

# Second Economy Strategy: Addressing Inequality and Economic Marginalisation

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## 1. Does South Africa have a ‘second economy’?

It depends entirely what is meant by the term.

If the concept is used to suggest that the ‘second economy’ ‘is somehow separate from the economy as a whole, exists in parallel, and is underdeveloped *because* it is disconnected from the ‘first’ – developed - economy, then it describes a fiction.

If, on the other hand, the term is used to describe the ways in which high levels of structural inequality and economic marginalization are manifest in South Africa, and the conditions of poverty which these perpetuate - then the concept may be useful for focusing policy attention on these issues. And the challenges of addressing inequality and economic marginalisation remain, however we choose to describe them.

The Annual Report of the Accelerated Shared Growth Initiative of South Africa (AsgiSA) presented in February 2007 identified a need for more focus on ‘the second economy’ and on mechanisms to ensure shared growth reaches the margins of the economy. The Presidency initiated the Second Economy Strategy Project, to focus on the development of strategies to target these issues. A Strategic Framework entitled ‘Second Economy Strategy: Addressing Inequality and Economic Marginalisation’ was approved by Cabinet in January 2009. In this framework, it is the latter interpretation that is used; the key arguments presented in this framework are summarized below.

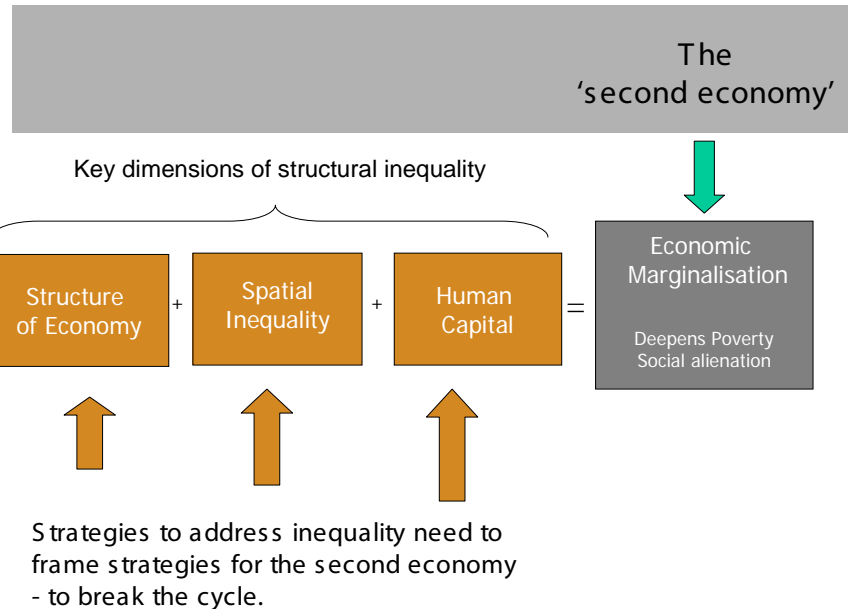
## 2. Structural inequality is the root of the problem.

South Africa has a highly unequal economy in which people with access to wealth experience SA as a developed modern economy, while the poorest still struggle to access even the most basic services. Stark as these differences may be, these realities are connected and interdependent in a range of complex ways, with certain common processes producing or reinforcing these extremes in access and opportunity. These issues have been the source of long-standing debate and scholarship in SA, which has sought to make these relationships visible.

Key legacies of apartheid make inequality deeply structural in SA – in particular:

- The centralised, monopoly structure of SA’s core economy - including labour market legacies of the pass laws, and migrant labour, as well as the highly skewed distribution of assets.
- The spatial legacy of bantustans and apartheid cities;
- The impacts of inequality of access and hence outcomes in relation to human capital.

These forms of structural inequality hamper the best efforts of development policy, reinforcing old forms of economic marginalisation at the same time as facilitating new ones. Strategies to address economic marginalization – or ‘the second economy’, if you want to use the term – have to be framed by strategies to address such structural inequality.



### 3. The Core Arguments

#### 3.1. While the main target is to end poverty, inequality matters as an issue for the following key reasons:

- In South Africa, structural inequality plays a key role in sustaining diverse forms of economic marginalisation and limits the potential for growth and employment creation;
- Evidence suggests that highly unequal societies tend to grow more slowly, and that the effects of such growth tend not to be pro-poor (World Development Report 2006). Addressing inequality is therefore key to achieving shared growth.
- In SA, the levels of growth required to impact significantly on poverty within current patterns of distribution are probably unattainable; shifts in the patterns of distribution are therefore a necessary part of an anti-poverty strategy.
- High levels of inequality can cause social conflict. This is undesirable on its own terms, but it has economic as well as social costs also.

#### 5.1. The structure of the SA economy constrains employment creation in the core economy as well as in more marginal contexts:

**In the core economy:** The South African economy is highly centralised, capital intensive and dominated by a set of monopoly industries. While policy has focused on addressing this in the core economy, through effective competition policy, for example, the structure of the economy also impacts on economic opportunities in more marginal contexts.

**On the margins:** In many developing countries, the informal sector provides easy access to livelihood opportunities for those unable to find formal employment. SA's relatively small micro-enterprise sector is often attributed to lack of skills, entrepreneurship or access to credit. Important as these are, this often overlooks the way the structure of the economy constrains the scope for growth in this sector, for the following reasons:

- Opportunities for small manufacturing enterprises targeting poor consumers are limited because most manufactured goods bought by poor people are already mass-produced in the core economy and are available even in remote areas.
- Access to opportunities beyond the local economy, in higher volume and/or higher-value markets tends to require greater levels of formality. While this is where the most scope for SME development and job creation exists, there are higher barriers to entry in these markets.
- Opportunities do exist in relation to fresh produce and services, but these tend to be small in scale unless they're part of more formal value chains.
- The scope for small artisan-based enterprises is limited by the skills challenge and the high demand for such skills in the formal sector.
- As a result, SA's informal and/or micro-enterprise sector is unusually dominated by retail activity, often in a dependent relationship to the core economy. There are limits to the scope for this sector to expand, or for street traders or spazas to climb a 'ladder' into more formal enterprise: that space is taken, with 'big retail' also increasingly encroaching into markets currently served by this sector.

## **5.2. The small farming sector and subsistence agriculture perform a very limited employment and/or safety net function in South Africa**

In many developing countries, such as India, China and Tanzania, the small farming sector is a dynamic part of food production and of rural local economies, and subsistence agriculture provides a form of safety net when employment opportunities fail. In SA, this role is severely constrained.

The coercive processes that forced black South Africans off the land and the men into labour markets in the early part of the last century destroyed the small-farming sector and led to the 'de-agrarianisation' of former Bantustan areas.

These processes stand in contrast to the active policies of support to white farmers over the same period. There have been decades of investment - including substantial subsidies - into the development of a 'big farm' model and the institutions required to support it: including access to land, water, inputs, credit, business services, infrastructure, and market access - as well as opportunities to share in the development of an increasingly vertically-integrated agro-processing sector.

In the former bantustans, however, these processes were mirrored by their opposites: those attempting to engage in agricultural production on increasingly small plots of land were not supported by the development of any of the institutions required to make a small-farm model viable. These two agricultural development paths still co-exist in an uneasy relationship.

## **5.3. The former bantustans face a chronic development deficit**

This skewed investment in agriculture was matched by the skewed investment in human capital, economic infrastructure, and access to basic services within the bantustans. This was coupled with coercive and patronage-based governance structures, including customary systems in which women's economic initiative was constrained - even though men were often absent. The former bantustans still have far to go to remedy these defects: and remain home to the poorest people in SA, and the poorest women in particular.

**5.4. Poor people are unusually dependent on wages and/or grants in SA; these in turn depend heavily on the performance of the core urban economy**

The constraints on the micro-enterprise sector as well as on smallholder or subsistence agriculture mean that poor people in SA are unusually dependent on wage income and/or grant income, relative to other developing economies. Both of these depend heavily on the performance of the core economy – which is largely an urban economy.

**5.5. Urban inefficiencies constrain growth and place a cost burden on workers and the poor**

Apartheid locked urban areas into unequal and inefficient patterns of development. These have been compounded by implementation choices and land market logics that still see poor people housed far away from economic opportunities, in poorly-planned, low-density housing settlements that have high service-costs, lack social-service infrastructure and do not facilitate local economic activity.

Yet these new housing developments have not managed to keep up with the influx to urban areas, and the growth in informal settlements and backyard shacks.

**5.6. Reliance on the wage mechanism to cover wider social and economic costs raises the costs of labour and disincentivises labour-intensity.**

Many of these social and economic costs are carried directly and indirectly by the poor, and impact on the costs of labour – such as through the high cost of transport. With limited social protection targeting the unemployed, workers often support an ever growing network of unemployed dependants.

This level of reliance on the wage mechanism to cover wider social and economic costs - rather than using the social wage to do so – strengthens wage pressures and impacts on labour costs and the costs of production in general – strengthening existing biases against labour-intensive production.

**5.7. High costs of living and high dependency ratios mean low-wage jobs do not lift people out of poverty.**

While growth since 2004 has become increasingly labour-absorptive, most new jobs have been in the retail and construction sectors: poorly paid and highly insecure. Casualisation and externalization have added to the phenomenon of the ‘working poor’ – those whose income from work is insufficient to lift them out of poverty.

**5.8. Youth, women and rural dwellers carry the highest burden of unemployment**

While unemployment is a structural problem, additional factors skew its distribution, with unemployment levels for black youth, women and rural dwellers disproportionately high.

## 6. What are the implications of this for strategy?

Firstly, a wider focus on inequality is needed. While this agenda should address all the areas of structural inequality identified, there are two clear priorities:

- Human capital development – with a particular focus on the ‘points of no return’ – early childhood development and child nutrition. Where these fail, policy is forced to focus on mitigating for yet another generation.
- The social wage. So far, this has had the greatest impacts on poverty and inequality. Strategies need to focus on gaps in coverage: social protection for the unemployed, access to basic services and to affordable public transport.

Secondly, employment creation on decent terms needs to be placed at the heart of all economic policy; it is the most important mechanism for addressing poverty, economic marginalisation and inequality. Employment creation can no longer be treated as a secondary concern in industrial policy and expectations that it can be achieved through small enterprise development or self-employment strategies need to be mitigated by a sharp reality check.

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**Employment creation ‘from below’ – through micro-enterprise or self employment - faces significant constraints and is a poverty trap for many.**

- The structure of the economy constrains the scope for significant or sustainable expansion in this sector – but the scope that does exist must be supported.
  - Evidence shows that those least likely to get a job are unfortunately also least likely to succeed in becoming self-employed;
  - Employment strategy cannot therefore rely on the poorest and most economically-marginalised people in the economy ‘self-employing’ their way out of poverty.
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Support to both the small enterprise sector and to the informal sector needs to be designed within a more realistic set of expectations of its scope for growth. This means more focus on the ‘patient support’ required to turn ‘start-ups’ into ‘stay-ups’, more caution in promoting self-employment as a solution for all – and a greater focus on the scope for employment creation in the core economy.

In practice, like it or not, new market-based employment is likely to be largely urban, where ‘urban’ includes small towns and dense settlements. Building efficient and inclusive cities and towns is vital to enabling economic dynamism.

Creating rural employment will be a greater challenge, and will therefore require a stronger catalytic role from the state to achieve results, as part of a wider strategy for rural development and agrarian reform.

Finally: all of the above is crucial to finding sustainable solutions: but these will take time, and will reach the most marginalised last.

**We need to prioritise strategies that reach the most marginalised first.**

There is no time to lose in building people’s sense of economic agency – of their capacity to change their material conditions through their own actions, to be productive members of their household, their community and their society. This requires that we find ways to facilitate their economic participation even where markets do not do so.

In particular, there is a need to provide a form of employment safety net until wider economic policies are able to deliver jobs: to strengthen people's capacity to work, and to provide access not only to income, but also to work experience and the enhanced dignity, social inclusion and economic agency that comes with it.

This is why it is proposed that we need to adapt the concept of a minimum employment guarantee to South African conditions, to target the most marginalised and to ensure that those who are willing and able to work can be sure of access to a minimum level of regular employment.

The Community Work Programme was initiated by the Second Economy Strategy Project, to develop such an approach, and has been piloted in a partnership between the Presidency and the Department for Social Development. It is now part of Phase 2 of the Expanded Public Works Programme. In President Zuma's State of the Nation address in June, he committed government to 'fast-track' the Community Work Programme, and it is currently being institutionalised in government to enable rapid expansion and roll-out in the most marginalised areas.

The CWP provides a minimum level of regular work – two days a week – to those who need it. It is assumed people will move in and out of the programme as their needs change, but the programme itself is expected to be ongoing at local level, providing an employment safety net that complements other livelihood strategies.

Finally, while the Framework emphasizes the urgency of targeting the most marginalised first, it concludes that in order to achieve sustainable solutions to inequality and economic marginalization, there's just no alternative but to address the challenge of restructuring the economy as a whole – and not just 'fixing' the second economy – or whatever you choose to call it.

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