Minimum Income Guarantee

Position Paper

Christopher Wood

28 July 2021

What is a PolicyLab position paper?

PolicyLab Position Papers are short research documents that propose a specific policy or intervention. Unlike longer research papers or analytical applications, Position Papers do not include detail such as background research, literature reviews, or data analysis; but summarize work from related projects in a simple narrative form. Position papers ask a standard set of six questions, namely: what is being proposed, why is it needed, how much would it cost, how would it be administered, what would the impact be, and why this policy rather than alternatives. Each question can be read in isolation from the rest of the paper.

What is being proposed?

A Minimum Income Guarantee (MIG) is a universal cash grant that would be available to all adult South Africans. Unlike the more well-known Basic Income Grant, the MIG is a conditional grant, in which only those earning under a specific threshold will qualify. For those earning under the threshold, the MIG is calculated as the value needed to 'top-up' your current earnings to the level specified by the MIG. For example, a MIG set at R2000 would distribute R500 to someone earning R1500, would distribute R300 to someone earning R1700, and would distribute R2000 to someone with no earnings.

The MIG can be thought of as a national minimum income that is guaranteed by the state. In principle, the value of the MIG should at least cover the basic amount needed to afford essential goods, or the closest we can get to this figure given political and fiscal limitations. The level at which the MIG is set would be the base earning that every South African could be sure they would receive every month. We recommend that the MIG is initially fixed at R1286 per month, which would cost the state approximately R46 billion annually.

The earnings considered under the MIG would include all taxable income, whether from wages or other earnings, and would include welfare payments. In-kind payments, such as parents supporting their children or gifts from friends, would not be considered income. As discussed below, the MIG could best be implemented by distributing unvalidated payments made on request on a monthly basis, while auditing claims for compliance on an annual basis. Incorrect claims, overpayment, and any appropriate penalties would then be charged as part of tax assessments during the usual annual tax cycle. MIG disbursements would be administered by SASSA, while auditing of MIG payments would be governed by SARS.

Why is it needed?

The unrest that gripped KwaZulu-Natal and Gauteng in July 2021 has brought the long-running debate around improving social protection in South Africa to the fore of national discussion. Regardless of the root cause of the unrest, the pace and scale at which it spread speaks to the depth of South Africa's historic deprivation and inequality. Mapping the unrest against measures of economic wellbeing (such as unemployment and earnings) shows the worst instability being concentrated in the poorest urban areas.[i] While the protests quickly faded, the underlying economic conditions and the anger and deprivation they breed have not, and will not until progressive policy helps develop a more just and equitable society.

The case for universal cash grants in South Africa has been made extensively by civil society groups such as the Institute for Economic Justice[ii], Black Sash[iii], and the Studies in Poverty and Inequality Institute[iv]; and the best way to explore this case is to read their work. Instead of recounting the full argument here, we'll focus on five core reasons for universal cash grants: meeting the basic needs of the vulnerable, stimulating economic growth, building economic resilience, improving economic mobility, and ensuring social stability.

Basic needs

Basic, universal income support's most immediate impact would be to realise the objective of decent living conditions for millions of South Africans. A basic grant would dramatically alleviate food insecurity and provide for basic needs like housing and transport, while a more ambitious grant would create the conditions needed for the most vulnerable households to find and realise opportunities like jobs and education. The foundation of a just society must be the knowledge that any given person passing on the street has fair access to the basic necessities – and universal income support is the best way to provide this.

Stimulus impact

But the impact of universal income support is not limited to grant recipients. Basic income grants can have a powerful stimulus effect on economic activity, putting money into the hands of people who are likely to spend in a way that recirculates grant money through the economy.[v] This argument is particularly true for South Africa, where employment remains concentrated in sectors that are directly linked to the wealth of households, such as retail. Universal income support can help the country escape the serious economic impacts of COVID-19 and, in the longer-term, act to stabilise weak growth rates.

This demand-side stimulus is complementary to long-term, supply-side development efforts. Income support helps improve education outcomes (by improving learning conditions for vulnerable students), provides for stable growth conditions that are essential to supply-side support measures like infrastructure development and investment attraction, and creates a larger domestic market to anchor productivity-centric growth strategies such as export expansion and investments in new technologies.

Future resilience

Early adoption of universal income support can also be a vital preparatory step towards the future of work. Advancements in technology and productivity have already dramatically reduced the labour requirements of most forms of production. Farms and steel mills that once employed thousands can now do similar work with a handful of people, and this trend is only likely to accelerate as improvements to digital technologies expand the scope for automation. The capacity of economies to adopt new technologies will be directly contingent on their ability to assist those whose jobs are lost. Building a functional support system can better position South Africa for the smooth adoption of the types of technologies that keep the country competitive – while ensuring a fair distribution of the fruits of these gains.

Economic mobility

Perhaps the most significant argument for universal income support is the impact it has on economic mobility. Extensive research in the last decade has shown that the earnings of parents is the largest determinant of the future earnings of their children. In a sense, everyone is born with an Opportunity Horizon set ahead of them. This horizon extends when parents' income increases, when the state offers support like free education and healthcare, and when economies have an accessible distribution of jobs along the earnings curve. These three considerations are extremely challenging for South Africa – where income inequality is extremely high, state services often fail the poorest, and jobs are concentrated on either side of a missing middle of accessible, decent-paying work.

In theory, having good quality schools, hospitals and economic policy would likely have a greater impact on expanding the Opportunity Horizon than direct payments. But given the deep, entrenched institutional problems facing all our key public services, as well as complex structural challenges to building a job-rich economy, the most effective way to speed up economic mobility is simply to make poor households richer – and universal income support is an excellent way to do so.

Social stability

As highlighted by the July 2021 unrest, universal income support can also help manage the extremely challenging question of South Africa's long-term social stability. With the world's highest levels of inequality, a history built on division and violent exclusion, continued physical segregation and marginalisation, a predatory political class, and slow rates of growth and development – there is every reason to believe that South Africa will face mass civil unrest in the coming decades. The form and magnitude of this unrest is, of course, uncertain, but it remains hard to believe that significant instability can be avoided unless there is substantial material change to the lived conditions of the majority of South Africans.

Minimum income support can act as one vital stabiliser against this volatility. While developing an economy and society that fairly distributes a rich set of opportunities remains the ultimate aim, every available approach to achieve this level of development will take decades, and the immediacy of universal income support can help bridge the gap between long-term development and the extremely pressing demands of the less fortunate. Beyond the human necessity of avoiding this instability, the stabilising effect of universal income support should appeal to the most basic economic logic. Even the relatively isolated unrest of July was estimated by the Presidency as costing the country R50 billion over a single week – R4 billion more than the annual cost of a R1286 minimum income grant. If a MIG avoids one week of unrest every year, it pays for itself.

Other benefits

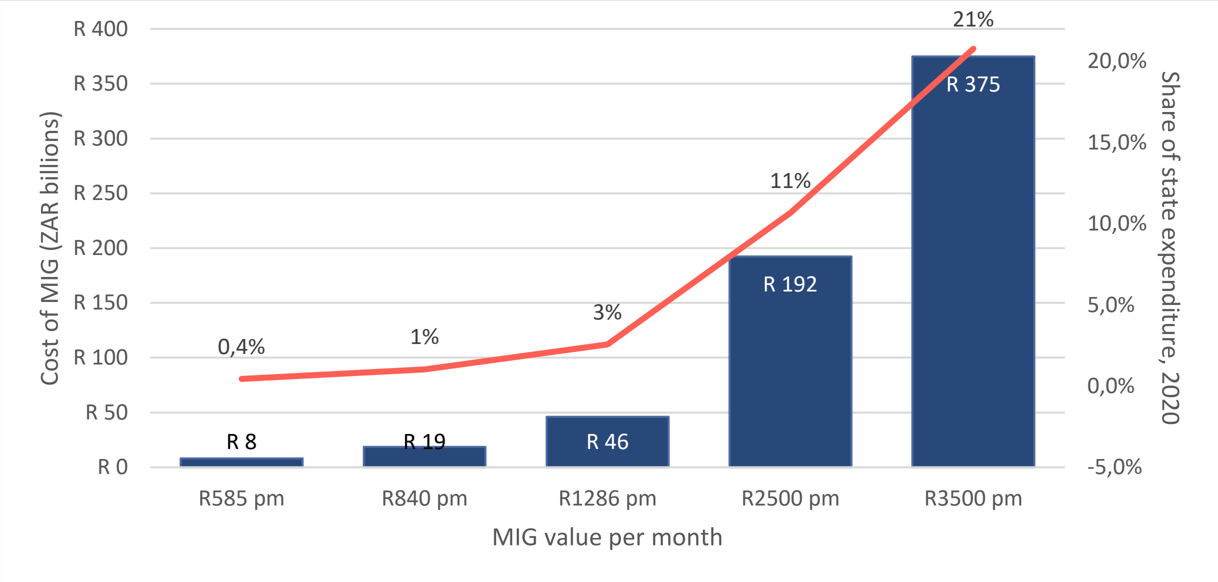
A shopping list of additional and ancillary benefits could be rolled out for universal income support. Income support provides workers with the bargaining power needed to fairly negotiate with employers, and provides freedom and choice to vulnerable people living in abusive households. Income support provides for healthier families, and can improve rates of political participation and government accountability. And, in the case of approaches like a Basic Income Grant – but not a Minimum Income Guarantee – universal cash support can actually help reduce the cost of administering complex conditional welfare payments.

There is no doubt that income support comes at a very high cost. Funding the system will be expensive and administering it will be very difficult. But the potential of a policy that provides for basic justice for the vulnerable, and a pathway to development for everyone else, is too great to be ignored. The debate on income support in South Africa must be on how to practically implement it, and not on whether it is needed.

How much would it cost?

Universal grant schemes are typically very impactful, but also very expensive. MIG is no different. The direct cost of MIG varies depending on the level at which the guarantee is set. For the most commonly discussed values for a basic income guarantee, the MIG would cost between R8 billion (for a R585 grant per month) and R375 billion (for a R3500 grant per month) – or between 0,4% and 21% of existing government spending, respectively. The basic costing of MIG can be found in Figure 1 below.

Figure 1: Estimated costs of MIG, direct costs and direct costs as a share of state expenditure (2020)



In addition, MIG would be complex and expensive to administer. While we propose using existing institutions (like tax and welfare records) to offset some of these complexities, the MIG would still be notably more expensive to implement than a comparable basic income grant. The cost of the administration of MIG is complex to calculate, and would be dependent on the details of the system adopted by the state. To use an unscientific estimate, assuming the MIG would add 20% to the current costs of administering social grants (a high benchmark), it could be assumed the policy would cost approximately R1,5 billion to implement.

The challenge posed by the large cost of MIG should not be underestimated. South Africa is already operating in a highly constrained fiscal environment, with limited room for new taxes to help offset the cost of the guarantee. Few easy answers are available. The frequently made point about simply cutting down on irregular spending and corruption is of course true in principle, but could not be implemented quickly, and would rather be the project of decades of institutional development, which would likely not result in the savings suggested (given that irregular expenditure is not the same as wasteful or corrupt expenditure).

Despite this, extensive work has been completed by research organisations like the Institution for Economic Justice (IEJ)[vi] and DNA Economics[vii] on potential costing strategies for the more ambitious Basic Income Guarantee – which include ringfenced income taxes (a social security tax) and a resource rent tax. Given the National Treasury's aversion to both ring-fenced taxation and new taxes of any type, these would be challenging to implement, but appear otherwise viable. In the case of the MIG, the base level of R1286 could be largely funded by a broad Financial Transaction Tax, which would likely be the best available option to fund the MIG without placing large costs on the middle class.

Perhaps more significant than the actual economic cost, is the role that very high costs play in passing a policy like MIG through the vested institutions and political interests that comprise policymaking in South Africa. The National Treasury has proven committed to austerity even in the face of some of the sharpest economic downturns in South Africa's recent history. The institutional and political dimensions of South Africa's budget conservatism mean that a universal income grant could not be implemented without aggressive opposition and an inevitable compromise (with which none of the purists would be satisfied). Given its more manageable costs, MIG could be a useful middle ground between advocates for a basic income grant and those holding the purse strings.

How would it be administered?

Implementing the MIG would be complex. Welfare payments that are based on need are among the most difficult and expensive to implement, because of the challenges involved in verifying information and managing non-compliance. MIG would be more complex and expensive to administer than BIG, and more complex and expensive than most existing grants, which tend to be based on non-financial considerations (like age or number of children) that are easier to verify.

In addition to the verification challenges, there is a timing challenge involved in the MIG. In theory, a recipient's income 'top-up' should happen at the same time as their income shortfall, otherwise the grant is not providing the minimum income level to which is aspires. This poses a number of complications. For example, someone with seasonal work may be under the threshold one month, and over the next. Payment in the second month might not be helpful to manage the previous month's shortfall. Some of these practicalities are unavoidable, and private sector solutions like short-term loans may be needed to allow individuals to properly match their needs to the capacity of the state bureaucracy.

In general, three models for implementing the disbursement of MIG are possible: annual-disbursements, monthly-at-a-lag, and declare-and-audit (which is the recommended approach).

Annual disbursements

Annual disbursements would involve calculating the MIG on an annual basis. Disbursements could then happen in a lump sum, potentially during the lean January period, or be broken up into monthly payments throughout the next year. The benefits of this approach include it being the easiest to implement, and that it captures the most accurate picture of the shortfall, because it is calculated on an annual basis. But it is clearly not the best for those who need immediate support. The long lead-time in receiving disbursements could be difficult to manage for the most vulnerable, and we could see money being distributed at exactly the moment at which it is no longer needed.

Monthly-at-a-lag

Monthly-at-a-lag disbursements are more complex to implement, but would reduce the time between when money is disbursed and when money is needed. The challenge, of course, would be that verifying income for the month would be complex. Without the annual cycle of tax returns to refer to (discussed below), recipients would have to prove their shortfall through cumbersome methods like submitting bank statements that officials would manually validate. It is questionable whether the complexities involved in managing monthly evaluations would even be possible in the timeline involved, particularly given the poor track record of institutions such as SASSA.

Declare-audit

Given these complexities, the recommended approach is declare-and-audit. Under this system, recipients would be able to declare a shortfall and be paid out monthly without any verification of their actual earnings. However, at the end of the year, all declared shortfalls would be evaluated against tax and welfare payment records, and any overpayments that resulted from misdeclarations would then be payable by the recipient as an additional cost on their tax bill for the year.

This should immediately raise red flags. This approach has high risks for recipients who don't fully understand the system, or who make mistakes. They could easily find themselves facing punitive charges at the end of the year that reverse the gains of the MIG, and potentially leave them in debt and/or with a tax violation against their name. Significant tolerance for loss will have to be built into the system, and the state will be taking on large risks in adopting this approach. The dependence on self-declarations for initial payments could make the system vulnerable to fraud. All of these risks are legitimate and, given the administrative constraints of the South African state, are likely to occur.

Despite these challenges, declare-and-audit is the best available option that balances the complexities of assessing MIG payments against the immediacy of the need among recipients.

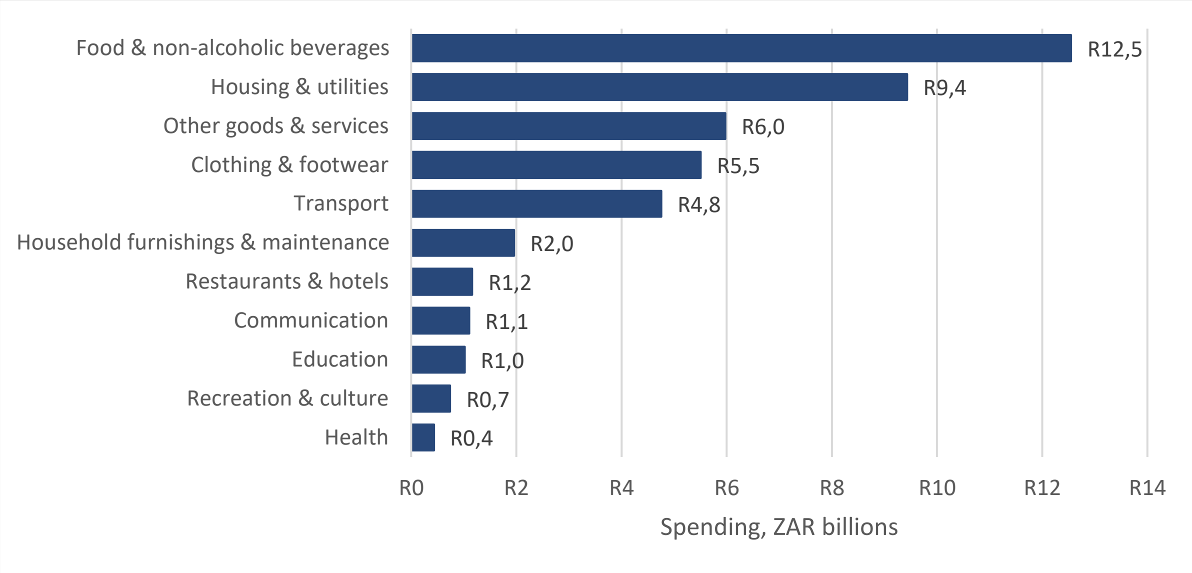
Declare-and-audit allows for enforcement and oversight of the MIG to fit into existing institutional arrangements. In particular, SARS would be well placed under such a system to be the principal oversight body for the guarantee. Existing annual tax assessments could be quite easily adjusted to consider the MIG as a source of income that is 100% deductible in the right circumstances (when income is below the threshold) or faces an absolute 100% tax (or higher for penalties) in cases in which it is non-compliant. SARS's existing payment, dispute and debt-management systems would similarly be well placed to manage the process of reconciling undue payments under MIG.

While MIG would not fix the multitude of problems at SASSA, the disburse-and-audit approach would play to what does work in the existing system. Because the verification stage is removed and placed in the hands of SARS, SASSA would simply have to focus on receiving applications for MIG shortfalls, and disbursing funds. This is primarily a customer service function, that would be complex to implement but would benefit from the networks of focal points (like SASSA and Post Offices) that already exist in the social security system.

What would the impact be?

In the short-term, it is expected that almost all of the spending on a MIG (or similar welfare measures like BIG) would be recirculated into the economy. Without conducting formal assessments on the impact, a rough estimate indicates that annual GDP would be expected to grow by between 0,99%[viii] and 2,1%[ix] for a MIG of R1286 per month. Considering the spending behaviour of MIG recipient households, an overview of the sectoral distribution of fist-order impacts can be found in Figure 2 below.

Figure 2: Estimated additional spending by recipient of a R1286 pm MIG grant[x]



The short-term expansionary impact is impressive, the real impact of MIG would be in the impact it has on inter-generational economic mobility.

There is a preponderance of evidence that the conditions of your birth define your likely future income and living conditions. As detailed above, everyone is born with a horizon of opportunity – defined here as the increase in lifetime income an individual is likely to experience over their parents. The state can have an immense impact on extending the horizon of opportunity. Interventions like free education, state healthcare, housing support, and of course welfare payments collectively lower the bar for achieving economic advancement, and increase the spending power of parents, and in so doing unlock better opportunities for their children.

Simplifying greatly: the more money this generation has to spend, the more money the next generation will be able to earn.

Whether the impact of the additional income is direct (such as helping pay for school fees), indirect (such as by relieving some of the stress in the household that poorer students have to contend with), or even secondary (such as by being spent on a visit to the movies that inspires some ambition in the watcher) – richer and more financially stable households are better placed to give their kids a better life, and MIG is well placed to make households richer and more financially stable.

The MIG will have some negative impacts. The most direct is the cost of financing the policy. Assuming a financial transaction tax is adopted, these costs would not be very significant, given the extremely high margins seen in the financial sector, and the relatively weak impact of non-banking finance on the lives of ordinary South Africans.

However, the MIG is expected to be significantly disruptive for labour markets. While there is virtually no evidence that welfare payments discourage work in South Africa, MIG likely would disincentive some work - because those currently earning less than R2000 a month would be able to earn more by not working. This is a complex challenge that would require careful evaluation, but the disruption is ultimately by design. As discussed below, the last two decades have seen a drastic erosion of the share of earnings going to workers, which has closed off many pathways to social progress for a generation of South Africans. A key secondary aim of MIG is to address this imbalance, by providing significant bargaining leverage to low-wage earners, and by working alongside statutory initiatives like a National

Minimum Wage to improve earnings. Many challenges will still need to be overcome, such as managing the impact of the MIG on sectors like agriculture and domestic work that rely on low-paid, part-time work.

Why this rather than alternatives?

A number of alternatives to MIG are available, including an expansion of existing welfare benefits and (from one perspective) not expanding the welfare system, and instead concentrating state resources on the likes of infrastructure investment or lowering tax rates. But perhaps the most obvious alternative to MIG would be the more widely discussed Basic Income Grant (BIG). While a number of BIG proposals exist in South Africa, including many that cover similar ground to MIG. The critical difference between these two policies is that everyone would automatically qualify for a Basic Income Grant, regardless of factors such as income.

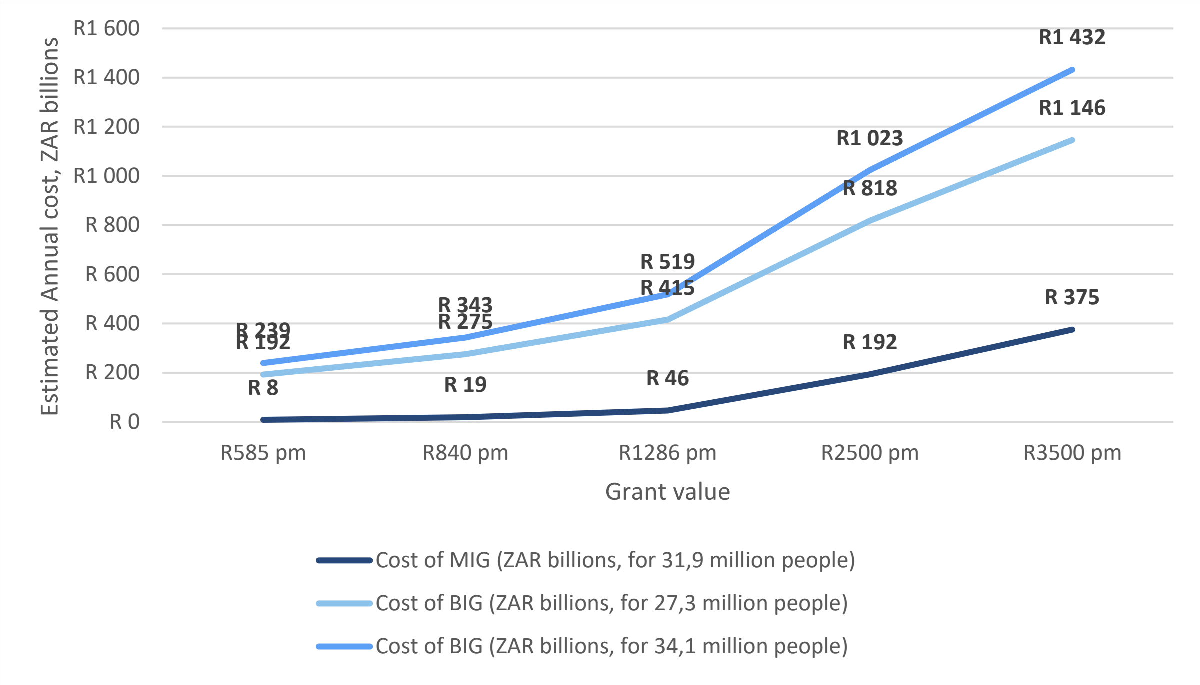
A Basic Income Grant would be a transformational policy and would have enourmous benefits for South Africa as a whole. Nothing in this paper should be read as a repudiation of the basic principles of BIG, and in many areas a basic income grant outperforms a minimum income guarantee. To give a few examples: BIG is much easier and probably cheaper to administer (because you avoid the complexities of deciding who qualifies), BIG of course has a far wider reach and avoids unfairly excluding deserving recipients, and BIG is less likely to create distortions in the labour market (because it remains constant regardless of whether you choose to take a new job).

It is altogether possible that BIG would be a more effective approach to take and, in the author's view, the balance of benefits between the two is only marginally tilted towards MIG. However, three considerations make MIG our recommended approach.

First, and most importantly, it is difficult to believe that a basic income grant will ever actually become official government policy. While there is clearly growing support for BIG, the incredible cost involved in a basic income grant of adequate scale would require coordinated, committed change across the entirety of government. The proposals for funding a BIG of only R586 per month would require dozens of major tax and other policy changes, each of which will be individually resisted, and all of which will need to be implemented by a government that stopped a paltry R350 Social Relief of Distress Grant during the worst economic crisis in recent memory. Advocates for BIG do heroic work in championing the policy, and their success would benefit everyone, but it is hard to believe they will succeed. MIG will be less impactful, but it comes with a much more manageable price tag, and thus with much greater potential to be adopted as policy.

Second, while in theory there is no hard or absolute constraint on what value a MIG or BIG could be set at, the practicalities of policymaking and state financing in South Africa mean that (assuming either are implemented) a minimum income grant is likely to be set at a higher value than a basic income grant. Because MIG is cheaper, for a given allocation from the Treasury, MIG would provide larger payments to a smaller group, rather than BIG's smaller payments to a bigger group.

Figure 3: Comparison of annual costs, MIG[xi] vs BIG[xii]



The size of these payments matter, because very low grant values are likely to be substantially less impactful in helping families make important investments in social goods like education, healthcare and job searches. While BIG payments would certainly help with these costs, the quantum of disenfranchisement in South Africa is such that most of a relatively small transfer would go towards meeting basic needs. That is an incredibly important contribution to make, but it has less of an impact in breaking families out of cycles of poverty.

If BIG were to be issued at a suitably high value, it could easily avoid all of these problems and make an even greater contribution towards economic mobility. Realistically however, it seems inconceivable that the vested resistance in core parts of the South African government, most notably the National Treasury, would accept a BIG that is anything but a nominal payment on par with the R350 Social Relief of Distress Grant. It is altogether possible that MIG falls to the same challenges, but the odds are better that a minimum income guarantee could achieve larger payments than could be achieved by lobbying for BIG.

Third, MIG has the potential to force change in the labour market. One of the arguments often raised in favour of BIG is the way in which it avoids disrupting labour markets. Workers are given some cover for their expenses, which improves their bargaining power, but in general the BIG is unlikely to undermine willingness to work or impose higher wages on companies. This is not true for MIG. Because your earned income is deducted from the minimum income guaranteed by the state, there is an absolute disincentive to accept work that pays less than the MIG. A worker offered a job that pays wages lower than the minimum would earn the same amount if he or she stayed home and did nothing.

While this will raise red flags for the usual critics of welfare systems, it is by design. Redistribution by the state is a vital avenue to fight surging inequality, but it is inadequate. The decades-long decline in the share of income earned by workers must be reversed in order to control inequality. This is particularly so given the apparent complete inability or unwillingness of governments to fairly tax high earners and corporate profits.

A MIG would help counteract this trend by offering individuals substantial bargaining power to demand fair wages. It would directly undermine the power imbalances currently enjoyed by companies, which allows some to offer low wages because of an oversupply of unemployed South Africans. These wages would now be inadequate because they would be competing with MIG, rather than with the desperation of the vulnerable. The net result would be that MIG sets a floor on income that is more effectively enforced than alternative arrangements, like a regulated minimum wage. By doing so, the MIG would force employers to offer enough for their workers to meet their basic needs.

---

[i] Christopher Wood, Devi Pillay, and Brandon Almeida, *Unrest Map* (Johannesburg, South Africa: PolicyLab.app, n.d.), www.policylab.app/desktop.

[ii] Institute for Economic Justice, "Introducing a Universal Basic Income Guarantee for South Africa: Towards Income Security for All," Policy Brief, Social Protection Series (Johannesburg: Institute for Economic Justice, March 2021), https://www.iej.org.za/wp-content/uploads/2021/03/IEJ-policy-brief-UBIG_2.pdf.

[iii] Engenas Senona and Black Sash Research Convening Committee, "Basic Income Support: A Case for South Africa" (Mowbray, South Africa: Black Sash, 2020).

[iv] Isobel Frye, "The Budget, Social Security and the Basic Income Grant Alternative," AIDC Analytical Paper (Johannesburg, South Africa: Studies in Poverty and Inequality Institute, March 30, 2020).

[v] Christopher Wood, *Decency Index* (Johannesburg, South Africa: PolicyLab.app, n.d.), www.policylab.app/desktop.

[vi] IEJ, "Financing Options for a Universal Basic Income Guarantee in South Africa," Social Security Policy Brief (Johannesburg, South Africa: Institute for Economic Justice (IEJ), July 2021), https://www.iej.org.za/wp-content/uploads/2021/07/IEJ-Policy-Brief-Financing-a-UBIG.pdf.

[vii] Fouche Venter et al., "Universal Basic Income Guarantee: Financing Options Analysis" (Pretoria, South Africa: DNA Economics for the Institute for Economic Justice, July 8, 2021), https://www.iej.org.za/wp-content/uploads/2021/07/DNA_UBIG-Financing-Options_Final-report.pdf.

[viii] Assuming multipliers estimated by Schroder, E. & Servaas, S. (2020). "Fiscal Policy in South Africa: Closed Input-Output Income and Employment Multipliers"

[ix] PolicyLab Interconn estimates based on StatsSA Input-Output Tables (2014-15).

[x] PolicyLab, "PolicyLab Calculations Based on StatsSA Living Conditions Survey 2014-2015, Adjusted by CPI," July 2021.

[xi] PolicyLab.

[xii] Institute for Economic Justice, "Introducing a Universal Basic Income Guarantee for South Africa: Towards Income Security for All."