

POLICY AND PLANNING BRIEF SERIES NO.1

Poverty, inequality and unemployment



Achieving a social protection floor and decent standard of living

The impact of state services on the cost of living for the poor

INTRODUCTION

This policy brief begins by sketching out the background that contributes to the policy and planning approach of the National Planning Commission (NPC) in promoting initiatives and expert dialogues on the understandings and role of a social protection floor in reducing poverty and achieving a decent standard of living. It goes on to analyse the cost of living trends and the impact these trends have on poor and working class households, and provides an overview of free government services and the impact they have. It also examines the factors that drive up costs, and the effects of these on consumption patterns. Finally, it focuses on strategies that the NPC can consider to reduce the cost of living of poor and working class households to achieve a decent standard of living.

CONCEPTUAL AND POLICY BACKGROUND

South Africa's *National Development Plan 2030: Our Future: Make It Work* (NPC, 2011a) is the overarching framework within which responses to poverty, inequality and unemployment is being addressed. Chapter 11 of the National Development Plan (2011a: 341) notes that:

Concepts such as a social wage and social floor have been used in South African debates to adjust crude distributional indicators to reflect a more balanced picture of distributional fairness. It is generally recognised that there is a need to identify a crucial "package" of social benefits capable of generating levels of social inclusiveness to radically transform economic development in South Africa. South Africa needs to work towards defining a social floor below which no one should fall.

The National Development Plan (NDP) further asserts that, together with social partners, a social protection floor should be determined that can be progressively realised. A social protection floor is understood as an essential prerequisite in reducing chronic structurally-based poverty, unemployment and inequality in South Africa. In 2009, the United Nations stated that a social protection floor could consist of two main elements that would in turn help to realise human rights¹ as contained in the Universal Declaration of Human Rights, namely:

- Services: Ensuring the availability, continuity, and access to essential public services (such as water and sanitation, health, education and family-focused social work support);
- Transfers: A basic set of essential social transfers, in cash and in kind, paid to the poor and vulnerable to enhance food security and nutrition, provide minimum income security and access to essential services, including education and health care.

The UN does not prescribe how countries design this social floor, but does recommend that each country adopts an approach that takes into account what is possible given the institutional, financial, and legislative contexts. In the South African context, the elements of the social floor should be consistent with the constitutional requirements and achievable within the institutional, financial and legislative capabilities of the country. The NPC links the process of attaining a decent standard of living through two processes: defining a social floor; and reducing the cost of living, particularly for income-poor people and households.

Income poverty and multiple deprivations are linked, and influence individuals' and households' capabilities and resilience to cope with shocks and vulnerabilities. A decent standard of living also includes the support required for them to access health and education, which, as part of a social protection approach, are instrumental in building this capability and resilience, thereby reducing inequality and eradicating poverty.

South Africa's existing social protection system includes a range of measures that together form the basis of what could constitute a social protection floor. These measures include income support through social assistance cash grants, such as the Child Support Grant, Social Old Age Pension, and Disability Grant; social insurance, such as the Unemployment Insurance Fund; free basic services in the form of stipulated quantities of water and units of electricity; free housing for those earning below R3 500 per month, in the form of Reconstruction and Development Programme (RDP) houses; and the provision of subsidised housing for those earning between R3 500 and R7 000 per month. Free education is provided in 60% of schools in poor communities, and a school nutrition programme also ensures that school children have access to at least one school meal a day (NDC, 2011a). Free health care is provided for pregnant women and children under six years and free primary health care should be available to all who need it.

Taking note of existing interventions by the government, the NPC is focusing on what needs to be done additionally to reduce the cost of living so that a decent standard of living is attainable in income-poor households. A key question is: "How will initiatives to reduce the cost of living link with an agreed social floor in South Africa?"

South Africa has one of the most unequal income levels in the world, with the richest 10% of households accounting for over half of household consumption and 95% of financial assets. The National Development Plan (NDP) argues that inequality and poverty can be addressed by raising incomes through productivity growth and reducing the cost of living to improve the living standards in poor and working communities. It suggests that a "commitment to a minimum living standard will ensure that all households can meaningfully participate in the economy," and goes on to say that the "costs of food, commuter transport and housing must be reduced, while raising the quality of free or low-cost education and health care" in order to achieve this.

¹ Human rights relating to health, education, employment, social security, water and sanitation are reflected in the Universal Declaration of Human Rights, paras. 22, 25 and 26, and subsequent legally binding treaties. These rights are also reflected in the Bill of Rights in South Africa's Constitution of 1996.

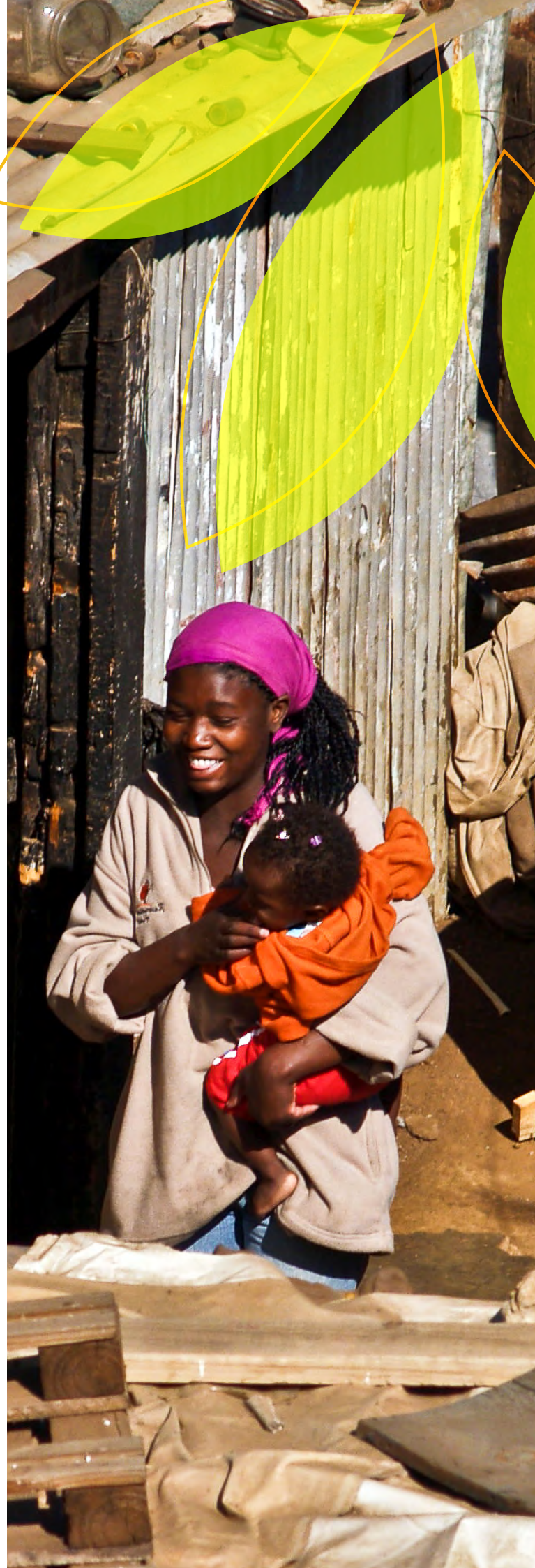
COST OF LIVING TRENDS FOR POOR AND WORKING-CLASS HOUSEHOLDS

This section analyses the key cost drivers for marginalised households and the formal labour force and indicates where the current structure of service provision and/or pricing reproduces inequality or tends to impose excessive burdens on poor households. Finally, it examines the way state services can promote both improved conditions and more inclusive growth on the basis that, if the cost of living can be lowered for working people without damaging their quality of life, the economy as a whole effectively becomes more efficient, which, in turn, should lead to stronger growth and job creation. There are significant differences in consumption patterns and cost drivers of poorer households compared to those on the other end of the income scale. Shaping state services to promote inclusive growth therefore requires an understanding of how these different groups relate to the economy, principally through employment.

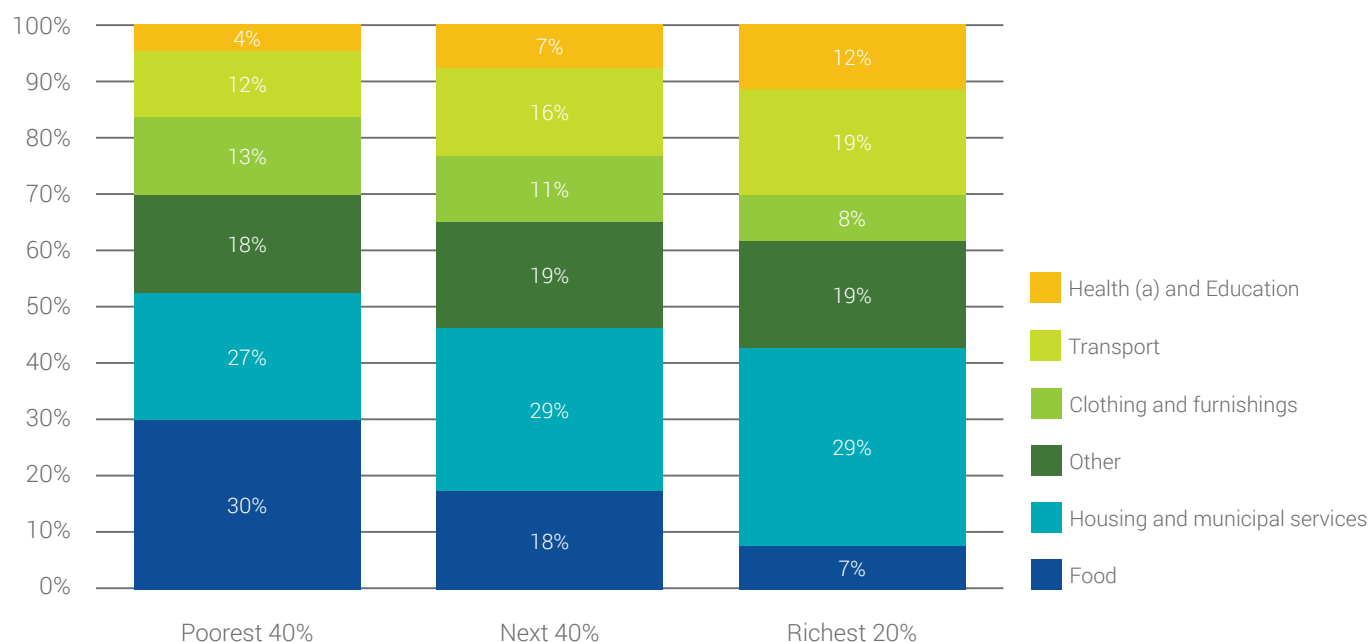
Families with at least one formal employee generally belong to the better-off 60% of all households. In contrast, the poorest households have limited and largely informal or poorly paid employment, if they have any at all. These families are disproportionately found in the former so-called “homeland” areas, where the main obstacles to job creation arise not from the cost of labour, but rather from factors such as poor infrastructure and the remoteness of urban markets, limited access to water and good land, and shortages of capital and skills. Research on which this policy brief draws shows that a significant income gap exists between the richest 20% and the rest of households, with relatively small gaps between deciles from the poorest to around the 60th decile. It also establishes that while most households in the poorest 40% had some access to income, these incomes were under R2,000 a month.

COST DRIVERS FOR HOUSEHOLDS

The cost drivers for the poorest 40% of households and the formal workforce differed significantly because they could not afford the same sets of goods and services. Using the 2010/11 Income and Expenditure Survey, this analysis reviews trends in composition and inflation for major elements of consumption by income level. It reveals that for the poorest 40%, almost a third of expenditure went on food. For the next poorest 40%, the figure fell to under a fifth, and for the top quintile, it was less than a tenth. The share of clothing and household furnishings in expenditure also declined with income.



Share of expenditure by major consumption and income groups, 2010/11

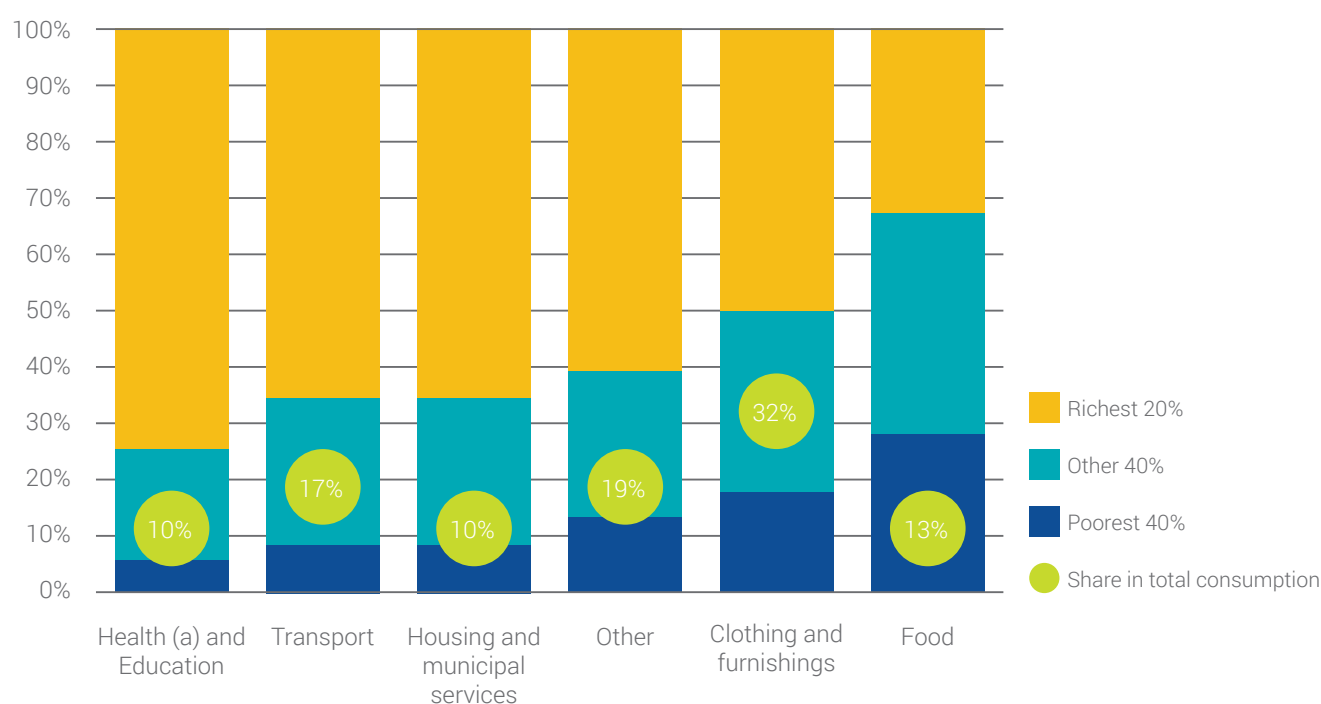


Note: (a) Includes health insurance, which Statistics South Africa categorises under miscellaneous. Source: Calculated from Statistics South Africa. Income and Expenditure of Households 2010/2011. Pretoria. 2012. Page 128 ff, Table 2.45.

Other major consumption groups absorbed a rising share of spending as income increased. For example, housing climbed from under a quarter of expenditure for the poorest 40% of households to over a third for the richest quintile (although this figure should be approached cautiously, since the main driver was imputed rent for homeowners, rather than actual expenditure). Transport rose from 12% of spending for the poorest 40% to almost 20% for the richest quintile, largely because car ownership increases with income, and health and education climbed from 4% of spending for the poorest 40% of households to 12% for the richest, with the bulk of spending going for health insurance and, in education, tertiary education.

Because of South Africa's unusually unequal income distribution, the richest 20% of households accounted for the bulk of consumption expenditure for every major product group except food. As a result, food, clothing and furnishings constituted under a fifth of total consumption expenditure for the country, although they made up two fifths of spending by the poorest 40% and over a quarter for the next 40%. In contrast, housing and transport, which are more important for rich households, accounted for half of total consumer spending, although they absorbed only around a third of expenditure for the poorest 80%.

Share of expenditure by major consumption and income groups, 2010/11



Source: Calculated from Statistics South Africa. Income and Expenditure of Households 2010/2011. Pretoria. 2012. Page 128 ff, Table 2.45

IMPLICATIONS FOR CONSUMPTION

This study identifies the main expenditure groups as food, housing and utilities; transport; clothing and furniture; education; and health.

FOOD

Food is a critical element of consumption for the most marginalised households, and nearly as significant for the formal labour force, especially in lower-wage industries such as retail, security and agriculture. Generally, however, inflation has been higher for food than other goods, largely because of rising red meat prices and, more recently, the drought. If the NDP aims to moderate the cost of living for marginalised households in particular, then it will need to reverse the long-standing trend toward relatively high food inflation. In the longer run, that would require measures to address the concentration of production, storage, processing and sales in the food value chain. The Competition Commission has begun to examine these issues. Medium to short-term possibilities include encouraging food gardening on a larger scale; engaging with the major supermarket chains to reduce the mark-up on a basket of staple foods, for instance maize meal, standard loaves of bread, frozen poultry and vegetables; resisting lobbying to increase tariffs on imported poultry before practical and specific measures are introduced to protect poor households; zero-rating VAT on staple foods and ensuring that retailers pass the benefits on to poor households (but there is little price difference between standard brown and white bread, for example, which suggests that the difference in VAT is not benefiting consumers); and increasing social grants by the rate of inflation for low-income households, rather than by the overall rate of inflation.

HOUSING, UTILITIES AND TRANSPORT

Housing

A legacy of apartheid is that formal housing is virtually unaffordable for most low-income households, who therefore depend on state subsidies. Although most own their own dwellings, they are generally inadequate and distant from economic opportunities. The upper end of the formal workforce are more likely to be in rentals, but in real terms the cost fell from 2011 to 2015. In contrast, while utilities and water made up a relatively small share of spending for households in the past, the cost rose sharply, especially from 2008. Moreover, as of 2015, only around two-thirds of households in the poorest 40% had running water in their houses or yards. While the analysis in this study suggests the main mechanism for addressing the housing crisis for the poor continues to be the provision of subsidised housing, these would work better in the context of: (a) improvements in planning for rural-urban migration; strategies to structure the built environment, as well as communications and transport systems, to make it easier for both marginalised households and the formal labour force to engage in the economy; and (b) measures to expand rental housing for the formal labour force, which meets the needs of these relatively skilled and well-paid workers, in that it is both reasonably high quality and offers easy access to economic centres.

Energy

The relatively rapid increase in electricity and other fuel prices from 2008 confronted poor households with a sharp hike in tariffs, despite some measures to alleviate the impact of electricity price hikes on the poor. At the same time, the extension of electricity to new households meant that they could replace comparatively high cost and dangerous fuels and candles with electricity, which remained a more efficient source of energy even at the higher prices. Nevertheless, by 2016 electrification had reached most households. The remaining houses without electricity tend to be poor and either relatively remote or part of new informal settlements. Unfortunately, South Africa has failed to diffuse available efficient renewable technologies for poor households on a large scale, with the exception of solar water heaters. This kind of technological shift could, at least, to some extent, have reduced the cost of electricity for low-income households. Still, even without a shift to more affordable energy sources, the end of the commodity boom moderated electricity price increases significantly. In addition to slowing the increase in the price of coal in rand terms, it brought downsizing at major refineries, which were key electricity consumers.

Water and sanitation

Although water and sanitation together appear to be less expensive for poor households than for higher-income ones, in contrast to electricity, the price of water to households rose faster than overall inflation from 2008, which would raise the cost of living for both marginalised households and the formal labour force. The relatively rapid increase in the price of water and related services for households obviously places a particularly heavy burden on poorer families. Still, as with housing, the price of using water does not seem to be the main problem for poor households, if only because many simply do not pay. A bigger threat to their quality of life is the persistent lack of access and the poor quality of the water supply and sanitation in many low-income communities. Again, as with housing, the first need is to secure affordable access for more South African households.

Commuter transport

Transport is critical for marginalised and working households because many live far from economic and social centres. They spend far less than richer ones on transport, in both rand terms and as a share of their expenditure, mostly because they rely on public transport rather than owning a car, but nonetheless, it absorbs a significant share of their budgets. The time, physical risks and unpleasantness of commuting on public transport places additional stress on many workers. Densification along commuter corridors and the development of more mixed-income housing near urban centres remains the main way to reduce transport costs for marginalised households and the formal labour force, which would, require fundamental shifts in the housing strategy. In the interim, a more rigorous analysis of current transport systems and more innovative and diverse solutions is necessary including, for example, wider use of bicycles so that marginalised households have an easier alternative to walking, as well as a significant expansion in low-cost individualised public transport, such as motor cycle and three-wheeled taxis to reduce the time required to get to public transport hubs.

CLOTHING AND HOUSEHOLD GOODS

As a percentage of household expenditure, spending on clothing and household goods declined steadily with income. The poorest households spent almost a seventh of their budget on these goods; the richest, under a tenth. Clothing and non-durable goods absorbed a much higher share of the budget for the poorest 80% of households than for the richest quintile. A substantial increase in imports since 2002 has helped hold down the price of clothing and furnishings, and since 2008 the state has embarked on a large-scale programme to roll out solar water heaters to low-income households. However, outside of this, the state has only influenced the cost of most clothing and furniture through industrial policy support and tariffs, which primarily aims to promote domestic production and protect employment. Trade-offs between efforts to promote local production and domestic prices for households arise only for the relatively small share of imports that constitute wage goods for low-income households. For these goods, a choice may emerge between moderating the cost of living for marginalised households and the formal labour force in the short run, and growth and job creation in the longer term. This trade off becomes particularly visible when the rand is at uncompetitive rates. The ideal way to manage it is to make more competitive production of wage goods a leading priority in industrial policy.

EDUCATION

Access to education remains highly unequal, which in itself reproduces inequality. Members of the richest 20% of households made up almost 60% of all university students in 2015. This situation arose in part because of the high cost of tertiary education, which accounted for the bulk of spending on education for the poorest 80% of households, and in part because of the persistent inequalities between rich and poor schools, which largely tracked the pattern set under apartheid. Fees for education at all levels have risen faster than overall inflation, but poor households generally do not pay for general education. As a result, the direct impact of rising education fees is greater for the formal working class, although the main effect is not on the cost of living, but rather through the exclusion of low-income learners from the best schools, which in turn reduces their chances of getting matric and post-secondary education.

HEALTH

Health is both a larger cost and more inequitably distributed between households than education, particularly in light of private medical schemes. The cost of health spending, including insurance, is a substantial cost driver for formal workers, in particular across the top 40% of income earners. State spending on healthcare is more focused on low-income households, since the relatively well-off largely use fully private institutions, rather than the kind of semi-privatised institutions found in education, and is more equitably distributed across income levels. Nevertheless, public health services vary to some extent by income level, in part because of the failure fully to overcome the inequalities entrenched under apartheid. The substantial differences in both private and public spending on health by income group contributes to markedly worse health outcomes for lower-income households, including in terms of disability and mortality.





STRATEGIES TO ENSURE THAT STATE SERVICES PROMOTE INCLUSIVE GROWTH AND REDUCE THE COST OF LIVING

As the NDP indicates, programmes to address the cost of living for poor and working households can promote inclusive growth in two ways:

- 1) **Government services and grants:** Poverty in itself prevents many households from taking advantage of economic opportunities. Where families face a daily struggle to survive, they cannot search for employment, pay to travel to work, maintain their health, and improve their children's education. In this context, government services and grants enable poor households to seek and hold down a steady job. Moreover, by providing both some initial resources and a safety net, they make it easier for low-income people to take on the costs and risks involved in setting up micro enterprises.
- 2) **Social wage:** State services and industrial policy can minimise the cost of living for employed people, thereby enabling workers to enjoy a decent standard of living without increasing costs for employers. The social wage directly benefits workers and indirectly incentivises job creation by moderating the cost of labour relative to capital.

In response to the NDP proposals, this study provides options for specific strategies to ensure that household and family services support inclusive growth.

KEY FINDINGS

- Programmes designed to improve living standards and productivity for poor households differ from those to moderate the cost of living for the core labour force. Poor households typically fall into the poorest 40% of households, which are disproportionately in the former so-called "homeland" regions; the formal labour force is primarily in the next most prosperous group. These groups have significantly different consumption patterns and consequently different requirements.
- Prices for food rose faster than other prices since 1994, even before the recent drought led to a sharp upturn. Since food is the biggest actual expenditure for the poorest 80% of the country, this is a cause for concern. High levels of concentration across the food value chain contributed to this situation. Food inflation would have been even worse if not for the rapid increase in frozen chicken imports, mostly for the low-income market, which stabilised the price of chicken while other meat products saw sharp price hikes.

- Most poor South Africans own their homes, so housing inflation, which was below Consumer Price Index (CPI) over the past 15 years, was not a critical driver for the cost of living. The apparent high cost of housing in the inflation basket for the formal working class reflected imputed, not actual, payments by homeowners. Still, the majority of households in the poorest 80% live in cramped formal or traditional houses or, in the case of around a quarter of households, informal dwellings. The housing problem persists due to a combination of extraordinarily high rural-urban migration, especially to Gauteng; the discrepancy between incomes and the cost of new formal housing, which has been met largely by housing subsidies; and the continued tendency, which is built into the current housing subsidy system, to push poor people far from economic and social centres.
- In 2015, nine out of ten in the poorest 80% of households had electricity for lighting, but only two thirds had piped water. While the cost of utilities taken together ran around 4% of budgets for the poor, their cost increased much faster than the rate of inflation from 2008. In the case of electricity, this situation in part arose because of a spike in the price of coal during the commodity boom. Efforts to fund major new bulk investments from around 2005 and municipal revenue seeking also fuelled higher household tariffs.
- The time and money spent on commuter transport remains a major factor reducing the standard of living for poor households. Most workers rely on a combination of walking, taxis and buses to get to work, spending an average of over an hour each way in the process. The cost of public transport tended to track the price of petrol, despite significant subsidies.
- Clothing and household furnishings represent a major source of expenditure for the poor. Because of high levels of imports, the prices of these goods have risen more slowly than inflation as a whole. From this standpoint, the challenge for industrial policy is to promote more competitive local production of basic products.
- The cost of university education accounted for the bulk of education costs at all income levels. In contrast, children from most low-income households did not pay for general education, but the quality of their schools was often very poor. As a result of this situation, close to 60% of all university students came from the richest 20% of households, which in itself replicates inequality.
- In health, as with education, marginalised households typically rely on free public services, which means their costs are relatively low. In contrast, formal-sector workers often have health insurance and turn to the private sector. As a result, health costs are a significant cost driver for formal semi-skilled and skilled workers, which in turn raises the cost of employment across the economy.



This policy brief will be used to advance discussions with stakeholders on the key elements of a social protection floor and system.

The full paper is available at:
www.nationalplanningcommission.org.za

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