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THE BASIC HOMEWORK ON BASIC INCOME GRANTS IN SOUTH AFRICA.

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[T]he social state is advantageous to men only if all have a certain amount, and none too much. (Jean-Jacques Rousseau, The Social Contract, 1762)

[1] Introduction.

Certain admirable people are campaigning for the institution of a basic income grant (BIG) in South Africa as the main policy to combat poverty. In a number of respects their arguments are persuasive, but alas, good intentions and good credentials alone are not enough. Prior research is essential before an informed decision is possible concerning the wisdom of such a large and ongoing transfer of resources. That research has not been completed yet, nor initiated in some instances.

It is important to stress that this paper's aim is not to argue substantively against a basic income grant policy. Rather, it sets out to raise the numerous questions judged still outstanding. Although directed at universal grant proposals, many of the uncertainties and knowledge gaps identified apply also to the range of pensions that exist as well as to child support grants. But these are not discussed explicitly.

A number of distinctions need noting at the outset to avoid any misinterpretation. First, it is logically as well as morally consistent for a commentator to be committed to social justice, and therefore to far-reaching actions of redistribution, and yet to doubt that the basic income grant policy is the most efficient way to achieve it. Equity and efficiency are distinct criteria for any policy action, but they may or may not point in the same direction in the formation of policy. It is a commonplace observation that "Public spending should promote efficiency (by correcting for various market failures) and equity (by improving the distribution of economic welfare)". (Van de Walle 1995: 1) An action scoring high on equity may nonetheless be seriously inefficient. This is the case with universal income grants.

Secondly, putting resources into the hands of the poor efficiently is an achievement, but it is not enough by itself. The kind of *use* made of such resources by the poor raises a set of key issues integral to effective anti-poverty policies, as argued in the following sections of the paper.

Thirdly, if one does question the efficiency of such a policy, using a criterion of maximum welfare per unit of resources (however measured), there is no obligation on the sceptic to propose immediately a superior alternative. In the current state of research on viable redistribution strategies in South Africa, it is not realistic to expect critics of a proposed initiative to have one or other substitute policies up their sleeves. But this is what income grant advocates demand.

Finally, because policy innovations of this size tend to cause changes in the perceptions and behaviour of economic decision-takers, their full effects will take a number of years to emerge. This introduces unavoidable uncertainty. Thus the decision to go ahead with a policy or not must distinguish immediate from ultimate effects, despite the serious information problems involved. Recognising constraints like this are essential for clarity of thinking.

A central argument of this paper is that the policies and institutions that will enable escape from poverty, and thereby diminish the size of the national poverty problem, will be more demanding of design and implementation than are regular income transfers to the poor. The latter are attractive because of their operational simplicity. But they are ameliorative more than curative in effect, we shall argue. This is their inherent weakness.

We need reminding that to arrive at correct policies is a discovery process. Interest groups and government have to learn about the underlying problems, like the kinds of new institutions required, the desired behaviour necessary to be attracted or coaxed from targeted beneficiaries, and the alternative policies that are realistic and rival to what is under consideration. The latter are a potential measure of opportunity cost.

[2] Investment, growth and poverty.

How do people escape from poverty? In a multiplicity of ways, but common to all these ways is the *investment* of resources in the present in order to reap a flow of additional returns in the future. Given the right institutions and behavioural responses, the outcome that results from this use is positive income growth. The alternative use of resources is *consumption* which stimulates growth only if there is idle productive capacity. This distinction between uses is basic in all economic appraisal.

The advocates of an income grant tend to assume that additional units of a resource made available to a poor individual will be *equally* effective in relieving that person’s deprivation no matter how they are used. This is not true at all. The consumption use of resources makes poverty easier to bear in the present because it increases personal welfare with immediate effect. Food, fuel, clothing, shelter, health-care and so on decrease the current burden of poverty directly and rapidly. Thus it is easy to predict that additional resources will be spent disproportionately on these commodities by the poor (and in households defined as poor headed by women, a higher proportion is devoted to *both* consumption and investment used by children: Lund 1993; Duflo 2003).

Surprisingly, the causal links between investment, growth and decline in the incidence and depth of poverty are not investigated by the proponents of basic income grants in South Africa. To view income grant proposals in an investment perspective, two channels of investment amongst a possible number are discussed here. These are *aggregate investment*, the economy-wide actions by the private and public sectors to increase the physical and human capacity to produce; and *self-investment* by economically active individuals seeking higher personal income in the future. These two kinds of investment are complementary. A higher rate of aggregate investment raises the probability of success in self-investment, although with a time lag.

Ultimately when self-investment is sufficient and appropriate, for some individuals at the bottom of the income scale their new capacity to produce enables a level of income and consumption high enough for them to escape the state of poverty. If this happens successively for enough people, we have a growth process in which the average income per head of the economically active population rises, so that the bottom ranks of the distribution of income are pulled up over time, enabling their exit from poverty.

A distinction underlying the argument in this paper is between *alleviating* poverty and *overcoming* or exiting from poverty. Escaping from poverty entails relief from poverty but not vice versa. This first category of action aims at amelioration. It provides resources to raise the current consumption levels of poor individuals and households. Whereas the second kind of action changes the material status of those defined as poor. By devoting a proportion of any additional resources coming their way to investment, poor persons raise their productivity as economic agents. Eventually they achieve self-sufficiency; that is, in the limit they cease being poor.

Acts of self-investment include additional education and training for adults and for children; preventative and curative health care; the erection of buildings or other structures dedicated to produce output for subsistence or for sale to others; buying or making plant and equipment like machines and tools; accumulating working capital by purchasing commodities for re-sale, or using such capital for adding value in production by stocking up on raw materials, semi-processed goods or work-in-progress as inputs into final products for generating income by disposal in the market.

For the present purpose, distinctions between *final* consumption items, like food, and *intermediate* items more durable, like houses, furniture and appliances that yield consumption services over time can be ignored. This intermediate category shares the time dimension with investment but not its most important characteristic, which is permanent change in the capacity to produce. The key point is thus that the resource use alternative to consumption, the investment of acquired resources, raises an individual's capacity for self-support, known as his or her *capability*. This concept, made prominent by Sen (1992, 1995) and others (Anderson 1999), is discussed further in the section on human rights.

Amongst economists this investment perspective is conventional.

> 'For the longer run [of an economy], if growth is what we want, the goal of public policy should be to create the institutions and incentives that will divert production from consumption to investment in the broadest sense: public and private investment, human and physical investment, basic and applied research. As for inequality…at a time when impersonal economic forces seem to be pushing by themselves in the direction of widening inequality, for public policy to be doing the same thing is not a technical mistake but a moral disaster.' (Solow 2003: 51)

> 'Wide access to a career and a livelihood in society's mainstream economy is again a subject of discussion…Great value is placed on the opportunity of working-age people [through self-investment] to obtain rewarding work in the formal economy and to earn enough in such jobs to be self-sufficient – twin conditions for what is often termed *economic inclusion*…Rewarding work here refers mainly to the job satisfaction provided by a job's challenges and the personal growth from the resulting interactions with others. Self-sufficiency here means that workers earn enough for a decent living by society's standards and possibly some involvement in community life – not just a wage sufficient for subsistence.' (Phelps 2000: 86, 104)

> 'There is broad consensus that expansion in the skills, knowledge, and capacities of individuals – increasing human capital – is a key element in developing countries' economic progress and in raising their living standards.' (Pritchett & Filmer 1999: 223)

Thus a key contention of the present paper is that investment is more important for overcoming poverty than consumption, and this is ignored in the BIG proposals. Although a truism, this distinction is of particular importance when these alternative uses are viewed in a lengthened time perspective. By "importance" in this context is meant efficacy in lifting the welfare levels of the poor individual and of society as a whole out of poverty through deliberate policy action.

Certain advocates of a universal grant policy in South Africa have training in economics and are certainly aware of this distinction. But their overwhelming emphasis on the desirable characteristics of a grant designed as unconditional, universally accessible and amenable to unconstrained choice in its use by the individual recipient perhaps obscures the crucial difference between investment uses and consumption uses of resources in the hands of the poor.

Understanding the key role of investment in growth and diminishment of poverty is helped by the standard framework for formalising ideas about the causes of economic growth. Starting with what are termed proximate *determinants* of growth, rising individual income measured by convention as GDP per person is deemed to be the result of one or all of the following four processes. All stem from *net* increases in the flow of investment.

- *I.* *Capital broadening* comprises the accumulation of new capital instruments for use in production by *new* members entering the labour force or self-employment, such as tools and equipment, new work stations, raw materials, work-in-progress stocks, and so on.
- *II.* *Capital-deepening* is *additional* physical capital like plant and machinery applied to an average unit of output by the average worker already active in the labour force.
- *III.* *Human capital accumulation* is education, skills training, on-the-job learning, lengthened work experience, higher nutrition levels, and effective health services for economically active individuals.
- *IV.* *Productivity growth* is the rise in output per unit of all the identified inputs in production, namely, physical capital, labour, natural resources, and energy. Higher productivity is transmitted usually by investment in new techniques of production. Often for calculation the inputs are weighted, eg. by their market prices, efficiency prices or imputed values, to obtain a single figure for the ratio between inputs and outputs by industry or type of commodity production (called *total factor productivity*).

In principle, self-investment by a poor individual can raise their own output in a number of ways. In practice, positive growth initiated by individuals takes place mainly by additional equipment entering production alongside newly active labour, or by the accumulation of one or other form of additional human capital. Broadly these are more education, learning-by-doing, and skills training. But it is difficult and rare for one person acting alone to do so through the successful introduction of a new technique of production.

Net investment is the increment in the flow of invested resources over and above what is required for the replacement of capital items at the end of their economic lives. That end is reached when an asset has depreciated in value to zero. An act of net investment can result from a transfer of resources (as distinct from the creation of additional resources) where *use* of those resources changes from consumption to investment in the hands of the new owner. This is the perspective to be kept in mind when devising methods and strategies for the poor to escape rather than alleviate their poverty.

Thus, the thrust of this section of the paper is to argue that the policies most needed for diminishing poverty are that kind which encourage the investment use by poor individuals of resources transferred to them by the state or by private philanthropy. Such use will require a deliberate bias towards investment. Plausible ways are the transfer of resources as merit goods, like longer compulsory education higher in quality; or by constructing infrastructure for making new economic activity profitable; or by public works programmes with a central skills training component to make participant workers more attractive in the labour market; or by subsidising new jobs in selected industries. The expanded supply of merit goods as a strategy alternative to income grants is discussed in the next section.

The second kind of investment singled out here, poor people investing in themselves to enlarge the range of economic choices open to them, is more likely to occur in practice given a suitable decision environment, the right signals, and the perceptions of likely positive returns. For instance, the higher productivity and matching earnings that result from net increases in education and skills acquisition persist over working lifetimes for individuals irrespective of characteristics like gender. This is not invariably true but it is so for the vast majority of the economically active.

A rate of return to such an investment of resources can be estimated by comparing its cost against the resulting flow of benefits projected to take place over a longer period. The private individual is interested mainly in the *private* gains – higher income, job stability, enhanced social status – but it is widely accepted that such investment also generates *social* benefits in the form of spillovers that are unpriced. These include outcomes like productivity improvements in fellow workers, a rise in the feasibility of new technology becoming profitable, the improved health status of family members, a lowering of birth rates, and a range of other external effects on welfare that are positive.

Recent work on explanations of economic growth has examined the so-called *deeper* determinants. These have drawn research attention because of continuing anomalies in the empirical and historical record, which do not yield unambiguous lessons for policy actions aimed at accelerating growth. For example, in the early decades of the 20th century, Argentina and Australia were economies generating the highest average per capita incomes for their populations. But subsequently they slipped down in the international rankings by income levels despite possessing favourable values of the proximate determinants of growth, ie. I to IV as described above. Similarly, there are national economies in the contemporary world that meet these proximate criteria for expansion, and yet exhibit an unimpressive growth record; instances are India, a range of Latin American economies and numerous oil producers like Venezuela and Nigeria.

The following three "deeper determinants" are subjects of an expanding analytical literature that aims to explain these anomalies. The role of institutions in encouraging or retarding economic growth in an economy is receiving particularly close attention, although generalisable conclusions are still elusive.

> '*Geography* relates to the advantages and disadvantages posed by a country's physical location (latitude, proximity to navigable waters, climate, and so on). *Integration* relates to market size, and the benefits (as well as costs) of participation in international trade in goods, services, capital, and possibly labor. *Institutions* refer to the quality of formal and informal socio-political arrangements – ranging from the legal system to broader political institutions – that play an important role in promoting or hindering economic performance.' (Rodrik 2003: 4-5, emphasis added)

We have argued that the distinction between investment and consumption when applied to poverty reduction is essential for clarity of thinking about strategies. Transferring resources with the aim of more self-sustaining outcomes for poor individuals can be carried out in more than one way. So to devise appropriate policies we need to understand how and under what circumstances such efforts can be successful, leading to questions like the following.

⇨ How effective are *particular* kinds of investment uses of redistributed resources relative to each other (in education, training, working capital, construction of fixed productive capacity) in enabling the individual to escape poverty? Can that rate of escape be accelerated by the right state actions?

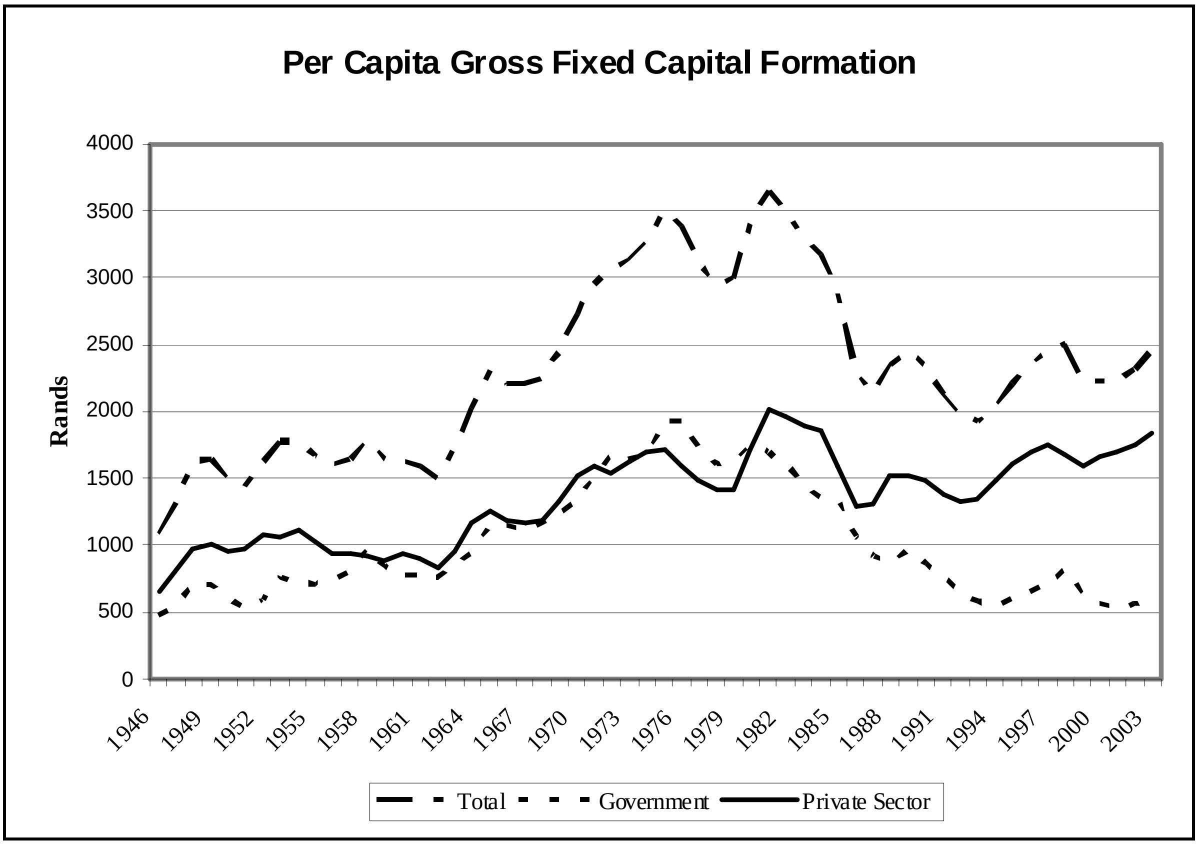
- Appropriate redistribution has been shown to contribute to "permanent effects on aggregate output and growth?" (Aghion *et al,* 1999: 1627). But again we need to ask what institutions and policies for redistributive transfers are most efficient in stimulating the growth process?
- The state's traditional role in fostering growth has been the provision of public goods (like administration and law and order services), of infrastructure (like communications), as well as expanded human capital capacity (like education and training). This puts in place the preconditions for future growth, as well as a stimulus to current growth under certain macroeconomic conditions.
- Historically the *direct* redistribution of resource endowments aimed at enabling individuals to escape poverty included methods like land reform, compulsory education, the founding of state-owned enterprises (SOEs) with preferential labour hiring, the nationalisation of strategic sectors, and the financing of public works for temporary job creation intended to result in permanent employment for a sizeable proportion of those hired.

These issues extend beyond the confines of this paper. For the present only the distinction between the consumption and investment uses of resources when made available to the poor is emphasised. But this distinction is a highly strategic one, particularly so given the dismal performance of the South African economy in generating investment in recent decades. Figure 1 shows this clearly. The first panel shows the declining ratio of *gross* investment to GDP since 1980; and the second panel, the same decline over the same period in the three components of *per capita* investment. These ratios reflect movements over time in both numerators and denominators.

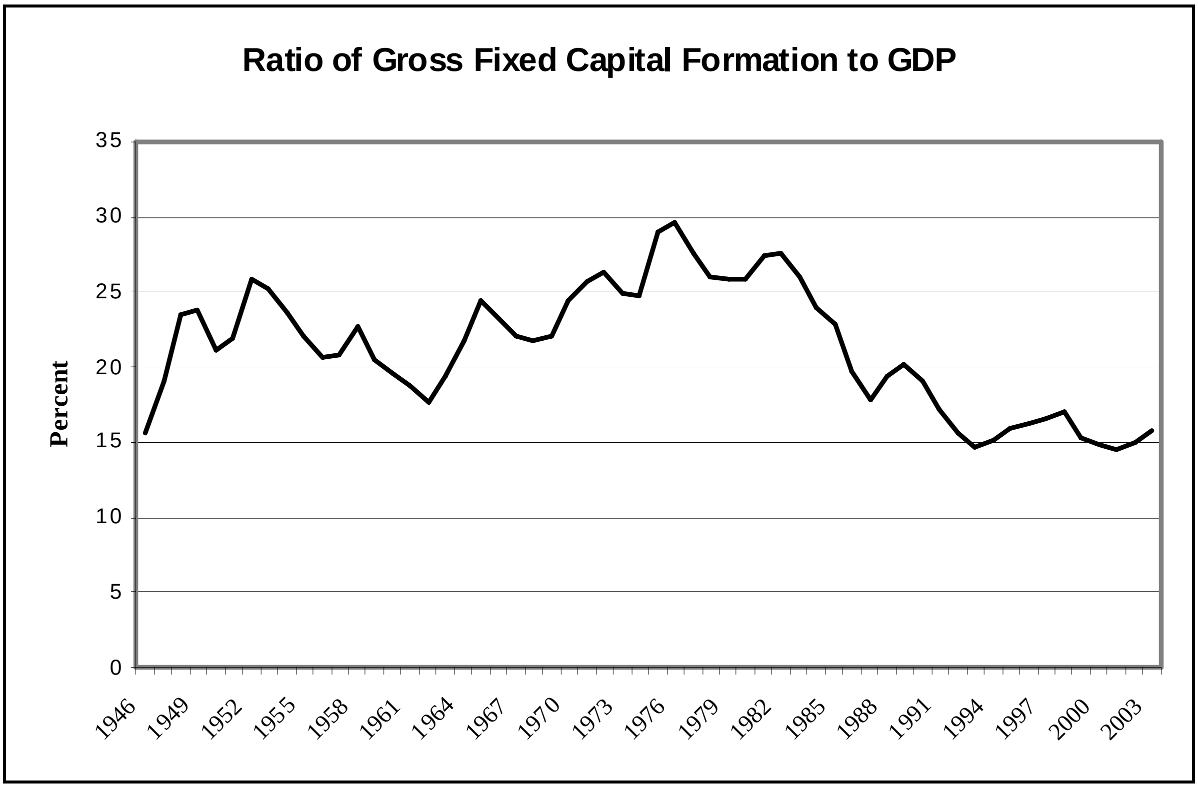
Note that this aggregate data does not show directly what this paper terms *self-investment*. But in the real economy a causal link between the two kinds of investment (aggregate and personal) exists, insofar as relatively low aggregate investment creates a decision climate that is not conducive to profitable self-investment by individuals. It is also noteworthy that *public* investment, the component that has declined in South Africa the most relative to population, has gone down similarly in certain other developing economies, for instance in Latin America over 20 and more years (Hemming & Ter-Minassian 2004). But we are not able to identify common causes affecting a set of middle-income economies including South Africa.

In practice, with the hypothetical institution of an income grant, some fraction of the new income will be devoted to self-investment by a fraction of recipients. That happens with existing transfer payments in South Africa (Lund 1993; Case & Deaton 1998; Duflo 2003). But the relevant case to be argued is whether that invested proportion of grant income would be the highest possible for the poor individual and for society under all circumstances open to policy influence? Put another way, can poor people be induced to invest *more* of their incremental income in pursuit of their long-run desire to escape from poverty? Can methods of redistribution alternative to a universal grant raise that proportion? These questions are not satisfactorily examined by the advocates of basic income grants.

Figure 1



Source: SA Reserve Bank, calculated by E. Blecher.



Source: SA Reserve Bank, calculated by E. Blecher.

In summary, by design a basic income grant is not a component of an economic growth strategy. It is thus not likely to be an effective tool for poverty elimination. It is in conception a means of poverty relief, ignoring for the moment its other deficiencies raised in the remainder of this paper. That is its key limitation from an investment perspective on poverty.

[3] Building a welfare state through merit goods rather than universal grants.

Is there a persuasive argument for ranking cash transfers in the national budget above the free provision of merit goods like good quality education, health care and housing provision in allocations for the poor? Proponents of a basic income grant either do not pose this question explicitly, or they take this ranked preference for cash to be so clear-cut and unproblematic that no reasoned persuasion is called for. That is far from being the case.

South Africa does not possess a welfare state. We have individual features of such a system that qualify for the title. Citizens receive a limited number of merit goods, like compulsory schooling up to Grade 9, old age pensions, child support grants up to age 12, disability grants, free medical care for children under age 6, and the like. The jewel in the welfare crown remains the state pension, instituted ironically enough under the old regime and therefore subject to means testing and differentiation by race up until the 1990s. Means testing still remains, but the pension's international uniqueness in a country where average income per capita is only middling has been widely noted (Lund 1993; Case & Deaton 1998; Seekings 2002).

A range of merit goods is one defining feature of a welfare state. In discussing the pros and cons of an income grant as well as the policy alternatives to it, the supply of such goods is the most important feature of any such state we shall argue. But assistance to the poor is not that system's only characteristic institution and programme. "The Welfare State is designed to provide a sense of security to all, not just to focus on those below the poverty line" (Atkinson 1995A: 1).

Also, constructors of welfare states do not necessarily share a common philosophical rationale. For instance, "luck egalitarians…take the fundamental injustice [in society] to be the natural inequality in the distribution of luck [and] view the welfare state as a giant insurance company that insures its citizens against all forms of bad brute luck" (Anderson 1999: 289, 292). This characterisation is true but it leaves too little scope for deliberate redistribution, the underlying drive behind developments in the second half of the 20th century.

In welfare states now considered mature, the institutional innovations that emerged after the 1930s depression and WW II were wide-ranging. They included social security in the form of a variety of grants in cash or kind, all conditional not universal; unemployment compensation; nationalisation or public ownership of activities identified as strategic for social welfare, like communications and electricity; deposit insurance against bank failure; expanded public sector infrastructure; and legislation providing trade unions with specified legal immunities for their actions, like strikes that can cause private losses to management, shareholders and other workers that would otherwise be legally actionable.

An account of the welfare state's history is not called for, although it is now prominently in the news with the Bush administration's stated intention to alter drastically US welfare institutions like Social Security. But certain features of its origins must be noted in order to provide a context for the present discussion of merit goods.

- First, in the past the political motivation for safety nets and poverty alleviation was not uniformly the result of democratic institutions, nor was it a simple liberal impulse. For instance, Bismarck is credited with the first German move towards social security provision in the 1870s as a tactic to head off more radical demands by organised labour and other non-property owning classes.
- Second, in European countries like the UK the commencing assumption underlying welfare policies early in the 20th century was that much poverty was accidental for the individual or family. It was caused by unexpected contingencies which by and large could be insured against.
- Third, later in the depression-prone years of the twenties and thirties the realization grew that poverty "could be the result not only of social accident, but also of more fundamental social and economic factors" (Helm 1989: 29). This called for permanent not contingency provision for alleviating social distress in the state's budget allocation.
- Fourth, because certain individuals provided for themselves less than was prudent for countering negative outcomes over their lifetimes, the rationale of "preference failure" to compensate for the consequences of such flawed choices was accepted early on by architects of the welfare state like Beveridge and his early 20th century contemporaries. Paternalism by the state became an entrenched principle, and only much later was it contested by libertarians on philosophical grounds and by other critics on the premise that state decisions instead of individual choices caused extra waste and inefficiency. We say more about this in section [5] on the normative dimensions of income grants.

The range of merit goods supplied by the South African state, their magnitude per recipient, and their coverage or availability to individuals and families are considerably lower than what is provided to the population in major industrial countries, with their average per capita income levels six to ten times higher (World Bank 2004). This has to be a qualitative judgement because directly comparable data on merit good coverage and expenditure is not readily available. There are, for example, definitional uncertainties as well as variation in conditionality, that is, the application of eligibility criteria concerning which merit goods are accessible to which individuals and groups. This makes quantitative comparison risky. But for the present purpose this judgement is unlikely to be questioned seriously.

If, as seems to be the case, in mature welfare states a universal cash grant is accorded *lower* status as a budget claim than more spending on the merit goods identified as inadequate or missing in those states, then the arguments justifying that policy ranking must hold even more strongly where the supply of merit goods is thinner. There are no serious suggestions in policy-making environments that outright grants be instituted above merit goods in these industrial countries. So one infers the same is true of South Africa at present, an inference reinforced by public statements from the Minister of Finance. This proposition – the ranking of merit goods over outright grants - is the main thrust of the present section of the paper. It can be illustrated by reference to the Swedish example, arguably the most thorough-going welfare state in existence.

What is a merit good? Definitions differ in the detail to an extent, but the core idea is clear enough.

- ⇨ Merit goods are those to which citizens [in a welfare state] are widely believed to have some right, irrespective of their financial situation, or those to which it is thought that access should be more equal than is appropriate for goods in general. (Holtham & Kay 1994: 5)
- ⇨ We label a good or service a "merit good" when (1) we decide that everyone who is in a position to utilize it should have access to it and (2) when, in the absence of government provision, there are people who would not or could not acquire it on their own. (Bergmann 2004: 109)

In no welfare state are all merit goods that can be realistically conceived freely available from the state. The obvious reasons for the shortfalls are their cost, uneven concentrations of political power influencing allocation decisions, challenging delivery institutions, and the difficult to measure and prescribe but vital dimension of quality in merit goods. The following list of unfulfilled merit goods in the Swedish case provides a guide to the items still missing in current South African efforts to build a welfare state (Bergmann 2004: 109-112).

- ⇨ *Schooling*. All political groupings, conservatives as well as social democrats and liberals, recognise this as the most important merit good. "The best estimates for developing countries…find that each additional year of schooling is associated with a 6-10 percent increase in earnings. This evidence appears robust across both methods and locations…[suggesting] that investment in education can be used to attack poverty both by encouraging economic growth and as a method of redistribution to the poor" (Besley & Burgess 2003: 14).

A major problem in all national systems of education is quality differences in what is on offer in primary and secondary schools. "Low-quality schooling and high-quality schooling are really two different services [and] in the United States…quality-enhancing reforms might well require a doubling of current education budgets" (Bergmann 2004: 110). At the tertiary education level a case can be mounted also for subsidizing the private costs of certain groups. But this is a weaker claim on equity grounds because university and other graduates eventually end up in the top echelons of the national income profile. Certain South African student groups are loathe to acknowledge the low priority of a demand on the public purse for free tertiary education, probably because of apartheid era politicisation of access to higher education.

- ⇨ *Health care*. Most welfare states provide some items of health care on unconditional or universal terms. But again there are quality problems, permanent rationing, and a temptation to let the value of budgetary allocations erode, as in South Africa's teaching hospitals and the UK's National Health Service in recent decades.

- ⇨ *Childcare*. In all welfare states this service, encompassing pre-schooling, after-school care and recreation programmes, is particularly vital for single-parent households. But it tends to be low-quality, often from private and profit-seeking suppliers, and yet a relatively expensive item in the family budgets of the poor.

- ⇨ *Mental health care*. In certain welfare states, homelessness and therefore poverty is associated with mental illness. Under the same heading are the disabilities caused by addictive behaviour from the abuse of alcohol, drugs and gambling facilities. A compelling case can be mounted for state-provided therapeutic services and dedicated institutions superior in quality to those in existence.

- ⇨ *Decent housing*. Partial state funded programmes exist in certain developed countries. In the US for instance, the principle is that eligible poor families should not have to spend more than 30 percent of their income for housing, the balance being paid for by vouchers. "But the program is not an entitlement so limited appropriations [of funding] allow only a small percentage of families eligible for this kind of aid to receive subsidies" (Bergmann: 111). Currently the Bush administration is attempting to place a financing cap on this programme labelled Section 8 (*New York Times*, 10/5/04).

- *Public sector transportation*. Like housing and tertiary education subsidies, merit good status for transport is much more contentious than for other listed items. Nation-specific factors – history and culture – play powerful roles in the legitimacy of subsidies versus privatisation. For example, the first Thatcher-led government in the UK was determined to abolish state inputs into the railways, and this policy stance has endured under recent Labour administrations. By contrast, the French national rail network remains highly subsidized, and its performance is a source of national pride. The rationale for subsidizing certain forms of transportation rests on grounds of positive spillover effects (or positive externalities), in addition to its merit good status. "Greater provision [of public transport subsidies] would slow global warming, reduce sprawl, preserve green spaces, save energy, and revitalize city centers" (Ibid: 112).

- *Social work services*. The arguments for either public subsidy or direct provision of this merit good are strongest in urbanised and socially differentiated communities. Child protection services, youth and released prisoner programmes, family counselling on conflicts and financial problems, along with the wide range of rehabilitation efforts in existing welfare states are the major components here.

This is an ambitious listing, so the categorizing of certain of these items as having merit status is bound to be contentious. But that problem is secondary here. For the purpose of this section of the paper – to illustrate alternative policy action to a basic grant - it is sufficient to concentrate attention on merit goods like schooling, health, and perhaps child-care and mental health services for which there is wide support. In most countries as already remarked, such support transcends differing value judgements and political orientations. Yet enough has been said to pose the following analytical choice clearly for the protagonist of basic income grants.

- *Either a convincing argument has to be mounted that* ***both*** *cash grants and additional merit goods have to come out of the state budget for policies on poverty to be effective.*

- *Or alternatively, a convincing case must be constructed for ranking grants in social welfare terms* ***higher*** *than the merit goods still needed by the poor, and therefore that allocations must be shifted within the budget to achieve this.*

There is ambiguous evidence from published sources that South African proponents of a regular income grant have advocated these policies or even posed these questions explicitly. In public statements the underlying presumption seems to be that a universal grant, if instituted, will be an "add-on" to existing social welfare policies, like the state pension and the range of conditional grants that have evolved in recent decades. But the further question, whether instituting such grants is advocated alongside an *expansion* of merit good provision, is also not posed clearly. From a resource point of view this would be even more radically ambitious. Financing the grants, their affordability in a wide sense, and the implications of additional taxation are the subjects of later sections of this paper.

[4] Economic and social rights and a basic income grant.

Investment has *instrumental* value because it is an essential means for the individual's escape from poverty, an ultimate goal for every poor person. But once we adopt a human rights perspective, any realization of a right by an individual through whatever means has an additional dimension of importance. It achieves one or more components of what is *intrinsic* to being human. Self-investment therefore has this additional dimension of value for every human being who is poor.

We need to take this concept of intrinsic value further back, to the set of moral ideals that provide the philosophical basis for the notion of a human right. Applied to the present question about the merits of a guaranteed income grant to benefit the poor, it is very clear that the moral goals that underlie human rights are quite incompatible with a state of poverty. These goals range over individual autonomy, self-sufficiency, dignity, self-realization, and freely chosen participation in a community of equals, or formulated as "free and equal citizenship" (Pateman 2004: 24). Extended characterisations of the ethical basis of rights are possible and available in the large rights literature. But this description illustrates the point well enough.

Poor children inherit their poverty status and their unequal opportunities from their poor parents. Such perpetuation of states of inequality and poverty is *not* compatible with human rights, particularly not social and economic rights (these perpetuation mechanisms can also, and often do, hinder the attainment of first generation rights that are political and civil in nature). It follows that on its own, a redistribution of current income flows within society towards the poor by itself provides no assurance of countering the transmission of personal deprivation between generations. Such payments are ameliorative but not necessarily curative, we have argued already.

So applied to the present discussion, the simple transfer of income alone, even when regular and persistent like a cash grant, is not likely to advance the goal of human rights fulfilment adequately. Rather, meeting such rights requires "expanding the opportunity sets of the poor", and this is effectively possible only with the investment use of the resources put into the hands of the individuals and households designated as poor (Bourguignon, Ferreira & Menendez 2003: 2).

This is an untested judgement. To test it will require accurate micro-level data on the spending habits of poor individuals and households. Then some extrapolation of the marginal spending decisions on a BIG, as a hypothetical increment of income in the hands of the designated poor, may be possible. But that is a future research task.

Interestingly, prominent international institutions in the development field now manifest a wider interpretation of their goals even when such goals are not tied explicitly to the fulfilment of human rights.

> 'In the past two decades we [the World Bank] have begun to look beyond incomes to health and education. Indeed, we now look beyond the basic elements of human well-being and see freedom as part of development. We see the state not as a substitute for the market, but as a critical complement…government action is crucial in enabling people to participate in the growth process and to take advantage of economic opportunities' (Stern 2003: xiii).

A second reason why cash transfers will not by themselves meet the economic and social rights clauses in our constitution, is because the size of the grant proposed is too low by itself to provide autonomy and self-sufficiency to the impoverished individual in a middle income country like South Africa. In richer welfare states this outcome may not be the case if the political process yields citizen support for grants high enough to meet the minimum amount of personal resources required for the individual to live on it (Pateman 2004). What that level is tends to remain an unsettled matter.

Further, universal monetary payments of this kind and size do not exist anywhere at the present time, an independent reason for caution discussed later in this paper (Goodin & Rein 2003: 777). In the South African case specifically, the high proportion of the population who are poor can make the level of income provision per head required for meeting all constitutional rights *fully* a target impossible in opportunity cost terms. Such a high required level could generate distributive conflicts and negative growth projections that endanger the stability of the economy as well as the political process. Like other crucial questions at this stage of the research work, this is a matter of judgement not one drawn from relevant evidence.

The literature here is extensive, so drawing attention to selected human rights approaches that provide a broader perspective on escape from a condition of poverty should clarify the present argument. These perspectives bear directly on the nature and limitations of an income grant as an anti-poverty measure. First, Rawls introduced the notion of "primary goods [defined as] basic rights and liberties, opportunities, income and wealth, and the social bases of self-respect" (Rawls 1999: 13). Primary goods have intrinsic significance for the status of every individual as human. In particular, "the social bases of self-respect" relates to the theme of this paper insofar as it widens understanding of what overcoming poverty means. Viewed thus, the proposals for instituting a universal income grant place an excessively narrow interpretation on the prerequisites for a human life.

Second, will the universal character of an income grant be a sufficient condition to avoid the emergence of a stigma on those individuals and households surviving on such grants, with universality intended as non-discriminatory? Again this is a before-the-fact judgement difficult to make with confidence. But the point is that if a stigma does emerge from differentiation between poor grant receivers and rich taxed receivers – through the 100% taxation of grant income projected as a form of after-the-fact means-testing - then this mode of helping the poor by grants would not advance but rather obstruct the attainment of a range of social and economic rights. Ironically, this would be a policy-initiated obstacle to the serious implementation of the Bill of Rights in the South African constitution that aims to elevate equality as a moral goal.

Third, an appeal to the general social interest will also not be a valid argument for a basic grant if we take the pursuit of human rights seriously. To weigh community advantage, presuming it for argument's sake to be demonstrably supported by a policy instrument like a universal cash payment, against the individual rights of a moral being, and to rule in favour of such a policy is to commit a logical error or category mistake. It would be to misunderstand the concept of a human right. Either one accepts that concept with all its implications or one does not. “Rights are trumps” in the well-known phrase coined by Dworkin (1978), meaning that individual right fulfilment is morally more important than raising social welfare. By way of illustration, Rawls starts his original argument about justice boldly:

> ‘Each person possesses an inviolability founded on justice that even the welfare of society as a whole cannot override…Therefore…the rights secured by justice are not subject to political bargaining or to the calculus of social interests’ (Rawls 1971: 3-4).

A related approach to poverty within the framework of rights objectives uses the idea of human *capability*. It is associated with the work of Sen and others contending that freedom and equality are constituents of individual well-being, to be treated as such explicitly in assessing poverty and in devising policies of amelioration. The initial contention is that human beings by definition, in their conception of themselves and that of others, have values and aspirations as well as needs. Being free from poverty, and therefore escaping from it if poor, must satisfy these expanded criteria *in addition* to achieving the material standards measured conventionally in money, in kind, or in access to the resources required to reach those standards through production.

Recent literature has formalised these notions in order to quantify poverty by the expanded concept of “capabilities-to-generate-minimum-necessary-income”. Those individuals at the bottom of the income distribution by this applied measure are taken to be the most needy. The new indicator in one interesting approach is labelled *self-reliant poverty* (Haveman & Beshadker 2001). It brings out as a constant reminder [1] that the poor, intrinsically and by operational definition, are unable to be economically independent, and [2] that the distinction between transitory and permanent capabilities is essential for analysing the difference between relief of poverty and escape from poverty.

When these new estimates are compared to those derived by the official US measure of “income poverty”, several conclusions are prominent. First, self-reliant poverty has grown “more rapidly and more steadily”. Second, the highest self-reliant levels of poverty are concentrated in the groups for long thought of as the most vulnerable: “Blacks, Hispanics, single parent families with children, and those with low levels of schooling”. Third, somewhat paradoxically, in recent times these conventionally poor groups have experienced *lower* rates of increase in self-reliant poverty than those conventionally less vulnerable and relatively secure economically: families headed by men, white families, with relatively high levels of schooling, and "married-couple families with children". The conclusion drawn is unsurprising for the United States with its large working poor population. But, more importantly for us, are the policy implications drawn for the US the same ones we should draw in the South African search for solutions, namely choosing more investment over more income transfers?

> The large and rapidly growing number of people who are unable to be self-reliant is discouraging for a society that prides itself on providing the opportunity for individuals to prosper and thrive by working hard, and playing by the rules…If income support measures are ruled out as eroding work effort, encouraging dependence, and fostering the growth of income poverty, what policy measures are available to reduce Self-Reliant poverty? Essentially, two general policy strategies are available:
>
> ⇨ Increasing the level of education, training, skills, and other human capital characteristics of those at the bottom of the capability distribution.
>
> ⇨ Increasing the "return" that the least capable members of society receive on the use of their human capital (Haveman & Bershadker 2001: 357).

Two further quotations bring out what is distinctive in this way of thinking, and make clear why acts of investment to achieve the human rights goals of autonomy and self-sufficiency are essential to that end.

> 'To use a medieval distinction, we are not only *patients*, whose needs demand attention, but also *agents*, whose freedom to decide what to value and how to pursue it can extend far beyond the fulfilment of our needs' (Sen 2004: 10).

> 'To be capable of functioning as a human being requires effective access to the means of sustaining one's biological existence – food, shelter, clothing, medical care – and access to the basic conditions of human agency – knowledge of one's circumstances and options, the ability to deliberate about means and ends, the psychological conditions of autonomy, including the self-confidence to think and judge for oneself, freedom of thought and movement' (Anderson 1999: 317-8).

Would regular payment of a basic grant at the low level advocated in South Africa advance these human rights of a poor individual? It would, but only in the weak and generic sense that any extra command over resources promotes that person's potential capability for meeting rights goals. But it would certainly *not* provide the rationale that organisations in advanced welfare states like BIEN (Basic Income European Network) claim to be most convincing for its introduction, namely that an income grant will provide a permanent guarantee of freedom from poverty.

That claim cannot be sustained here in our social and economic situation, which makes it a major difference and perhaps weakness of BIG campaigns in developing countries like South Africa when viewed in a rights perspective. As a policy initiative that demands a large mobilisation of resources even at the low level of R100 per person per month, its supporters must ask to what extent the aspirations of our Constitution will be advanced by it. The answer is not by much when measured against the programmes of grant protagonists in countries with average per capita income levels ten times that of our own. There a central aim is fulfilment of this "basic right" as a constituent in the deepening of democracy.

> 'If a basic grant is to be relevant to democratisation, it should be adequate to provide what I shall call a modest but decent standard of life. This is a level sufficient to allow individuals a degree of control over their lives and to participate to the extent that they wish in the cultural, economic, social, and political life of their polity' (Pateman 2003: 131).

> '[Under a basic income proposal] all citizens are given a monthly stipend sufficiently high to provide them with a standard of living *above* the poverty line. This monthly income is *universal* rather than means-tested – it is given automatically to all citizens *regardless* of their individual economic circumstances. And it is *unconditional* – receiving the basic income does not depend upon performing any labor services or satisfying other conditions…as a matter of basic *rights*, no one should live in poverty in an affluent society' (Wright 2004: 5, italics added).

[5] The normative dimensions of income grants.

The South African campaign for a basic grant has borrowed ideas and tactics from the international groups that seek similar political objectives. These are either access to capital assets or a guaranteed income over the individual's life-time, but with differing eligibility or conditionality criteria. Questions logical to ask are whether the local rationale for the grant that is put forward shares a common philosophical base with the other movements, and whether the South African proposals meet the criteria and circumstances postulated or presumed in the goals of the older proposals. The short answer is that there is a measure of overlap but also troubling differences.

The issues below are selected from a large and growing literature, the purpose being to describe what is in question rather than to pass judgement on the merits of the normative propositions.

5.1 The *principle of reciprocity* is the most prominent omission from the local advocacy literature. There are no statements asserting that the individual's receipt of an income grant under the proposed policy, will be "conditional on his/her satisfying behavioural requirements, such as active job search, retraining or work itself" (White 2000: 509). Instead, following a number of left-libertarian proponents, access to the highest possible unconditional income on a regular basis is assumed or asserted to be a "social right" in South African discussion, although no direct link is established with our constitutional Bill of Rights. To Van Parijs for example, an international advocate of basic income with numerous publications (2000, 2004), it is an "entitlement derived from a theory of justice conceived in terms of real freedom for all [and] by 'real freedom' Van Parijs means (roughly) the ability to do what you want, and …his criterion of justice is that the freedom of those with the least real freedom is to be maximized. The means to real freedom so defined are resources…" (Barry 2000: 5).

Following the social right rationale, to benefit from such unidirectional transfers requires no more than the status of being citizens, or possibly legal residents that constitute a wider category in all societies with sizeable foreign and refugee populations. Ultimately this is a normative position based on moral values that a commentator from outside the forum of debate must either accept or reject. But it is pertinent to note that such a judgement – no reciprocity required - is in conflict with other moral traditions that are currently alive and well, for instance, what has come to be known as *welfare contractualism*. In this way of thinking, unconditionality has to be tempered by reciprocal obligation.

In addition, whether this requirement concerning reciprocity is in direct opposition to the notion of a social right is itself unclear. We have to examine the question whether a right to *receive* some resource without conditions attached is the only acceptable interpretation of this particular concept of a social right to resources. Or is a right of *reasonable access* an acceptable alternative that still retains the moral essence of such a right?

> ‘The notion of a social right can quite intelligibly be understood in the second way as well as in the first: as an unconditional right of reasonable access to a given resource, rather than as a right to be given this same resource unconditionally…If you leave me all the ingredients for a meal, a recipe, the use of a cooker and all necessary cooking utensils, and I have at least moderate cooking skills, then you will almost certainly have provided me with reasonable access to a specific meal, in the above sense, even though you have not actually given me the meal itself.’ (White 2000: 510)

This distinction, as well as the legitimacy of both forms of delivery of a grant, is unlikely to be acceptable to many proponents of a South African grant. But if so they are obliged to explain (i) why it is not acceptable, and (ii) why it does not feature in their justifying arguments for paid income alone, particularly as it is a distinction – access to a resource contrasted with receipt of the resource itself - that arises explicitly in our Bill of Rights, raised in the previous section (Archer 2004).

5.2 Commitment to the freedom of every individual, for instance the real freedom stressed as the ultimate objective by Van Parijs and others, seems to be the underlying moral impulse for the unconditionality of a grant. This conception of unqualified freedom will not recognise any indivisibility in the notion of freedom, nor any ranking of different kinds or dimensions of freedom, nor therefore any limitation on eligibility for resources deemed essential for that freedom. But the obvious question to be answered is whether such an absolute stance is compatible with other values that determine the integrity of complex societies with large and anonymous populations?

The promotion of generic freedom can be argued not to entail enough moral content by itself so as to constitute a self-sufficient value judgement. Rather, for logical completeness and for realism, we need to distinguish different kinds or dimensions of freedom for the individual. These must be ranked by their moral and social weights, with that weighting made explicit, open and supported by a rationale. “Thus it [real freedom] gives no special priority to freedom from disease over the freedom to be idle: freedom is freedom…The UBI [unconditional basic income] promotes freedom without responsibility, and thereby both offends and undermines the ideal of social obligation that undergirds the welfare state” (Anderson 2000: 1, 2). Again, these considerations go unrecognised in local discussions.

5.3 As discussed in the taxation section [8] below, the South African income grant proposals contain the stipulation that a maximum income threshold that determines eligibility is integral to the policy. Individuals earning income from other sources above some maximum level will not be allowed to retain grant income. It will be confiscated fully by special tax provisions. This is philosophically anomalous, as will be pointed out later.

Oddly enough, this is not a deliberate limitation found in conceptions of basic income in the international literature. Universalism is treated as absolute, although tempered with the recognition that upper income individuals will bear a larger cost burden on the financing side. The numerous variants here do not need discussion. It suffices to bring out the difference by quoting again a prominent advocate.
Relative to existing guaranteed minimum income schemes, the most striking feature of a basic income is no doubt that it is paid, indeed paid at the same level, to rich and poor alike, irrespective of their income level…For the ex nihilo introduction of a basic income to work to the financial advantage of the poor, the key condition is simply that, relative to their numbers (not necessarily to their incomes), the relatively rich should contribute more to its funding than the relatively poor. (Van Parijs 2004: 12)

Although generalisations are elusive, it needs noting that in existing schemes of social security including pensions, there tends to be continual movement in both grant conditionality rules and in the shifting incidence of the cost burden. This is probably because the longer-term consequences of programme introduction cannot all be anticipated in advance, an obvious enough note of caution but prone to be overlooked in the South African debate. For instance, the political costs of having to go back on a basic income grant policy would be high and socially disruptive.

Two welfare state examples of changes in *regime* (recipient’s point of view) and *pillar* (provider’s point of view) that moved away from universalism in recent times are provided by Goodin & Rein (2003: 787-8). In Australia, coverage of the age determined pension was almost universal at one point in recent decades, but then a means test – or “tall poppies test” – was “designed just to cut out the rich (‘tall poppies’) by excluding the top 20 per cent of the high-income and high-asset population.” Similarly, Canada has witnessed “a ‘paradigm breakdown’, with the rules of conditionality shifting from universality to targeting”, so that the year 2001 saw the introduction of “a new income-tested programme to replace the various earlier rules of conditionality, based on universal entitlement, guaranteed income supplements and tax clawback for high-income seniors.”

5.4 Although the idea of a grant in itself does not stipulate any particular level of income paid, there are major differences between the proposals for industrial countries and the local suggestions for a BIG. The international discussions mostly favour payment of a *subsistence income*, whereas the South African campaigners project a size of grant dictated principally by affordability. By convention in many European countries, the poverty line is taken to be half the median per capita income of the population at any one time (this amount for South Africa is R2609 in January 2005); and low pay is defined as a level of individual earnings less than two-thirds of median earnings (OECD 1999: 154; Barry 2000: 6). Both of these measures influence thinking about the appropriate level of proposed basic income in the countries characterised by active campaigning.
In practice, the amount of the income grant in the policy debate is more often left open deliberately. It is considered negotiable between government and groups active on behalf of the poor; therefore what expenditures per individual are judged to be essential and how they are weighted is seldom explicit. But the rationale itself for setting a particular level of subsistence income is usually couched in the international discussion at a higher level of abstraction, as the following examples show.

> ‘The idea is not simply to assist those who lose out through accident or misfortune (although this must be done), but instead to put all citizens in a position to manage their own affairs and to take part in social cooperation on a footing of mutual respect under appropriately equal conditions.’ (Rawls 1999: xv)

> ‘What we owe [to each other] are not the means to generic freedom but the social conditions of the particular, concrete freedoms that are instrumental to life in relations of equality with others. We owe each other the rights, institutions, social norms, public goods, and private resources that people need to avoid oppression (social exclusion, violence, exploitation, and so forth) and to exercise the capabilities necessary for functioning as equal citizens.’ (Anderson 2000: 1)

> '[I]f a basic income is to be relevant to democratisation, it should be adequate to provide what I shall call a modest but decent standard of living…a level sufficient to allow individuals a degree of control over their lives and to participate to the extent that they wish in the cultural, economic, social and political life of their polity.' (Pateman 2003: 131)

These statements convey the flavour of what is argued to be the ethical and political basis for setting a high grant in high-income societies. In passing, note that a translation problem is an immediate hurdle, along the lines discussed in the previous section of this paper dealing with human rights. How do we come up with a Euro or Franc or Rand figure which instantiates these ideas operationally? But the South African discussion sidesteps this problem, because the main determinant of the level of a basic income in the future is presumed to be a hypothetical budgetary decision about affordability and opportunity cost. That decision will not be easy to make – assuming that, against the direction of current official scepticism, the political will for a basic grant should ever become manifest – because heavier taxation will cause a range of adjustments in investment flows, employment levels, changes in the industry mix, and so on (Barry 2000: 3). We cannot simply presume that second and third-round effects in economic terms will be too weak to have a bearing on the net outcome in the longer run.

5.5 One other difference between industrial country and South African contexts for the institution of grant income is the markedly greater volatility in the incidence of poverty experienced by individuals in industrial countries. First, a much larger proportion of the population at the bottom of the income scale experiences temporary or transient spells of being poor. Short in duration, the dispersion of personal need, which is the target of grants, is continuously altering. Secondly, in these economies the poverty of most individuals and households tends to decline over time, for reasons difficult to untangle but probably because of greater access to merit goods like education and training, health care and housing. In access to resource terms, there is no path dependence in that a history of being poor does not significantly predispose an individual to continue in a state of deprivation. So in high-income countries, "poverty is not a life sentence" whereas for large numbers, probably the majority of the designated poor, it certainly is in low-income, developing countries. (Goodin *et al* 1999: 7-8)

The consequences for the potential role to be played by income grants in combating poverty have to be speculative in the absence of comparative research. Two implications illustrate what the differences might be that stem from the different national contexts. First, the investment functions to be played by transfers to the poor, analysed above in the first section of this paper, are needed less by the defined poor in high-income countries. Resource grants, whatever their form, can be ameliorative more than preventative and restorative in nature. This means they can be simpler administratively. Secondly, the temporary character of poverty spells in industrial countries implies an increased scope – in comparative terms – for anti-poverty policy to pursue goals other than merely placing funds in the hands of poor individuals. Such scope for instance would include *qualitative* improvements in the nature of the services made available as merit goods to poor individuals, like education, health care and social security benefits.

5.6 In the international literature, much attention has been devoted to the "Malibu surfer problem", named after the example developed in the writings of Van Paijs. Malibu surfers are that category of income grant recipients who would choose deliberately not to make a productive contribution to society were a regular grant for everybody to be instituted. By definition such a grant has to be at subsistence level to provide the material support necessary for individuals with no other sources of income. Van Parijs has put up a spirited defence of free choice for Malibu surfers, a consistent logical inference from his left-libertarian emphasis on the absolute right of every individual to "real freedom". This notion of freedom was discussed earlier in this section. But it is no surprise that commentators on international basic income proposals have found this implication of such an interpretation of freedom of choice hard to swallow.

Are we likely to see a significant Malibu surfer problem in South Africa under a grant policy? Probably not. First, in the foreseeable future the level of the grant will be much too low. Secondly, an inherent constraint on the number of surfers, and indeed on the magnitude of all transfer policies, lies in the ratio between contributors and non-contributors in any economy. "[As] liberals emphasize and everyone else acknowledges, however grudgingly, the re-distributive sector of the economy is necessarily parasitic upon the productive sector of the economy" (Goodin *et al* 1999: 260). Thirdly, the really interesting question concerns perceptions, particularly whether our historical background and cultural conditioning will induce responses similar to the Malibu surfer in a proportion of income recipients? In the local political arena there has been much rhetorical discussion about the emergence of entitlement attitudes in the years since political change was initiated. If they exist widely then we would confront a local version of the Malibu surfer problem (depending on the ultimate level of the grant), with the attendant resentments against non-workers to be observed elsewhere. Other potential effects of an instituted grant upon work perceptions, work seeking and work performance are discussed in section [8] of this paper.

5.7 Two final issues to arise out of the contrast between international and South African grant income discussions are (i) the feminist strand observable in the former literature, and (ii) the realisation that action on poverty is a process probably marked by increasing unit cost, an observation also found in the wider literature. It is surprising that neither of these aspects are prominent in the BIG debates, although it is accepted that in South Africa "[pension] money which goes directly to women is more likely to be spent on beneficial goods such as food for children and education" (Lund 1993: 21). In the wider literature, grant proposals are criticised for overlooking or underplaying the maldistribution of income and power *within* many, perhaps most, living units in poverty. Making a grant available for every individual in a household may well entrench single-person decision-making power, with a lowering of total welfare effects from a given sum of transferred income. Once again the empirical evidence for confirming or faulting this surmise is lacking in virtually all countries where existing, not proposed, grants income flows are substantial.

> 'Putting democratisation at the center [of existing discussion about welfare policies] requires attention to institutional structures… Household-based schemes disregard not only all the problems about the sexual division of labor, and the fact that women earn less than men, but also income distribution *within* households. Can it be confidently assumed that income would be distributed equally between husband and wife? A basic income is important for feminism and democratisation precisely because it is paid not to households but *individuals as citizens*.' (Pateman 2004: 24, original italics.)

The second point about declining cost is simple enough, but it is not addressed in the local advocacy literature. Helping certain poverty-stricken groups – whether escape or alleviation is the objective does not matter – is usually cheaper than helping others. For instance, in head-count terms those beneath but closest to the poverty line require the least transferred resources so that the largest reduction is achieved by concentrating a given sum of transfer payments on them. But, although efficient by this measure of the extent of poverty, it is hardly the criterion and the strategy most people would support (Atkinson 1995A: 35). In addition, it is likely that many of the poorest of the poor will be concentrated in remote, rural districts of any country because of weak infrastructure, and therefore are just the sorts of persons least touched by the state and civil society actions to lift poverty burdens. Under the principle of increasing cost or diminishing returns, achieving the last remaining fractions of any economic objectives can entail high marginal cost, or cost per person whose poverty is lessened in the present instance. Again this efficiency dimension is likely to conflict with widely-held ideas about priorities in poverty alleviation.

Local protagonists of basic income grants do not face such dilemmas or trade-offs explicitly.

[6] Macroeconomic implications of income grants.

Will payment of an unconditional basic income grant have positive effects on the macroeconomic stability of an economy? Or will it lead to overheating, evidenced by higher inflation, balance of payments imbalances, shortages of foreign exchange, and ultimately stringent fiscal and monetary actions of retardation? In short, will it more likely increase instability in the economy as a whole? The problem with the existing advocacy literature in South Africa is that proponents of an income grant all make the assumption that an *output gap* indicative of deficient aggregate demand is a chronic condition in our economy and indeed most market economies. In other words, a large and positive gap – deficient demand - is uniformly taken to be a structural constant at the economy-wide level. If true that would make every stimulation of aggregate demand a contribution to stability, as well as providing the impetus for accelerating economic growth. But the plausibility of this presumption about the macro-economic data is *not* demonstrated at all in the writings on income grants now available, nor does the standard data support such an interpretation; for example, see Arora & Bhundia 2003, IMF 2003.

By contrast, there is clear evidence of long standing, locally as well as internationally, that the output gap is itself a cyclical phenomenon in all economies. Figure 2 shows such fluctuating behaviour in tracing the movements in actual and potential GDP, and thus the output gap, for our economy over the last 30 years approximately. Therefore demand stimulation, from an expansion in state spending *and* from a rise in the level of total consumption, which is what transfers through basic grants will tend to do, can sometimes be a beneficial stimulus but sometimes not. Indeed such stimulation at certain junctures can push up inflation, price-wage spirals, interest rates and other symptoms of macroeconomic strain.

The model of a mature economy that provides the background to this interpretation is simple enough. It reflects the fact of more-or-less continuous growth since the recovery from the 1930s depression and the peculiar conditions of World War II, although marked by deviations in growth rates up and down.

‘Real output in most advanced capitalist economies fluctuates around a rising trend. One can argue about whether it is best to think about that trend as passing through successive cyclical averages, defined in one way or another, or best to think of it as passing through cyclical peaks, or some other measure of “potential” output. The important observation is that, on the whole, the observed fluctuations around trend are contained within a moderately narrow corridor. Unemployment rates tend to run between, say, 5 percent and 10 percent in the United States. Other countries have different typical ranges…’ (Solow 1997: 230).

This is not the place to discuss in detail the concept of an output gap as a measure of macro-economic fluctuation. But two points are worth making for non-economists. First, this idea remains at the heart of discussion in macro-economics going back to the early 1970s when events like inflationary financing of the Vietnam War and dramatic oil price rises caused instability in most mixed economies of a magnitude not seen for decades. Equally serious for the discipline was the realization that received macro-economic theory was inadequate to provide clear policy guidelines to counteract this surprising instability. Simple demand cut-backs or expansions by state action seemed to make matters worse, not better. New strands of theory emerged to modify the old “neo-classical synthesis” that incorporated Keynesian thinking about deficient demand into the conventional framework. But the high degree of consensus once existing amongst macro-economists has never been recovered.

Second, a related idea is that of the *non-accelerating inflation rate of unemployment* or NAIRU, which analyses economy-wide fluctuations in terms of employment rather than output changes. It is relevant to mention not because employment creation is now stated to be at the centre of South African policy actions (a useful by-product to this discussion), but rather because analytical work on the NAIRU has demonstrated that policy actions aiming at more stability can push inflation and employment in opposite directions in the short run. Most economists accept this, yet they also accept that this trade-off – buying lower unemployment by living with rising prices – does *not* exist in the long run. One cannot go on playing the trade-off indefinitely. But there is always the temptation to believe the opposite, as demonstrated by the Latin American policy experiments mentioned below.

One recent example of thinking an output gap to be a structural constant is to be found in the 2003 Human Development Report on South Africa.

> '[W]ith almost 50 per cent of the population living in poverty, the total level of financial resources for buying goods and services in the economy remains severely constrained (constrained aggregate demand). This, in turn, deprives producers of a potentially much larger domestic market – a market that would allow them to operate at a higher level of current production capacity and/or invest in expanding their production capacity and employment. This conclusion is strongly supported by [the] regular survey, *Manufacturing: Utilisation of Production Capacity*…Household expenditure surveys also suggest that, owing to high-income inequality and poverty, the overall demand for goods and services is relatively weak among 80 per cent of households in South Africa…These observations provide consistent evidence that low demand is one of the main inhibitors of economic growth in South Africa' (UNDP 2003: 186-7)

This passage is riddled with *non-sequiturs*. First, the manufacturing sector contributes about 24 percent of total GDP currently. How this sector's average level of idle capacity can be extrapolated to the whole economy needs explicit justification. Second, in no economy in the world is the utilisation rate of a production sector, particularly manufacturing as the most usually measured, at any time a figure approaching close to 100 percent.

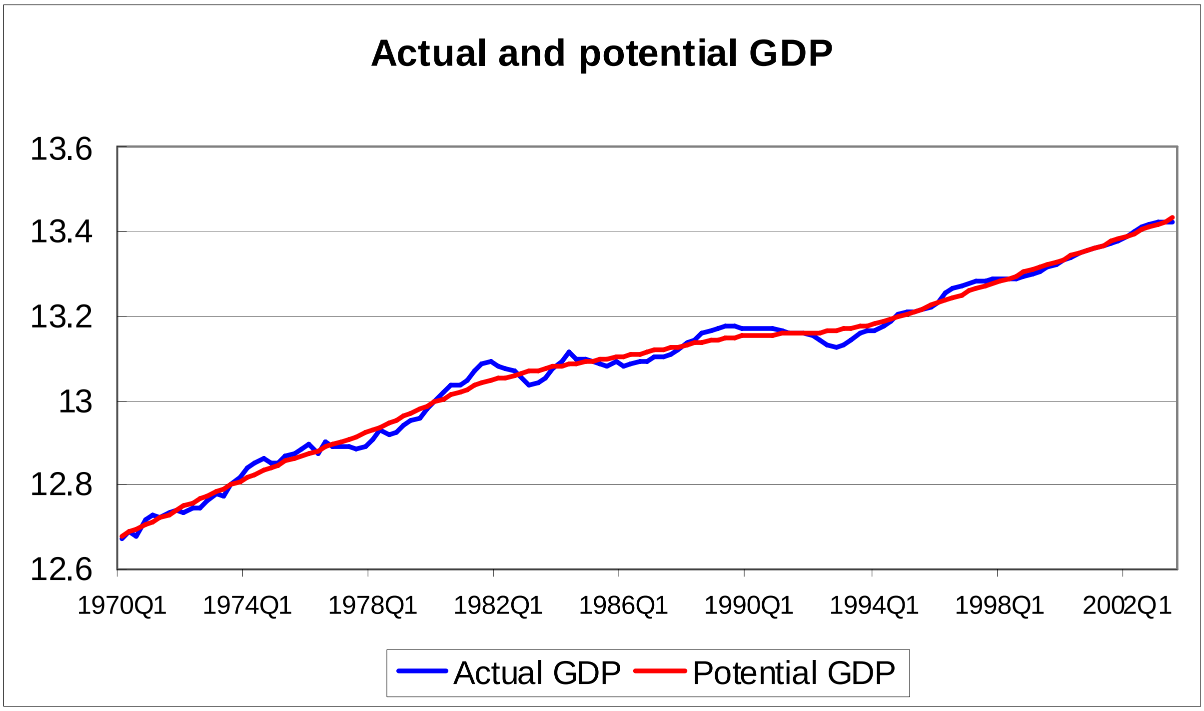
There are well-known microeconomic reasons why what is nominally "unused capacity" is desired by producers. So the cyclical existence of such capacity is quite compatible with profit maximisation and equilibrium. Third, it does not follow at all that an expansion of aggregate demand, engineered by simple fiscal expansion – higher government spending or lower taxes - whether for redistribution or some other purpose, will lead to higher activity rates and higher real economic growth in a national economy. Fourth, under this way of thinking redistributive action is a panacea for macroeconomic gains because such gains are simply presumed to lead to higher levels of social welfare. All that stops this process happening is taken to be weak political will.

These inferences are what the Human Development Report apparently wants the reader to believe. To place this belief in chronic deficient demand in perspective because it is shared by certain local activists pushing for a basic income grant (as well as other research projects under the UNDP umbrella currently working locally, like "An employment-targeted economic program for South Africa"), we need to recall the experience of a number of Latin American economies during the 1970s and 1980s. Regimes in power in Argentina, Brazil, Chile, Mexico, Nicaragua and Peru experimented with stimulatory policies known in retrospect as "macroeconomic populism". These episodes had enough in common to make up a common policy pattern or paradigm that existed for a brief and concentrated period of time in these countries.

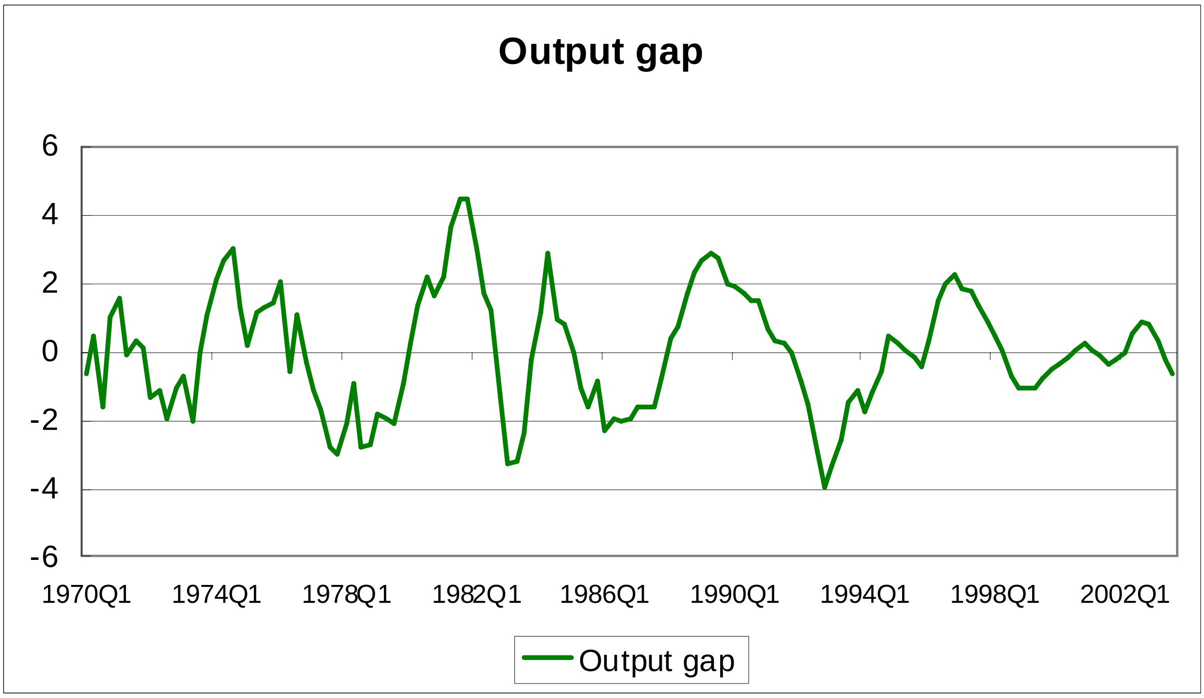
First, the initial capacity utilization rates in each national economy were diagnosed as disappointing but holding the promise of more output. Previous stabilization efforts had put the state budget in balance as also the payments balance with the rest of the world, so that latent scope for expansion of the economy was identified by populists in government. Second, by assumption spare capacity and unit cost decreases brought about by higher levels of production were forecast as limiting possible cost pressures and inflation in most branches of production. In addition, the risks attendant on expansion through deficit financing by the state were dismissed as exaggerated. Third, policy prescriptions in the populist programmes of all six countries laid emphasis upon three components:

> '[The] reactivation, redistribution of income, and restructuring of the economy. The common thread here is "reactivation with redistribution". The recommended policy is to actively use macroeconomic policy to redistribute income, typically by large real-wage increases that are not to be passed on into higher prices [enforced by controls]' (Dornbusch & Edwards 1991: 10).

Figure 2



Source: SA Reserve Bank.



Source: SA Reserve Bank.

In all cases the first phase seemed successful for these populist expansions. But in the second phase it led to negative outcomes, indeed to disastrous consequences, because of bottlenecks in the supply of goods produced in the domestic economy and in the availability of foreign exchange. Governments began to realise they were unable to switch the processes dominant in their economies from redistribution goals towards investment in all its needed forms. These components of investment were the stocks of goods in process (or inventories) as well as the fixed investment in plant, machinery, buildings and infra-structure needed for a permanently higher level of activity. In the third phase, pervasive shortages continued, inflation accelerated rapidly, the state's budget deficit continued to expand dramatically, and real incomes, ironically wages in particular, declined markedly. In the fourth or final phase, some measures of orthodox stabilization were inevitable, usually under a new government, but after a great deal of suffering by the population. "The extremity of real wage declines is due to a simple fact: capital is mobile across borders, but labor is not. Capital can flee from poor policies, labor is trapped." (Dornbusch & Edwards 1991: 12; Mohr 1994; Moll, Nattrass & Loots 1991)

South African income grant proposals do not fit this paradigm completely. That is not in contention here. Yet a central *presumption* shared by the economic argument justifying basic payments is that the redistribution they effect will raise the level of effective demand. It will take income from groups who consume a smaller proportion of income, relative to the average, and give it to groups who consume a higher proportion of it. But this rise in expenditure by the poor (and by the state) is predicted not to cause economy-wide imbalances because excess capacity exists in advance.

This was a faulty premise to start off the argument for macroeconomic expansion in the Latin American cases, and it is a faulty presumption to make in South Africa. As stated already, true excess capacity is a cyclical phenomenon not a structural constant that marks all market economies. Expansion of aggregate demand through fiscal transfers may result in benign macroeconomic growth or it may result in overheating and imbalances: it depends on the cyclical position of the output gap and the magnitude of the transfer at the time. Further, the financial and budgetary orthodoxy adopted by policy-makers in capital-hungry economies is usually to attract foreign investment, amongst other objectives. Sometimes this is out of theoretical (or even ideological) conviction, but often it is simply because there appears to be no sensible alternative in a world where capital movements across frontiers, financial as well as real, have speeded up greatly in recent decades.

[7] The targeting and means testing of social transfers.

In the sphere of policies that target individuals and groups for assistance in contrast to policies of universal access, we are again in an arena of competing judgements. We lack direct as well as comparative information from international experience. Thus an evidence-based choice on efficiency and equity grounds is not possible. The brief discussion here aims to tease out what is presumed and claimed by campaigners for a basic income grant, in South Africa as well as elsewhere. It provides perspective on the discussion not finality in the judgement.

Curiously, our old age pension is not a universal cash grant that shares non-conditionality with the basic income under discussion here. The state pension is available only to those citizens who fall below the maximum income stipulation at the minimum ages applicable to men and women; that is, it is means tested. An acknowledged success, it is regarded as one example of South African “exceptionalism”. No other national grant or pension system exists on an equivalent scale in another country at a similar level of average per capita income (Case & Deaton 1998; Seekings 2002). But our successful pension is a *counter* example not a confirming precedent for a basic income, in that it does not provide support for the claimed merits of universality.

The second curious feature of the proposal is that protagonists of an income grant in South Africa advocate that recipients of it above a certain threshold level of pre-existing personal income will have the entire grant taxed away. One presumes this is on equity grounds mainly, because the resulting saving in the aggregate cost of the policy is difficult to project *a priori*. For this to happen, once again a means test must be applied, as is inherent in all tax systems containing progressivity, meaning higher proportions of income paid in tax at higher levels of income. We discuss other difficulties and details below under the next section on taxation. These two examples illustrate that the aversion to means-testing for a basic income grant appears to be selective, and it is necessary to understand why.

The relevant issues are the following.

- As proposed, a basic income grant is *universal* in two senses. It is non-contributory, not confined to individuals committed to a scheme by making dedicated contributions in advance; and personal access is unconditional, ie. not governed by conditions like inadequate means, disability, unemployment status, family circumstances, and so on.
- It is financed out of general state revenues not by an ear-marked tax or levy dedicated to that purpose.
- Pitfalls in the targeting of poverty alleviation instruments are recognised in the literature but perhaps less so in policy practice.

  [C]laims [for increased targeting] implicitly assume that incomes can be observed with little error and that the observed initial incomes are fixed, that is, unaffected by the policy. In reality, the policymaker has imperfect information and can incur (possibly high) administrative costs in attempting to identify the poor with precision. Furthermore, potential recipients often face an incentive to alter their behavior when facing a targeted (or untargeted) scheme. Potential losers from perfect targeting may also exercise greater political influence than gainers; [thus] political economy considerations may militate against the policy ideal of perfect targeting. (Van de Walle 1995: 3)
- Universal access to income transfers would have a uniform effect on the welfare of the poor if this group were homogeneous in the relevant respects. But what respects are relevant? First, differences between income levels of poor individuals and households in the *pre-grant* situation clearly are one characteristic of interest. Taking the lowest 40% of individuals or households on the income scale as the relevant target group, how

> much variation is exhibited within the intra-group distribution? If there is a long tail to the distribution of income amongst the poor then the implicit assumption of homogeneity – implicit in BIG proposals of a uniform grant – is potentially misleading in welfare terms.

A simple measure of intra-poverty distribution for the present purpose is comparison of the mean income per decile (10%) for each of the four lowest deciles making up the 40% defined poor. These differ strikingly, as Table 1 brings out for the year 2000, even if we ignore decile 1 with its anomalous implication that up to 4 million people were living in the year 2000 on R30 per month. To presume common average economic circumstances for the poor masks significant dispersion of income within the group when it is so defined. Distinguishing between the four broad decile groups shows that median incomes range in proportion from first to fourth decile at 1.00, 3.05, 4.63 and 6.67, or expressed in the monetary values shown in the table. The relevant question is at what *opportunity cost* to potential help targeted disproportionately at the most poor are these income differences ignored in advocating a uniform grant to all poor persons irrespective of their income per head?

Table 1

Median Income By Decile with Weights				
	Decile 1	Decile 2	Decile 3	Decile 4
Absolute	360	1170	1800	2727.636
As Proportion of Decile 1	*1.00*	*3.25*	*5.00*	*7.58*

Source: Income and Expenditure Survey, September 2000, Person File, calculated by K Reynolds

Second, gender sensitivity is a convincing criterion of interest for poverty relief, as also is the incidence of female-headed units in the household group that is designated poor. Third, the families containing above average numbers of children are plausibly an independent target of special anti-poverty efforts, where their numbers are increasing while the incidence of other poor sub-groups like the aged are decreasing within the total poor. Fourth, there can be serious urban bias in the availability of physical and social infrastructure. So two individuals or two households equally poor by an index of goods and services – possessing the same endowments in economic terminology - can face differing probabilities of exiting from poverty simply because of their different locations. Fifth, individuals and families designated poor vary in their ability to spend income and non-income resources prudently. So their welfare gains from the same-sized increment of transfers received from the state will differ. That this may or may not matter for the design of pro-poor policies has to be argued explicitly. Finally, a parallel and overlapping category are the unemployed in the South African labour force. They are shown to differ amongst themselves in ways that bear on their probabilities of obtaining a paid job, and therefore require “specific kinds of interventions” not a single tactic only (Woolard 2004: 3). One size does not fit all.

Thus, whatever weight might be given in principle to other dimensions of poverty, for instance, relatively higher HIV infection rates amongst the poor, opting for a universal vehicle of transfer like a basic grant comes at a *cost* in foregone targeting. That cost is in no identification and no special measures for high-priority groups within the poor population. Focused “pro-poor” growth and poverty elimination policies are not possible because the relevant circumstances that govern the differing welfare significance of cash receipts for some individuals and households are ignored under universal access.

On the other hand, specific targeting has its pitfalls, some already alluded to above. So we are yet again in an arena of choice between recognisably imperfect policies – the economist’s concept of second-best - yet with little evidence to guide the welfare-maximising choices that have to be made.

[8] Behavioural responses of recipients and payers to tax-transfer mechanisms.

An assumption implicit in all income grant advocacy is that the *net* effect of such a re-distributive policy on the welfare levels of a national population will be consistently positive. Yet the underlying reasoning is left unargued. It is presumably that the benefits are worth more than their costs, so that one unit of spending power received by someone lower down the income scale has consistently greater welfare significance than it has when yielded up by a payer higher up the scale. This is probably true over a certain range of re-distributive transfers, but we do not possess a widely accepted calculus for making simple judgements about *all* changes in the personal well-being of givers and receivers. Comparisons of changes in income utility between persons are of doubtful legitimacy, in that there are long-standing arguments that these are philosophically incoherent, even though we make such comparisons without inhibition in the everyday business of life. But also there are multiple effects of taking and giving that are difficult to identify let alone quantify.

That is the first difficulty to be noted. The second is that showing a positive welfare gain by an act of redistribution is not a sufficient justification. We have to go further and show that *this* way of transferring resources – via an income grant in the present case – is the most efficient feasible. The poor have to receive the biggest "bang per transferred buck" amongst all ways of making transfer payments in their favour. That is rather more difficult to show.

The purpose of this section is to raise certain questions about gains and losses that must be faced before any broad judgement about the net effects of payments like unconditional cash grants can be sustained. Taxation and transfer payments can have the following effects in an economy, although this list is not intended to be comprehensive.

- ⇨ After imposition of a new tax or increased tax, the supply of productive effort by tax-payers can decline or it can rise depending on the choice they exercise; that is, they can perform more work and thus retain income levels, or opt for lowered consumption and savings but increased leisure. This topic is a staple of economics textbooks, even if the evidence often remains ambiguous in practice. Generally it is accepted that a decline in the labour supply is more likely than a compensating rise in work aimed at maintaining the same level and mix of individual income and leisure that existed before payment of the tax. This has to be tentative because the major research problem is isolating how much work input changes downwards in practice due to this specific cause, higher tax liabilities.

- ⇨ Incentives to invest and take risks in the economic arena can be weakened by higher tax rates, resulting in a loss of potential GDP and therefore lower levels of social welfare. But again this has to be a tentative proposition in the absence of empirical studies difficult to conduct because respondents may tailor their answers to benefit themselves, ie. avoid higher taxes being levied.

- ⇨ Perverse effects on individual welfare are common. "On the recipients' side of the tax-transfers system, there is also a disincentive to produce. For each extra dollar a low-skilled person earns with extra work, part or all of that dollar will be taken away from them because they [now] have less 'need' for income support, a clear disincentive to work. One can fiddle with the system… [but] sooner or later the benefits must be withdrawn if the person keeps earning more and becoming more self-sufficient." (Lindert 2003: 4)

⇨ Altruism is the “willingness to have one’s tax dollars spent on other people” (Gutmann 1998: x). It has to be conserved because it is a scarce resource. We do not all have utility functions like Mother Teresa whereby we obtain satisfaction from other people’s gain. But implicit in the underlying arguments of many universal grant protagonists in South Africa is the *presumption of infinite altruism*, as we might call it. What limits apply to tax-payers’ willingness to pay taxes for redistribution purposes in a given society at a given historical moment remains a matter of conjecture not of evidence, because of the intrinsic difficulty of the required research. But in general, in most or probably all societies, “altruism is scarce; there is never enough to go around. [So] the function of economics [as a discipline] is to devise social institutions that make it possible to economize on altruism and still live tolerably” (Solow 1998: 3-4).

It follows that it would be prudent to minimize demands on altruism, given the set of difficult-to-identify variables that influence its nature and extent in practice. These conditioning determinants or variables include the felt strength of a common culture; solidarity of beliefs and shared values in the population; legitimacy and acceptability of state expenditure policies in general, and on redistribution and merit goods in particular; perceptions of corruption in state departments and agencies; and the extent and tradition of private philanthropy. A commonplace observation, but vitally important nevertheless, is that all tax systems rely, for high yield and low cost per unit of revenue, on the unforced compliance by the vast majority of assessed payers. So it should be unsurprising that voluntary payments of tax liabilities can be fragile, as evidenced still in a range of middle to high-income countries like Greece, Portugal, Korea and Mexico (Van den Noord & Heady 2001).

⇨ In national tax-transfer systems that have conducted research on the attitudes of grant recipients (like the US and Canada), it seems clear that the overwhelming majority *prefer* working to earn eligibility to receive payments rather than passive acceptance of transfers. The reason is not complicated. It has to do with self-respect, social standing and the dependence of “felt identity” on the regular performance of productive work. One key question is whether and to what extent the populations of transfer recipients differ in such attitudes, and in strength of preferences, in other countries than those where such research has been conducted (and which in general have developed welfare state institutions)? In South Africa, critics of specific re-distributive policies like free provision of water or the subsidised supply of electricity, housing and health care, for instance, cite a culture of entitlement arising out of our recent history. It follows that attitudes of entitlement will conflict with a preference for work performed as the route to eligibility. But it is not yet possible in this regard to draw a line between accurate research findings and political rhetoric.

The ongoing enquiry into the differing performance of European labour markets and welfare states by comparison with that in the United States, illustrates the unsettled state of much of the debate on these questions. The following quotations from recent studies bring out the views *contrasting* with certain presumptions that underlie the grants campaign, while bearing in mind that South Africa is still far from possessing the resource levels and institutions of these mature welfare states.

> 'Our study relies on the large size and persistent character of tax differences among rich countries to draw inferences about long run tax effects. In summary terms, the data tell this story: Higher tax rates on labor income and consumption expenditures lead to less work time in the market sector, more work time in the household sector, a bigger underground economy, and smaller value added and employment shares in industries that rely heavily on low wage, low skill labor inputs.' (Davis & Henrekson 2004: 36)

> 'Why haven't countries that tax and transfer a third of national product grown any more slowly than countries that devote only a seventh of GDP to social transfers?…This paper has surveyed [in a range of European welfare states] some institutional clues pointing toward a non-negative contribution of social transfer programs toward economic growth and well-being. The list of clues is eclectic and incomplete. We now have a better understanding of the tax mix practiced in welfare states, and the limits on the damage done through work disincentives…These findings can only be suggestive, and we are a long way from an overall quantitative accounting. Much of the story consists of welfare states' avoiding ruinous patterns of taxation. In fact, their tax mix even resembles some classic prescriptions from economists' optimal-taxation literature. The heavy taxes on addictive complements to leisure [tobacco, alcohol and gasoline] fit both the growth prescription and the need to address [negative]

> externalities…Behind the eclectic set of clues and the hint of classic fiscal wisdom may lie a fundamental unity, a single mechanism that explains how welfare states found such an assortment of safety devices and avoided damaging their economic growth.' (Lindert 2003: 2, 28-9)

> 'Can European countries maintain the same level of social protection, but do it in a way which allows them to return to low unemployment? Again, this is a question which vastly exceeds the bounds of this article. But the evidence from a number of countries that have returned to low unemployment, from the Netherlands to Sweden, suggest that the answer is positive.' (Blanchard 2004: 31-2)

Turning to the taxation side, discussion here once more is selective in a complex field. Three issues are singled out for attention. First, how should we measure the burden of taxation in an economy, specifically a marginal increase in that burden needed to fund a grant? Further, can we generalise about the potential effects of South Africa's taxation system – ignoring the welfare gains from expenditure of its receipts for the moment – by drawing on measures for a similar purpose from other countries? This seems a working presumption of some local proponents of an income grant (Samson 2002). Second, arguments for the institution of a BIG include the proviso that individuals with incomes higher than some designated threshold level will have their entire grant receipts taxed away, or "clawed back" by the state in the phrase used by grant supporters. This applies to a recipient group of unpredictable size who would take up grant income as a matter of personal right despite their exclusion by a means test decision. What complications and what consequences can be anticipated in carrying out this kind of confiscatory taxation? Third, all taxation changes payers' behaviour to a greater or lesser extent. The relevant questions have to do with the efficiency and equity consequences of that changed behaviour.

First, in making international comparisons to decide the affordability of higher taxation we are interested in assessing *effective* tax burdens. This means the actual amount paid to the treasury by taxable units (individuals, companies, commodity vendors) and not the formal statement of liabilities according to the tax rules in each country in the comparison. The latter do not take into account variables like individual or group exemptions and eligibility conditions which influence the tax actually paid and therefore the behaviour responses. Thus, a simple enough point, two similar "tax ratios" relating total receipts to national income in two countries may rest on quite different underlying adaptations and adjustments.

‘Why tax-GDP ratios can be deceptive [can be illustrated]. Assume the ratio of corporate income tax revenues to the value of GDP in countries A and B is 2.5 per cent and 5 per cent, respectively. This suggests that tax burdens are higher in country B. However, this need not be the case. If corporate earnings in countries A and B constitute 10 per cent and 20 per cent of GDP, respectively, the average effective tax rate for the corporate sector is 25 per cent in both cases since in country A corporations pay 2.5 per cent of GDP on their profits equal to 10 per cent of GDP, and corporations in country B pay relatively twice as much in taxes on profits that in relative terms are twice as high as in country A.’ (OECD 2000: 9)

Next, the nature of the tax base is ignored when using an aggregate ratio as indicator of the tax burden. In two countries with the same ratio, Country A’s tax system may aim to be more comprehensive than Country B’s system, for instance including fringe benefits and capital gains in the definition of taxable income that comprises the base. “One main shortcoming of [relating total receipts to national income] is that it disregards the tax base a tax is levied on. A ‘tax ratio’ for a certain type of income tax of x% may be the result of a combination of (a) a broad tax base and a low tax rate; or (b) a narrow tax base and a high tax rate. The economic consequences are, obviously, very different.” (Immervoll 2004: 7)

Additional problems can be listed briefly: (i) some kinds of taxes have consistently a stronger impact on economic behaviour than others but these differences are cloaked by aggregating all taxes together; (ii) an extreme example but not unrealistic is a specific tax in place which generates no revenue at all but is wholly detrimental to economic growth because it makes a certain type of productive activity so financially unattractive as to preclude any engagement in production at all; (iii) tax burdens need wider contexts for assessment, in that in some countries the private sector may be compelled by regulation to provide public goods in contrast to their supply by the public sector in other national systems, and can include the compulsory provision of social insurance; and (iv) the treatment of self-employed income is considered the Achilles heel of every tax jurisdiction because of the scope it poses for inefficiencies, inequities and inconsistencies. Generally speaking therefore, no simple statements are possible about the net effects on tax benefits, work incentives and the overall tax burden by using macro-level indicators like tax ratios. (Atkinson 1995B, Van den Noord & Heady 2001, Immervoll 2004)

Second, all proponents of a basic grant propose that a threshold level of maximum personal income should determine eligibility, that is, to keep and spend the grant not merely to access it. Above that income level, not yet specified in advocacy writings, individuals who take up the grant will have it taxed away. The contrasting procedure with the state old age pension is instructive. A means test is the hurdle to be overcome at present *before* being deemed eligible for the old age pension in South Africa; that is, the person's level of income and financial value of owned assets is calculated in advance. But the difference in the case of the grant would be that ineligible recipients will be tracked *after* the event and required to pay back the entire annual grant receipts in a special tax assessment of grant income. Although the process is not described in concrete detail this seems to be what BIG supporters have in mind.

A range of questions here need research attention. One clear requirement is accurate and up-to-date record keeping of grant payments to identified recipients, coupled to close liaison with ordinary individual tax assessments so that cross referencing can pick up grant income receivers amongst those above the grant retention threshold. Most of this sub-category of grant takers will presumably also pay conventional taxes, the number determined by the relative heights of the two thresholds: that for grants and that for income tax liability. Then having isolated the grant proceeds, or "ring-fenced" that targeted component of personal taxable income, a dedicated assessment formula must be applied to it in the shape of a "multiplier" to raise the marginal rate of tax on the grant to 100%. Then no net benefit will remain. In other words, the whole R1200 of grant income in a tax year – R100 per month in this illustration – must be taxed away.

But a basic income grant is prescribed as universal in the sense of unconditional availability. That means that any citizen or any legitimate resident can obtain it without fulfilling any conditions. Yet an *after-the-fact* means test as a qualifying rider is an integral feature of the proposal. This may be politically expedient but it is a philosophical sleight of hand. Two virtues of the proposed grant are trumpeted to be (i) its universal character in keeping with democratic values, and (ii) the absence of a means test tainted by past humiliation, corruption and indeed racist distinctions between categories of recipients and between recipients and bureaucratic decision-takers, as well as administrative costs.

But the inconsistency in the present proposal remains. In conception this is a grant based on solidarity. That means universal access for every citizen without exception, yet policy advocacy starts from the premise that it is not intended for individuals who command resources above a level set by political and affordability calculations. These exclusion criteria are contingent and ad hoc in nature, on a different plane from the deeper moral purpose stated to underlie the legitimacy of the grant for everyone.

Third, the most important effects from an economic point of view, and yet most difficult to predict about a tax-transfer process in the absence of more empirical information, are those relating to the behaviour responses already mentioned. Will the average South African tax-payer, when faced with higher tax liabilities, compensate by adopting more productive practices, by taking more risks, by working for longer hours, with greater intensity, by saving more, by retiring later, and so on? Or will he or she do the opposite because they calculate that every marginal increase in income is liable to a higher fraction of tax payable, so that increased leisure becomes their preferred alternative as it is not taxable? On the recipient side, will grant beneficiaries look for jobs more consistently and energetically, or pursue more informal opportunities that generate income, once their resources expand by the extent of the grant? Or will they put less effort into the range of activities, like job searching, that might yield greater economic independence, and instead devote their new grant income wholly to consumption?

The sobering fact is that we do not know *a priori* which responses are most likely to occur. But it is erroneous to pretend that behavioural changes following taxes and transfers do not matter, as is implied by omission of the issue in much local grant advocacy literature. A number of questions need airing (Atkinson 1995B, Barr 2001, Disney 2004).

- Informally it has been suggested that, by international standards, a higher than average tolerance of "tax fatigue" exists in South Africa because of consciousness amongst tax payers that in our apartheid past deliberate race and class barriers governed access to economic resources. It may follow that these circumstances call now for specially effective modes of redistribution. This conjecture might or might not be plausible, but does it provide a sufficient rationale for ignoring the question of higher "excess burden" from higher levels of taxation, ie. lowered welfare levels from distorted choices, meeting compliance and administrative costs and so on? In the absence of appropriately designed attitude surveys, not an easy task, this informal conjecture is far from an adequate basis for designing expanded tax programmes to finance a new grant.
- Spending on a basic grant will be financed largely by current tax contributions levied on the population economically active at any one time. This is known as "pay-as-you-go" (PAYG) financing. In the international literature it is accepted that this can insert a tax wedge into the labour market, depending on how it is levied. It means that the real cost of labour facing employers differs

from the real wage received by workers. It is an unambiguous distortion. Depending on the size of the wedge, it can inhibit employment creation or even decrease the workforce itself, which will aggravate the financing problem because fewer workers will be shouldering the burden. This is a possibility not a research result.

- Another broad generalisation about the effects of taxation found in the literature on other countries is that male economic activity rates – broadly labour supply and saving behaviour - are relatively insensitive to net increases in tax liabilities. This is not the case with women. But in an intermediate economy like South Africa's in which women from a variety of groups are in process of becoming economically active outside the home (many being informally productive inside it), the burden of a heavier tax regime on activity rates may be particularly difficult to identify. (Disney 2004)
- One key determinant of behaviour responses to changes in taxation is the closeness of the link between individual contributions and individual benefits in the *perception* of the payer. This is a complex question, concerning expenditure on public goods (law and order services, defence, public administration, enhanced environmental quality) as well as merit goods like education and health care discussed earlier in this paper. But in the South African case of basic grant financing and distribution, such a link would be particularly tenuous if direct taxation is employed. This will be so because the vast bulk of tax liabilities on income and wealth intended to finance a grant will be to the account of individuals purposely *excluded* from its benefits. For them there would be no link whatever between tax payment and grant receipt.
- Finally, we cannot make direct use of established empirical results about taxation's effects in one context, say in one country, to draw inferences for another context even if we keep it tentative. We certainly do not have a controlled experiment in so doing.

  We observe that Sweden, say, has typically set higher income tax rates than the United States. Can we examine the labour supply in Sweden, compared to the United States, and draw conclusions about the impact of taxation? If Swedish doctors play more tennis and see fewer patients (a purely hypothetical statement), is this evidence that progressive taxation reduces work effort? The problem with such an inference is that we have no idea what

> *other* factors may be influencing labour supply decisions. There may, similarly, be common influences on *both* variables [tax and work]…without there necessarily being any direct causal connection [between them]…The same objection applies to the time-series studies. (Atkinson 1995B: 140, italics added)

[9] The preferences and choices of the poor.

If poor individuals in any society were given a set of unweighted choices to make about the form in which they want to receive a net increase in resources, what would be the outcome of their choices? In particular what would be the majority choice? We certainly do not know *a priori*, and the international literature is probably not a reliable guide on a general answer to this question, given the influence of history, local attitudes and individual circumstances. Yet South African proponents of the basic income grant take the answer to be a uniform preference for cash income on a regular basis, rather than, say, the improved delivery and quality of merit goods. What the backing is for this presumption is not made clear in published advocacy sources.

One contentious matter should be raised up front. Is the average poor person sufficiently well informed to make decisions between alternative uses of resources that consistently lead to outcomes in the best interests of themselves and those dependent on them? Again, we do not know. To some this question is anathema because it does not start off from the value judgement that individuals must be allowed to do whatever they want to with resources legitimately obtained. That is the left-libertarian strand of thinking referred to earlier, and argued eloquently by writers in the BIEN and other movements propagating a basic income. Nevertheless it is not helpful to be frozen into immobility by the fear that merely to pose the issue is to be found guilty of paternalistic attitudes towards poor people which are morally problematic.

This issue ramifies too widely to be summarised satisfactorily here. Whatever position one adopts one is still faced by the circumstance that no modern state is inhibited to make a range of choices for its national population. It does so respecting the allocation of resources to supply merit goods like education, health care and grants to deserving groups, as well as by devoting resources to inhibit self-destructive choices leading to crime, unwanted pregnancies, drinking and drug-taking. It uses sticks alongside carrots, eg. by taxing the consumption of addictive goods, on wholly paternalistic grounds.

Of particular relevance to the basic grant discussion is the attitude towards work performance by the representative poor individual. Given the free choice, would such a person prefer paid work to inactivity in exchange for a cash handout? Clearly this version of the required question is under-specified. Much depends on the relative amounts paid as wage or transferred as grant; what work is on offer, with what probability and how onerous its demands are; the social standing that attaches to such work; and the stigma, if any, of receiving grant support. Thus a range of variables will bear on the decision between working and not working in exchange for grant income. These cannot be incorporated as *a priori* presumptions into the decision framework for modelling the question. They must have empirical backing, which we do not appear to possess in South Africa.

Similar concerns were aired earlier in section [5] on the normative dimensions of income grants. But the difference is that the focus here is on what is plausible to project on the attitude of grant recipients to the performance of productive labour. Would the average poor person in South Africa, in reasonable health, actively *prefer* making a productive contribution? We do not know, and extrapolating the experience of rich welfare states is fraught with unknown margins of error. But the American experience during the 1990s is instructive for showing what a change in welfare policies coupled to favourable labour market conditions can do to influence the choices of the poor, without any presumption that the same will be true here. The US achievement in expanded employment does not provide a generalisable answer to the question posed – in what form would poor individuals prefer to receive extra resources – but it demonstrates the kind of choices which a national poor population are capable of making in their self-interest when their circumstances change.

> ‘There is one additional piece of good news from the 1990s boom [in the US economy], on which social science research is just beginning to focus – that forms of socially deleterious behavior that threatened to lock persons into a life of poverty also declined in the 1990s. Persons in poverty-prone groups seem to have responded substantively to the employment and earnings opportunities that the boom offered them, taking advantage of newly available opportunities to work and rejecting “underclass” activities that many analysts had come to view as an intractable part of the US social system. The most well-documented behavioural change is the drop in crime…econometric studies, covering somewhat different time periods and area groupings, have found that the change in crime is closely associated with labor market conditions…For disadvantaged women, the key indicator of underclass behavior is having children out of wedlock in their teens,

> which has historically led them to rely on welfare for their later subsistence. In 1996 the US Congress enacted legislation designed essentially to eliminate "welfare as we know it"…[policies] that in the strong labor market, succeeded beyond anyone's expectation. There was a remarkable drop in the welfare population and increase in the employment of former welfare recipients.' (Freeman 2001: 24)

What this episode demonstrates is the *preference* for work in exchange for transfers in the choices of the poor, even though government had first to break the logjam by changing the eligibility rules. The majority of industrial country studies of poverty, not just American, take this demonstrated preference for granted. Why in the South African discussion about grants does the suggestion of a positive choice for a work contribution, or the institution of "workfare" over cash handouts, feature hardly at all? This is a puzzle. Is the assumed difference mainly a cultural phenomenon? Or has it to do with labour market institutions specific to each country? Probably both apply, as well as other influences like ethnic, religious and gender divisions.

Certainly, economic inactivity rates for low-income individuals, like "the out-of-school jobless, i.e. those inactive with respect to education as well as the labor market" in the 16-19 year old population, *vary* markedly between the industrial countries. For example, in 1997 this particular measure of inactivity ranged from Japan 1.5% to US 4.5%, Sweden 9.9% and the UK at 10.8%. Other measures show similar large ranges of variation, like the "unemployed" and "jobless" categories defined specifically for estimating the magnitude of inactivity (Ryan 2001: 37-8).

What the ultimate causes of high inactivity are, and by extension why a positive preference for inactivity might exist in a given society, raise questions that extend outside the confines of this paper. But for a perspective on the singularity of the South African proposals – their neglect of a potential preference for work by a proportion of grant recipients who might perceive it as a benefit not a cost - a brief account of the different presuppositions that characterise the American discussion of welfare and workfare makes clear what is at stake. This is additionally relevant because a *participation income* is a variant proposal to a universal transfer that is argued internationally to be much more acceptable politically at the present time – being activity-tested – than the institution of a basic income (Atkinson 1996, Barry 2000, Goodin 2000, 2003, White 2003, Dowding *et al* 2003).

In American society paid work is "a primary source of public respect" (Gutmann 1998: vii), but somewhat paradoxically the raising of children is largely unpaid and not a similar source of status. This high valuation placed on work, or on "productive reciprocity", has a number of key consequences. First, although workfare that meets certain criteria of "fairness" can be more expensive to the state than welfare, it has highly prized advantages. These are (i) meeting the positive preferences of poor people for work in exchange for transfer income, (ii) providing a net increase in personal self esteem, and (iii) obtaining thereby increased public respect for the poor. Second, economic policy needs to pursue or "to devise social institutions that make it possible to economize on altruism and still live tolerably" (Solow 1998: 4), which in the present context means conserving the willingness of tax payers to see their paid revenues spent on other people. Third, the fostering of *mutual* dependency in preference to complete dependency becomes an end in itself in the design of policy. Fourth, the number and proportion of people able but unwilling to work – historically depicted as the undeserving poor, and epitomised by the Malibu surfer in contemporary discussion – are judged to be only a small minority in present day America (Gutmann 1998, Solow 1998).

We certainly cannot generalise these features of workfare and accompanying social norms to the South African policy arena, for a string of reasons that encompass differing political history, prior policies of social support, ethnic heterogeneity in the population, the institutionalised bias by race in the distribution of opportunities and resources, and a range of other causal influences. To take one simple instance, the international literature deems it likely that the strength of the poor individual's desire to work in exchange for received transfers is influenced strongly by the total numbers of the receiving poor in aggregate, and by the fraction they make up of the economically active age ranges of the population. Yet we have neither quantitative nor qualitative information locally about this probable determinant of attitudes to workfare.

Another clear dimension of international difference is that opportunities for paid work are in much shorter supply in the local economy for well-rehearsed reasons. In contrast to industrial country labour markets like the US, our joblessness is structural and chronic more than cyclical. Labour demand is determined strongly by technological change imported from abroad, that is, the skills bias attaching to input intensity, coupled to a preponderance of unskilled amongst the unemployed job-seekers, and a far less promising education and skill profile applicable to the average poor individual. Together these severely inhibit the attraction of net investment to new labour-using spheres of production. This unpromising outlook for net job creation is socially corrosive. But this negative effect is perhaps weaker than in social contexts where paid work is a key source of respect. Second-best substitutes to work for payment, like performance of civic duties and public works construction, will need careful devising. Atkinson (1996) is a widely cited protagonist of such an extended “participation” condition for eligibility.

> ‘In my proposal, the basic income would be paid conditional on *participation.* I should stress at once that this is not limited to labour market participation. While the qualifying conditions would include people working as an employee or self-employed, absent from work on grounds of sickness or injury, and unemployed but available for work, it would also include people engaging in approved forms of education or training, caring for young, elderly or disabled dependents or undertaking approved forms of voluntary work, etc. The condition involves neither *payment* nor *work*; it is a wider definition of social contribution.’ (68-9)

Finally, as a matter of simple arithmetic, if an income grant is instituted without any increase in employment or productive work performed on own account by those not engaged in production, then the burden of re-distributive transfers shouldered by the average member of the economically active population *must rise*. In the long run will this be viewed by the producing individuals as free riding by others, as seems likely in countries like the United States where work performance has intrinsic as well as instrumental value? Or instead will the governing perception be that of benevolence justified by purely moral considerations of a particular kind that lack the expectation of productive reciprocity?

We do not know which of these potential outcomes is most probable in South Africa. The attitude of potential recipients towards work performance in exchange for grants remains a closed black box. But that the pursuit of egalitarian objectives without reciprocal obligations might provoke feelings of resentment that undermine the spirit of solidarity *presumed* to exist in both givers and receivers is a distinct possibility widely canvassed in the broader literature. (White 2000: 513) So it must play a role in policy deliberations. Yet such an adverse outcome is not seriously acknowledged in the advocacy literature arising out of local South African discussion.

[10] Private philanthropy and state-funded grants.

How will the flow of private donations to charities serving the poor respond to the institution of an income grant from the state budget aimed at the poor? Yet again the refrain has to be that we do not know. But we certainly need to know in case there is a significant decline in private giving. This would have to be deducted from the gross resource flow towards the relief of poverty from all sources in estimating what the total available – or *net* – amount is reaching the poor population at any one time.

Discussion in other countries takes it for granted that the reaction of the non-profit sector to increases in public contributions of resources, towards particular activities like welfare and charity, can cause a *crowding out* of private contributions to these activities. "Crowding out occurs when donors feel that their contributions are less needed because of increases in other revenues, or where the character of such revenues make the [non-profit] organization seem less attractive" (Young 1998: 198).

Symmetrically there have been documented effects in the opposite direction, when *decreases* in public contributions to a range of causes have occurred. For instance, in recent years declines in federal government funding of universities and research institutes in the United States have lead to increased solicitation, more private donations and even the inception of commercial transactions involving research results (Weisbrod 1998).

In keeping with the concerns of this paper, one contention in the literature is "that private charity to the poor in the US fell to almost zero beginning in the 1930s, around the same time when large-scale federal support programs for the poor were first implemented…[although] it is difficult to determine from this temporal correlation whether public programs displaced private charity or whether they were instead implemented *in response to* a decline in private support networks" (Jensen 2004: 91, original italics).

In South Africa, the rough equivalent of the non-profit sector is what we term NGOs or civil society organisations devoted to an enormous range of activities, of which charity is a substantial sub-set. But the main question we raise here about the potential extent of crowding out in response to a basic grant policy, concerns not only the responses of established welfare organisations but also the private and informal gifts to the poor which are not necessarily channelled through institutions. There do not seem to be research results from an all-encompassing research net that is needed to provide an answer.

Two final observations about South African philanthropy are worth pondering. First, in contrast to the large-scale corporate providers of social spending, who concentrate on sport and education, it is their smaller counterparts who "spend more on local welfare and benevolent agencies. Small and medium-sized companies are the backbone of local welfare initiatives" (Schlemmer 1999: 5).

How they would react to the institution of a tax-funded universal grant would be highly pertinent to know. Secondly, an important change for the NGO sphere initiated by the new ANC-led governments of the last decade has been the attempt to centralise the receipt and dispersion of development funding, especially that from abroad. How successful this strategy has been for meeting state priorities and for raising the volume of aid flow is a matter of conjecture. What does seem clear is that the NGO sector has shrunk absolutely. Yet whether this policy will be judged overall a success in the long run is difficult to decide given the political dimensions that attach to the question. But if the following suggestion is correct we will certainly continue to need a substantial NGO sector to serve South Africa's heterogeneous population.

> 'The more homogeneous a society is, the more similar are its citizens' preferences, and the smaller the need for nonprofit organizations. In countries with relatively homogeneous populations, such as in Scandanavia, government is sufficient to meet the wants of its citizens for the various collective-type services; thus we find that governments are in fact considerably larger in those countries, while the nonprofit sectors are relatively unimportant. This helps to explain two phenomena that have been widely observed: first, the far greater importance of the nonprofit sector in the United States than in other countries; and second, the growing importance of nonprofits everywhere, as population migration and information flows through television and computers are having the effect of magnifying diversity in country after country' (Weisbrod 1998: 3).

[11] Logistical issues in a basic income policy.

To a number of commentators the successful institution of a regular grant, whether on a monthly or quarterly basis, will hinge decisively on the mundane question of logistical and administrative feasibility. The precedents are not promising. First, at present the combined efforts of the banking sector, the private security industry, and the police have only limited success in controlling the volume of "cash-in-transit heists". Making a much higher flow of cash available throughout the country will probably increase the incidence of losses through crime, although the relationship between cash flows and crime losses might not be proportional. There are claims that provincial officials in departments of social welfare and population development are implicated in cash robberies, for instance recently in Kwazulu-Natal (*Sunday Independent*, 13 March 2005). Second, monthly pension payouts are still not efficiently conducted, even where the work has been subcontracted to the private sector.

Also, the logistical problems besetting payouts of pensions and other grant incomes seem most frequent and intractable in the poorest provinces.

The international literature on basic incomes devotes little attention to these practical issues. Where payment mechanisms are in question the common assumption is that the most advanced technology for cash dispersion can be presumed in place were a grant scheme to be instituted. Whether the presumption of lower costs (in the quotation below) due to the universal – unconditional – character of such a policy would make the overall costs per unit of transferred income lower than a conditional scheme would is entirely conjectural. But that is not the main point here, which rather concerns the realism of assuming the most up-to-date technology would be affordable and workable in South African conditions.

> '[Transfers] are reallocations of purchasing power. This does not mean they are costless. They do have a distributive cost to the net contributors, and they do have an economic cost through the disincentives they create…In addition, there are administrative costs. But, as also pointed out earlier, assuming a computerised and efficient tax-collection and tranfer-payment technology, these are likely to be lower under a universal, ex ante scheme than under a means-tested ex-post one, at least for a given level of effectiveness at reaching the poor' (Van Parijs 2004: 20).

[12] Conclusion: wishing will not make it so.

If persistence and commendable intentions were the only criteria for deciding on good public policies then a basic income grant proposal would have won the day by now. A fair number of individuals as well as groups like the BIG Coalition subscribe to the view that an income grant will assist the South African poor *more* than will any other policy instrument of equivalent cost that might be devised.

This paper argues that such a conclusion is wholly premature. It is not supported by research that poses the questions outstanding, and therefore universal grant advocacy presents few answers that bear unambiguously one way or another. At this stage in policy formation we are in the realm of tentative judgement and not evidence-based conclusion. Many people are in favour of redistribution on grounds of social justice, including adherence to the moral basis of human rights for all citizens. But that does not entail commitment to any specific policy action. The basic income grant proposal is an example of "misplaced concreteness", in that it opts for one mode of transfer to the poor to the exclusion of all alternative modes. As members of a moral community, what we owe one another is not simply money, "not the means to generic freedom but the social conditions…the rights, institutions, social norms, public goods and private resources that people need to avoid oppression (social exclusion, violence, exploitation, and so forth) and to exercise the *capabilities* necessary for functioning as equal citizens" (Anderson 2000: 1, italics added).

In accordance with this conception of the poverty problem, a major theme of this paper has been that an investment perspective is essential for clarity of thought about policies of escape by poor individuals. That it is missing from the majority of writings that urge the institution of a basic grant in South Africa is regrettable. We speculated earlier that it might be a consequence of the single-minded concern with the universality of access deemed to be an absolute precondition for any and every increase in resource transfers to the poor. That contrasts markedly with the set of conditionalities that characterised poverty programmes under the old regime, and provided scope for discrimination as the essence of apartheid. Because of black political subordination, a great deal of arbitrariness, inefficiency and personal humiliation accompanied many transfer payments. But this suggestion of an exaggerated reaction against past practice by grant protagonists is a conjecture and no more at this stage of the research.

Whatever the true reason, one consequence is that advocacy arguments blur the distinction between transfers aimed at the *relief* of poverty and transfers intended to facilitate *escape* from poverty. Commonplace though it may be, this distinction is the key to clarity of thought about choices between anti-poverty policies. As a thought experiment, if a basic income grant were put in place now, and twenty years down the line the same proportion of the population were judged in relative and absolute terms to be in poverty, would the programme be assessed as having been successful? Consistent with BIG arguments the answer would have to be *yes*, because there was less deprivation and suffering in the interim period. Yet many other people concerned with poverty would be inclined to say *no,* because the magnitude of the problem remains just as large as at the commencement of the policy.

A final remark is that untapped altruism amongst the rich is presumed by many basic grant proponents in South Africa. Yet for consistency they need to make the even stronger presumption that the existing solidarity is so robust – there are such surplus reserves of altruism amongst tax-payers – that an income grant policy that raises the tax burden will not erode solidarity. So it is deemed politically feasible in South Africa.

One searches in vain for evidence-based arguments in support of either these premises. They go entirely in the opposite direction to what is judged to be realistic in international discussion of redistribution actions, and thus what is deemed to be feasible in shoring up the welfare state in industrial countries. There the reciprocity principle is alive and well on *both* sides of the transfer relationship between payers and receivers. That alone should make us pause when faced with the demand for a universal, unconditional and indefinite payment institution.

We have argued that a move to a grant paid to all citizens – or to the wider class of all inhabitants in line with a recent Constitutional Court ruling confirming access to rights for legally resident foreigners in South Africa – will require a major transformation in social attitudes and economic structure. There is no sign of that likely to come about without social tensions and economic disruption. But no protagonist of the grant appears to be pursuing the research outlined in this paper to make informed decisions on the range of issues that inhere in the policy they propagate. On the contrary that seems to us an essential pre-requisite for rational decision-making.

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