled by only those of neighbouring Botswana and war-torn Iraq. Some developed countries have much more extensive systems of public welfare, but for them an unemployment rate of 10 percent is considered unacceptably high.

The combination of social assistance and extremely high unemployment also subverts the oft-presumed association between welfare and withdrawal from the labour force. In more developed Northern welfare states, welfare is presumed to encourage “scrounging”, as people choose to be unemployed and live off the state rather than to look for work. Such a choice is encouraged when welfare programmes are means tested. In South Africa, however, there is little public dis-

cussion of welfare's disincentive effects on the labour supply. The government, which is generally opposed to a BIG, refers to the "dignity of work" and invests small sums in modest public works programmes. Ministers and other critics of a BIG point to its considerable cost and to supposed problems of "dependency" (as if direct dependency on the state is so much worse than dependency on old-age pensions funded by the state). But they rarely cite disincentive effects on employment (Matisonn and Seekings, 2003; Meth, 2004).

The reason is obvious. With such a high unemployment rate, it would not matter to the economy or prevailing wage rates if even a substantial proportion of people withdrew from the labour supply on receipt of a pension. Similarly, no one worries about the possibility that the existing welfare system might discourage work-seeking. Any disincentive to working or searching for jobs is most likely among the unskilled, for whom the marginal gains from employment are lowest, not the skilled, who are economically far more important. A second reason for the weakness of disincentive effects is the very modest value of the proposed BIG. Whereas the old-age pensions and the disability grants are currently set at the equivalent of more than US\$100 per month, proposals for a BIG envisage it being set at about US\$15–20 per month per person. Even Mangosuthu Buthelezi, the leader of the Zulu nationalist Inkatha Freedom Party, has come out in support of a BIG, in part because "the low level of the grant is unlikely to prove to be a disincentive for people to find work that pays more than the grant" (Buthelezi, 2007).

1. Evidence of Labour Market Effects

There is some evidence on the actual effects of social assistance on labour supply in South Africa precisely because South Africa already has a range of generous social assistance programmes.

Lam et al. (2005) examine the direct effects that old-age pensions have on participation in the labour force and work. They point out that the means test is not administered aggressively, and survey data show that a minority of pension recipients readily admit working. The effect of the pension on work is simply an income effect: Is the pension sufficiently generous that a significant proportion of seniors decide not to work? Using data from both sample surveys and censuses, Lam et al. show that the old-age pension does affect labour supply. Among the poorest racial section of the population, participation rates among both men and women decline sharply at the age at which they become eligible for the pension. About half the African men who are participating in the labour force at the age of

64 (when they are not eligible for the pension) are no longer working at the age of 66 (when they are). The data also show, however, that labour-force participation rates decline steadily with age from as early as the age of 45. *Most* poor men and women are no longer working or wanting work prior to the age at which they become eligible for the pension. Therefore, it is likely but not certain that the introduction of social assistance for men younger than 65 and women younger than 60 would reduce labour supply. But there would only be a very small reduction in the actual working population, since many of the people who would withdraw from the labour force would otherwise be unemployed.

Booyesen and Van der Berg (2005) examine the effects of grants among households affected by HIV and AIDS. They found that receipt of an old-age pension or a disability grant by an AIDS-affected household increased the likelihood that a household member would be unemployed but made no difference to labour-market participation. As Booyesen and Van der Berg suggest, this is as likely to be because illness forces other household members to give up work to care for the sick as it is to be an indirect income effect. They also found that receipt of the modest child-support grant (about \$25 per month, paid to poor mothers) *increased* the likelihood of labour market participation. One plausible explanation for this is that the cash income, however meager, makes it possible for a mother to employ child care – perhaps even within the household – and thus makes it possible for her to look for work.

2. The Basic Income Grant

The trade-union-led BIG Coalition and a government commission of enquiry recommended a BIG of \$15–20 per person (Seekings, 2002; Standing and Samson, 2003). The proposed value of a BIG in South Africa is a small fraction of the value of the current old-age pensions as far as individuals are concerned, although the aggregate value of BIG in a larger household would be substantial. Therefore, the effect of a BIG on an individual's decision to work or to look for work is likely to be minor relative to the effect of an old-age pension or a disability grant. The value of a BIG would be more similar to the child-support grant. Therefore, any small negative effects on employment would, quite possibly, be offset by small positive effects on labour-market participation.

Even if a BIG does have a minor disincentive effect on labour supply, this is probably not a bad thing. Given South Africa's exceedingly high unemployment rate, encouraging some unemployed men and women to stop looking for work might be a good idea. Encouraging more men and women to retire in their 50s

would have major social benefits for society, if it opened up more opportunities for younger people.¹ This would be a strong argument for reducing the age of eligibility for the means-tested old-age pension. The overall dependency ratio in the economy is a concern, because relatively few people are working and even fewer are paying taxes at the same time as many others are dependent on them, either privately or through the state. Increasing employment is an urgent priority and is indispensable to long-term poverty reduction. But it is unlikely that the expansion of low-benefit social assistance is going to have a major effect on the dependency ratio. The fundamental causes of chronic and high unemployment in South Africa remain the lack of demand for unskilled labour, in itself due in part to public policies that favour capital- and skill-intensive growth, and to the inadequacies of public education.

The South African case reveals some of the complexities in the relationship between unemployment and basic income. High rates of unemployment increase the importance of a BIG in terms of poverty reduction. They also reduce or even eliminate concerns about disincentive effects on employment. But they also make it hard to finance any form of public expenditure. At present, there is much less public enthusiasm for a BIG than there is for existing social assistance programmes. Most South Africans think that *some* poor people are undeserving because they have made insufficient effort. But many poor people who do not receive social assistance are considered deserving. These include men and women in their 50s (and men in their early 60s) who lack skills and whose meager prospects in the labour market are not of their making. Because there are so many of these deserving but currently unassisted poor, there is support for welfare reform.

If social assistance is extended to a large number of such deserving poor, then South Africa might soon reach the stage where the costs of administering a means test on social assistance exceed the benefits in terms of payments to the nonpoor, and where the costs of running several programmes exceed the costs of including everyone in one standard programme. Even if the concept of a basic income enjoys only patchy support among both elites and the general public, and despite some likely small effect on labour supply, it might become rational (as well as moral) to shift from an unreliable quilt of social-assistance programmes to a universal BIG.

¹ Most African men and women above the age of 50 lack skills; the minority who are working are, for the most part, very dispensable in macroeconomic terms.

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