Integrated social development as the accelerator of shared growth
Executive summary

South Africa has embarked on an initiative to accelerate economic growth in support of shared income (ASGI-SA), which succeeds the RDP and GEAR strategies. The latter policies, which focussed on macroeconomic stabilisation and trade liberalisation, have contributed significantly in improving the economic growth performance in South Africa over the past decade. The recent momentum in GDP growth has been predominantly propelled by demand-side stimuli, like lower interest rates, reduced tax rates and enhanced accessibility to credit and financial markets.

However, despite the increases in GDP growth rates, economic growth has proven to be unsuccessful in making significant progress towards eradicating poverty by addressing the unemployment, redistribution and associated socio-economic problems in the economy. Focus 55 builds a case for the persistent prevalence of structural rather than cyclical impediments to employment and consequently shared output growth. Cyclical factors are contributing very little to the current high and unresponsive rates of unemployment. The inability of output growth to translate into significant employment creation and poverty reduction has created a dualistic economy. A “second economy” has consequently emerged with distinctly different features, based on unstable fundamentals and offering limited social protection to those forming part of this economy. The more stable and robust first economy represents the basis of the “era of hope” with high levels of output growth, low inflation and fiscal debt, buoyant financial markets and strong consumption spending.

Policy making in South Africa has to find a new paradigm - one where employment creation and resultant poverty alleviation is not merely accepted as a by-product of economic growth, but where employment creation is viewed as a key accelerator of economic growth. Social development targeted at mobilising and empowering the unemployed needs to constitute the backbone of any growth, employment and redistribution policy. This calls for an integrated strategy on social development to address the imbalances and structural impediments of the past facing the poverty stricken communities. The focus here should be on designing and implementing policies that truly empowers and mobilises this untapped potential of society towards spurring higher levels of future economic growth rather than merely awarding handouts.

The innovative and skilful redesign of existing policies will significantly impact on the returns of social spending on employment and growth. Focus provides empirical evidence that a 10 per cent improvement in the socio-economic environment would increase South Africa’s growth potential to about 6.5 per cent, thereby generating sustainable levels of output and shared income growth. These results clearly highlight the importance of job creation through socio-economic development as a key accelerator of growth.

The proposed policy paradigm is based on an integrated national strategy for social development, where growth initiatives focus more intensively on employment creation. This broad based approach will ensure that any future accelerated income creation is truly “shared” by all levels of society. It also represents the only way to eradicate the growth and poverty trap once and for all and to realise goals envisaged in ASGI-SA.
Accelerated economic growth may not necessarily be sustainable and translate into accelerated employment. Demand-side fiscal and monetary policy intervention aiming at accelerating gross domestic output will be effective in an economic environment without structural constraints impeding the capacity of the economy to absorb everyone willing and able to work. It will also serve to attract sufficient investment capital. In an environment unfettered by structural constraints, this course of action will achieve the goal of higher economic growth without putting pressure on the balance of payments, the exchange rate and domestic inflation. Figure 1 shows that a demand-side based strategy, such as the lowering of taxes and/or interest rates will cause increased demand/spending assuming little or no capacity constraints, which will translate into higher domestic production and subsequent higher shared income for the owners of domestic production factors (labour, capital and land). However, in a scenario where the economy is faced with structural supply-side constraints, domestic production will fail to meet increased demand. In this case, accelerated growth represented by increased domestic expenditure on gross domestic product will not cause an equivalent increase in employment and hence fail to have everyone share in the higher income generated in the economy. The lack of domestic production to meet the increased domestic demand will merely be supplemented by increased imports, which, in turn will impact negatively on the balance of payments, the rand exchange rate and domestic inflation.

Unemployment in an environment subjected to capacity constraints will generate a poverty trap. The limited capacity of an economy to absorb labour will result in high and increasing levels of unemployment with depressing socio-economic and growth implications. Figure 2 indicates that high and rising levels of unemployment will cause a large portion of the population to be subjected to low income levels and poverty, thereby limiting their access to a range of economic and social services and which further diminishes their chances to be absorbed into the economy. The problem is further exacerbated by those who have become discouraged and have lost faith in the ability of the system to generate jobs, resulting in them remaining unemployed “by choice”. In addition, low income and poverty-stricken groups have little financial manoeuvrability and make little to no contribution to savings, which in itself hampers investment, output growth and employment. While adverse socio-economic conditions contribute to the creation of only a limited amount of job opportunities, a high level of relatively unskilled labour supply, supplemented by the high influx of illegal immigrants, further exacerbates the unemployment problem. Unemployment and poverty thereby becomes a self-fulfilling prophecy – unemployment creates a poverty trap which requires innovative intervention targeted at eliminating the significant structural impediments.

Figure 1: A demand-side fuelled growth strategy

<table>
<thead>
<tr>
<th>Spent income</th>
<th>Demand for goods and services</th>
<th>Domestic production</th>
<th>Exports</th>
<th>Imports</th>
<th>Balance of payments deficit</th>
</tr>
</thead>
</table>
Achieving economic growth is required if South Africa is to reach its goal of halving poverty by 2014. This is also illustrated by the high level of income inequality in the country. A new approach to escaping.Whilst the rich are getting richer, the poor is caught in a poverty trap of which they are seemingly unable to perform. But other indicators such as education show no significant improvement over the last decade. The problem is also evidenced by South Africa’s unimpressive development performance. South Africa is ranked 55 in the world with regard to GDP per capita. However, as indicated by figure 3(b), the country’s overall development performance in the UNDP’s Human Development Index is 66 positions lower at 121.

Even more alarming is the downward trend in South Africa’s HDI ranking since 2000. This indicates that little of the new wealth generated in the country contributes to the socio-economic development of the country’s poorest. South Africa’s downward trend in its HDI ranking may be largely attributed to its poor health performance, but.

The decrease in household’s income share is intensifying the already skewed distribution of income in South Africa relative to other emerging economies. A lower Gini index value indicates a better or more equal distribution of income. South Africa’s Gini index value of 0.58, which again highlights the challenge the country faces in achieving a more equitable distribution of income and wealth. High levels of income inequality often lead to social instability and economic inefficiency within a country. The poorest 40 percent of South Africa’s population contributes very little to the GDP, and further highlights the need to mobilise and empower those currently excluded from economic activity.

A lack of opportunity to participate in the accelerated economic activity has caused a lack of shared sense of prosperity by unsustainable demand-side driven growth policies. The most disconcerting about the overall employment rate is that the number of employed people, formal and informal sectors, to the economically active population. The declining trend in this ratio implies that the labour market has not sufficiently absorbed new job-market entrants, causing growth in the economically active population to outstrip the amount of new jobs created, resulting in increased unemployment. The most disconcerting about the overall employment rate is that.

The compensation of employees, or wage income, as a percentage of GDP has declined considerably in recent years. This has happened despite relatively high GDP growth and consumer expenditure growth. Consumers presented with new opportunities to borrow large amounts of money often spend more and inequality more of this potentially productive part of the population needs to be empowered to contribute due to credit and remittances. A value of zero would indicate perfect income equality with every individual sharing income and has exacerbated the extend of inequality in a country. A value of zero would indicate perfect income equality with every individual sharing.
innovative and targeted external interventionist programmes. Extreme poverty associated with poor socio-economic conditions for the larger part of the population demands spending. However, the "second economy", with high and sticky unemployment, unacceptable levels of output growth, low inflation and fiscal debt, buoyant financial markets and strong consumption instability. The stable and healthy "first economy" lays the foundation for an "era of hope" by exhibiting high a dualistic economy – two "sub-economies" with opposing fundamentals, causing potentially for severe instability. The failure of output growth to translate into significant employment creation and poverty reduction has created unresponsive rates of unemployment.

In nature – cyclical factors or the lack of sufficient GDP growth are contributing very little to the current high and 1970s and has reached levels of 25 per cent, but the larger part of the official rate of unemployment is structural. Figure 5(b) not only indicates that structural unemployment in South Africa has been upward trending since the 1970s but also that the decline in the employment rate is not sufficient to counteract this rising trend. In Figure 6(a) we show that the increase in the unemployment rate has been linked to a decrease in the rate of GDP growth in the 1980s, but has not been related to the rapid rise in the unemployment rate since 1995.

Several explanations can be offered for this increase in unemployment, some of which are at least partially associated with the lack of sufficient social support services, which include both social security and education. Lack of mobility, exacerbated by high and increasing transport costs on the back of the rising fuel prices and the lack of infrastructure maintenance, may be measured in terms of the "non-accelerating wage rate of unemployment" (NAWRU). The NAWRU is defined as the unemployment rate below which unemployment cannot fall unless the economy itself begins to contract. In South Africa, this rate was estimated to be around 5% in 1977, but has increased to around 18% in 2001, indicating that any downward movement of the unemployment rate has been linked to a corresponding decrease in GDP growth.

The legacy of apartheid and related to a lack of education and skills and the deteriorating skills and motivation of individual job seekers; etc. Little opportunities for the unemployed to learn-by-doing or on-the-job-training; prolonged periods of unemployment may lead to a deterioration of skills and motivation of individual job seekers; etc. Insufficient access to effective education and skills development opportunities; mismatches between skills supplied and demanded; etc.

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A large part of South Africa's potentially productive population is immobilised and incapacitated – a "sub-economy" with high and sticky structural unemployment, unacceptable levels of output growth, low inflation and fiscal debt, buoyant financial markets and strong consumption instability. The stable and healthy "first economy" lays the foundation for an "era of hope" by exhibiting high a dualistic economy – two "sub-economies" with opposing fundamentals, causing potentially for severe instability. The failure of output growth to translate into significant employment creation and poverty reduction has created unresponsive rates of unemployment.

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...as well as sufficient and quality health services...

While the percentage of government expenditure on health compares favourably with most other developing countries, the availability of medical practitioners and nurses is a concern especially given the prevalence of illnesses such as HIV (Aids), tuberculosis and malaria that affect labour productivity.

In Figure 11(a) - presented later in Focus 55 - it is shown that government expenditure on health as a percentage of total expenditure remained fairly constant between 1983 and 2003 (9.4%) and Figure 7(a) shows that the level of expenditure compares favourably with that in other countries at similar levels of development. However, despite this tendency, the number of medical practitioners available per 100,000 of the population is disproportionately lower. Also, Figure 7(b) shows a downward trend in the numbers of doctors, dentists and nurses over the past 15 years. Given the prevalence of life threatening illnesses and the impact of these illnesses on quality of life and labour productivity, this trend is a cause for concern.

...a stable and crime free environment...

The weakening in the social welfare of a large part of the population and the massive inflow of work seekers from neighbouring countries of which many live in precarious conditions have contributed to an increase in various criminal activities - a concern to investors and entrepreneurs.

Despite figures released by the Commissioner of Police at the end of September 2006 that indicate a marginal decline in some crime-related events, the South African society is still subjected to rampant criminal activity. Of particular concern is the high and increasing level of violent crime associated with organised crime. Figure 8 shows that between 1994/95 and 2003/04, common assault increased from approximately 200,000 cases to more than 270,000 cases while burglary at residential premises increased from about 230,000 to 300,000 cases. In a lead story in Business Day, one of South Africa's leading entrepreneurs said that crime is beginning to affect business negatively. This leads both directly and indirectly, to job losses and social misery.

Figure 7: A socio-economic dimension: Health

a) Public health expenditure and the availability of doctors - a country comparison

b) Growth in the number of medical practitioners and nurses per 100,000 of the population
Those in the lower income groups have limited access to financial markets—a barrier that prevents them from developing entrepreneurial skills and therefore from sharing in the wealth of the economy. Numbers revealed by Finscope South Africa (Figure 9(a)) show that more than 48 per cent of the adult population in South Africa are not using any formal financial service but the number has declined from more than 54 per cent in 2004. The number of banked adults increased sharply from 2005 to 2006 (about 5 per cent) which mirrors the growth in consumer spending over the past year. Of those using financial services provided by the formal financial sector, most use saving/transaction accounts while a relatively large number also have funeral coverage (see Figure 9(b)). Only a limited number of adults use financial services such as insurance policies, pension schemes and mortgage bonds. In October 2004 a special low cost banking scheme was introduced (Mzansi), but its current membership is still limited to about 6 per cent of all adults. On the question in the Finscope survey why people do not bank, most indicated that they simply cannot afford it.

Thus, the poor community in South Africa is largely excluded from the country’s relatively sophisticated financial sector. For them to have access to financial intermediation, innovative informal mechanisms will have to be devised in addition to the formal structures with supplementary financial literacy programs. Microfinance institutions that provide basic credit, saving and a range of financial services to the very poor such as transfer payments, insurance and even pension schemes could be a powerful tool in reducing the poverty problem and allow those who have been locked out of formal financing to be financially sustainable, provided that such services are affordable.

Poverty reduction does not only mean the eradication of extreme poverty but also relative poverty. Housing, education, health, nutrition, and transport infrastructure are key determinants of living standards and therefore of sustainable poverty reduction (see Figure 10(a)). Poorest households are not only likely to be poorer in income terms but also suffer from a wide range of physical and social constraints. The type of dwelling, material used and condition of housing are all important indicators of household welfare. Figure 10(b) shows that of the estimated 12.1 million households in South Africa, approximately 10 million, or 83 per cent, are described as “non-formal” housing. A further 2.5 million households, or 21 per cent of the total, live in structures described as “not suitable for families”. The proportion of households that can access piped water, electricity and other infrastructure and services is shown in Figure 10(c). These statistics are provided by the National Population Council (NIPC), a statistical agency of government. The NIPC is responsible for the compilation of socio-economic data for South Africa’s population.

These statistics show that many of the poorest households have limited access to basic infrastructure and support services. For example, electricity is available to less than 30 per cent of households, piped water to less than 40 per cent, and formal education to less than 20 per cent of children. These deficiencies in infrastructure and services are a major constraint on poverty reduction and on the achievement of the Millennium Development Goals (MDGs).
While accelerated demand-driven economic growth is not translating into significant employment and poverty reduction ("well-being" of all), lack of shared well-being inhibits the growth potential of the economy, thereby exacerbating the problem.

In the preceding analysis it was shown that South Africa's higher economic growth rates have not been effective in significantly lowering unemployment and poverty. Figure 12(a) depicts the flipside of the "growth-to-employment" coin: unemployed South Africans do not share in the income generated by the economy, caused by their inability to participate in significant income-generating economic activity. The economy is therefore underutilising its labour resources – the high and sticky levels of unemployment hamper South Africa's ability to grow sustainable at levels of 6 per cent.

An analysis of South Africa's growth potential by Du Toit (2005) indicates that South Africa's growth potential is limited to approximately 4 per cent. The implication thereof is that if actual GDP growth rates exceed 4 per cent (figure 12(b)), that is, if actual output exceeds the potential of the economy, the economy is "overheated" and production prices and wages will start rising. Given the subsequent impact on consumer prices and the balance of payments, monetary policy will ultimately have to intervene by deflating the economy through increased interest rates. A growth potential of 4 per cent does not imply that the economy can indeed grow at levels exceeding this rate, but actual growth rates in excess of 4 per cent will be unsustainable in the medium and longer run. If growth in "supply" through employment, productivity and investment growth, does not meet the growth in "demand" mainly fuelled by lower tax and interest rates, it will jeopardise the balance of payments position, destabilise the exchange rate and ultimately give rise to increased domestic inflation.

The chart in Figure 12(b) highlights the concept of overheating and underutilisation of resources in the economy. The left side of the chart shows the "growth potential" constrained by lack of shared well-being, where limited growth potential is due to lack of shared income and underutilisation of resources.

The right side of the chart illustrates the "current growth potential and consequences" with excess capacity and the economy being overheated. When actual GDP growth exceeds potential GDP growth, this is considered an "overheat" situation, leading to higher production prices and wages, and ultimately impacting on consumer prices and the balance of payments. Monetary policy may need to intervene by increasing interest rates to deflate the economy and maintain stability.

Figure 11(a) shows the composition of socio-economic expenditure as a percentage of total government expenditure. Since the beginning of the nineties there has been a marginal increase in the share of expenditure on education but a substantial increase in social security (14.4 per cent in 2004 compared to only 6.3 per cent in 1990). However, despite this increase, poverty as measured in terms of individuals eligible for grants has also increased, which could be interpreted as an increase in poverty amongst the poorest (Figure 11(b)). Attempts at reducing poverty through grants exclusively, is overtly unsustainable and should be complemented by an extended and comprehensive socio-economic agenda to develop and enhance human capacity.

When scrutinising the dependency on grants, growth in child support grants tops the list of increases in grants, followed by foster care and care dependency. The actual overall amounts spent on the above-stated grants, are however far below that of old age pensions, disability and child support (R20 billion, R15 billion and R14.5 billion, respectively).
development needs to be pro-active and needs to be perceived as an essential investment in human capital. A traditional reactionist/interventionist/survival strategy aiming at providing security to the most vulnerable. Social development demands a new philosophy regarding the expanded role of social development, which is much broader than the employment creation and become sustainable by contributing to GDP growth through employment creation. This approach also requires that the notion of social spending as an expense item needs to be replaced by significant investment in the development of an untapped and poverty stricken workforce. The population. This calls for a strategy to address the imbalances and structural impediments of the past, however, at fuelling economic growth from the supply side by mobilising and empowering the potentially productive workforce.

Policy making in South Africa has to enter a new paradigm, where employment creation and resultant economic growth is targeted as a key accelerator of economic growth.

However, figure 13(b) represents a new paradigm for the role and contribution, but more specifically the design and implementation of social security practices to ensure the sustainability of these programmes by facilitating external programmes of intervention. In this regard, the current economic conditions are depicted in figure 13(a), which shows the current status quo.

Figure 13: Adjusting the growth strategy

<table>
<thead>
<tr>
<th>Economic Conditions</th>
<th>Employment</th>
<th>Price and Interest Rate Effects</th>
<th>Balance of Payments</th>
<th>Policy Intervention</th>
</tr>
</thead>
<tbody>
<tr>
<td>Demand &gt; Supply</td>
<td>No</td>
<td>Domestic economic Conditions</td>
<td>Demand for goods and services</td>
<td>No</td>
</tr>
<tr>
<td>Demand &lt; Supply</td>
<td>Yes</td>
<td>Domestic economic Conditions</td>
<td>Demand for goods and services</td>
<td>Yes</td>
</tr>
<tr>
<td>Demand = Supply</td>
<td>Neutral</td>
<td>Domestic economic Conditions</td>
<td>Demand for goods and services</td>
<td>Neutral</td>
</tr>
</tbody>
</table>

Policy intervention needs to focus on employment creation and shared well-being through addressing the socio-economic impediments of the past. This also includes the implementation of social security practices to ensure the sustainability of these programmes by facilitating external programmes of intervention.

Figure 14: Model evidence

<table>
<thead>
<tr>
<th>Economic Variables</th>
<th>Percentage Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>GDP growth</td>
<td>0.5%</td>
</tr>
<tr>
<td>Employment</td>
<td>1%</td>
</tr>
<tr>
<td>Inflation</td>
<td>0%</td>
</tr>
<tr>
<td>Productivity</td>
<td>10%</td>
</tr>
<tr>
<td>Output growth</td>
<td>30%</td>
</tr>
<tr>
<td>Income growth</td>
<td>50%</td>
</tr>
</tbody>
</table>

Modelling evidence supports the view that an improvement in the socio-economic environment holds significant benefits for the domestic economy. In the macro-econometric model, a scenario was created assuming a 10 per cent improvement in the socio-economic environment through the computable general equilibrium (CGE) model of the South African economy. Simulations by the research team using both a macro-econometric and a computable general equilibrium (CGE) model of the South African economy indicated positive results.

Improvement in the socio-economic environment significantly contributes to productivity, output and income growth (additional growth of between 4 to 7 per cent). As figure 14(a) shows, an improvement in the socio-economic environment significantly contributes to productivity, output and income growth (additional growth of between 4 to 7 per cent). As figure 14(b) shows, the CGE model shows the sustainability of output and income growth. In the macro-econometric model, a scenario was created assuming a 10 per cent improvement in the socio-economic environment through the inclusion of elements of education, energy, health, crime and various socio-economic index included in the model. The socio-economic index factor in the model, which again supports the sustainability of output and income growth. In the macro-econometric model, a scenario was created assuming a 10 per cent improvement in the socio-economic environment through the inclusion of elements of education, energy, health, crime and various socio-economic index included in the model. The socio-economic index factor in the model, which again supports the sustainability of output and income growth. In the macro-econometric model, a scenario was created assuming a 10 per cent improvement in the socio-economic environment through the inclusion of elements of education, energy, health, crime and various socio-economic index included in the model. The socio-economic index factor in the model, which again supports the sustainability of output and income growth. In the macro-econometric model, a scenario was created assuming a 10 per cent improvement in the socio-economic environment through the inclusion of elements of education, energy, health, crime and various socio-economic index included in the model. The socio-economic index factor in the model, which again supports the sustainability of output and income growth. In the macro-econometric model, a scenario was created assuming a 10 per cent improvement in the socio-economic environment through the inclusion of elements of education, energy, health, crime and various socio-economic index included in the model. The socio-economic index factor in the model, which again supports the sustainability of output and income growth. In the macro-econometric model, a scenario was created assuming a 10 per cent improvement in the socio-economic environment through the inclusion of elements of education, energy, health, crime and various socio-economic index included in the model. The socio-economic index factor in the model, which again supports the sustainability of output and income growth.
This new paradigm demands an integrated national strategy on social development as a key accelerator of employment and shared growth…

As government embarks on the Accelerated and Shared Growth Initiative (ASGI-SA), expectations arise that more jobs will be created. However, based on the preceding analysis, little evidence exists that the employment opportunities created through the normal course of expansionary economic policy will be sufficient. Furthermore, no guarantees exist that the most destitute will share in the growth benefits nor that the most vulnerable will gain opportunities to engage in meaningful and sustainable economic activity. Social development must therefore step in to build human capital with the aim to ensure inclusivity for all.

An integrated social development strategy proposes the expansion of the social safety net, in a sustainable fashion, while deliberate efforts are made by all stakeholders to mobilise beneficiaries to enjoy the dignity and benefits of work and not become dependent on the state. The poor needs to be given the necessary support either to pursue self-employment or to secure the adequate skills and/or other employment in the "first economy".

The conceptual framework (figure 15) is presented in four phases:

1. Strategies need to focus on mobilising and empowering the potentially employable, thereby enabling them to move from poverty and welfare support to gainful employment, which again will support higher, sustainable and shared economic growth.

2. The target needs to be broader than the individual – it needs to consider the households as an economic unit in an attempt to lower the dependency and subsequent impediments or constraints that children and pensioners may pose on the economically active poor.

3. Based on the specific needs and characteristics of the community, which will directly be linked to their geographical location, attempts need to be made to identify socio-economic packages, consisting of nominal wages, social wages, in kind compensation, infrastructure and services needs. This again requires an integrated national strategy from all social partners such as health, education, etc.

4. A "shared" initiative between government (policy), business, labour and civil society, with government providing clear guidelines and incentives in support of clearly defined social development objectives. This initiative should however be sufficiently flexible to allow for industry and society specific interventions.

…with such an investment in the well-being of all breaking the growth and poverty trap to realise the ASGI-SA goals.

Focus 55 proclaims that the impediments on the country's growth and poverty alleviating potential are predominantly supply side in nature. This finding critically affects policy decisions regarding a concerted effort to increase the productive capacity and future growth path of the South African economy, hence effectively translating into employment creation and poverty alleviation.

Notably, the most important challenge for government is a redesign and redirection of its budget allocation priorities away from operational expenses towards investment in human capital and the socio-economic environment. Such a strategic intervention will improve productivity levels, increase the labour absorption capacity of the economy and raise its growth potential to ensure higher sustainable output growth and shared income. A policy change whereby investment in integrated socio-economic development, will act as a key accelerator of shared future economic growth.
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