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Elaborate scaffolding, weak foundations: Business–government relations and economic reform in democratic South Africa

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Abstract

This paper explores the evolution of the business–government dimensions of South Africa’s democratic political settlement. It details how and why market-based reforms were embraced by both political and economic actors in the 1990s as part of a broader commitment to a rule-bound political settlement. It explores two aspects of the subsequent play of the game: the rise and decline of a ‘corporatist’ elite bargain; and the evolution of initiatives to foster black economic empowerment. Overall, rule-bound, disciplining reforms were embraced more readily than pro-active initiatives to build capability. The result has been that South Africa became mired in a combination of economic stagnation and the strengthening over time of forces antithetical to market-based reform.

Keywords: business-government, industrial policy, rules, deals, industrial policy, corporatism, Black Economic Empowerment, patronage

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I: Introduction

The exuberant optimism of the early 1990s, in South Africa and around the world, has curdled. South Africa's seemingly miraculous democratic political settlement – and, more broadly, the third wave of democratization, which witnessed a doubling in the number of countries classified as democratic from 60 in 1984 to 120 15 years later – seemed to signal a renewed, hopeful political order globally. A quarter of a century later, hope has receded, leaving a bitter, angry residue.

Disappointment has come with special force in middle-income countries (MICs). In the 1990s, MICs seemed to be offering their citizens the promise of a rising tide of affluence, of a better life for all. But, by 2016, many had become mired in a middle-income trap of stagnating incomes, high inequality and political polarization, from which there seems to be no escape – with the cause of the trap traceable to political economy, rather than narrow economic considerations.

A shift in perception as to the place of business in the political economy of the MICs has accompanied these changes. In the hopeful years, increases in private investment, and in the productivity of business were seen to be key to the realisation of economic potential – and a progressive business class was perceived to be integral to the political coalition that would midwife this thriving, globalised future into being. But, as of 2016, business increasingly was perceived to be part of the problem – intertwined in a corrupt embrace with political elites that was a root cause of stagnation and inequality.

What is perception, and what is reality? Were the hopes of the 1990s based on flimsy evidence and false premises? Is the cynicism of 2016 overdone? Or perhaps things have changed over time, with both the hopes and cynicism grounded in changing realities? This paper explores these questions for South Africa. It is part of a broader comparative analysis of the political economy of business–state relations in five middle-income countries -- including also Turkey, Mexico, India and Egypt – and undertaken under the aegis of the DFID-funded *Effective States and Inclusive Development* (ESID) research programme.

For all five countries, the research uses a 'political settlements' lens to explore the political economy drivers of the embrace in the 1980s and/or 1990s of market-based reforms and their subsequent (at least partial) reversal, with particular emphasis on the role played by business along the way. All five studies interpret 'market reforms' broadly to characterise a growth agenda which includes a variety of market-friendly government initiatives (including active industrial policy) that actively support the re-orienting of an economy in a more productivity-oriented direction.

The central conclusion of this paper is broadly as follows. In the 1990s, South Africa's market-based reforms were embraced by both political and economic actors as part of a broader commitment to a rule-bound political settlement. However, for all of the seeming support, rule-based, pro-competitive reforms were not underpinned

by powerful interests with the commitment and authority to sustain them in the face of a loss of momentum, and of rising pressures for reversal. Further, drilling down into the details of the reforms reveals that influential stakeholders were more willing to embrace some aspects of the market-based reform agenda than others. Paradoxically, there was an early critical mass of support for action on the ‘disciplining’ dimensions of the reform agenda, with a weaker (and progressively declining) embrace of those aspects of reform that provided pro-active support for building the capabilities needed for global competitiveness. The result of the policies and the broader political environment has been that, instead of setting in motion a sustained virtuous circle of rising productivity and competitiveness, South Africa’s political economy is seemingly mired in a combination of economic stagnation and the strengthening over time of forces with interests antithetical to market-based reform.

The paper proceeds as follows. Part II sets the stage, with an overview of South Africa’s disappointing economic performance in the two decades of democracy. Parts III and IV explore analytically and historically some key reasons for the disappointing economic performance. Part III focuses on some inherent limitations of the political settlement and economic reforms put in place in the 1990s. Part IV examines two key aspects of the subsequent ‘play of the game’ in the wake of the initial burst of reform: the rise and decline of a ‘corporatist’ elite bargain encompassing business, government and labour; and the evolution of initiatives to foster black economic empowerment; and trends in inequality, poverty and the transformation of the middle class. Part V analyses broadly how the patterns of business–government relations, together with some broader structural patterns of poverty and inequality, have, over the past two decades, progressively reshaped South Africa’s political settlement along increasingly contested lines (including a rise in patrimonialism). We find that, paralleling other middle-income countries, South Africa’s political settlement has arrived at a point of inflection.

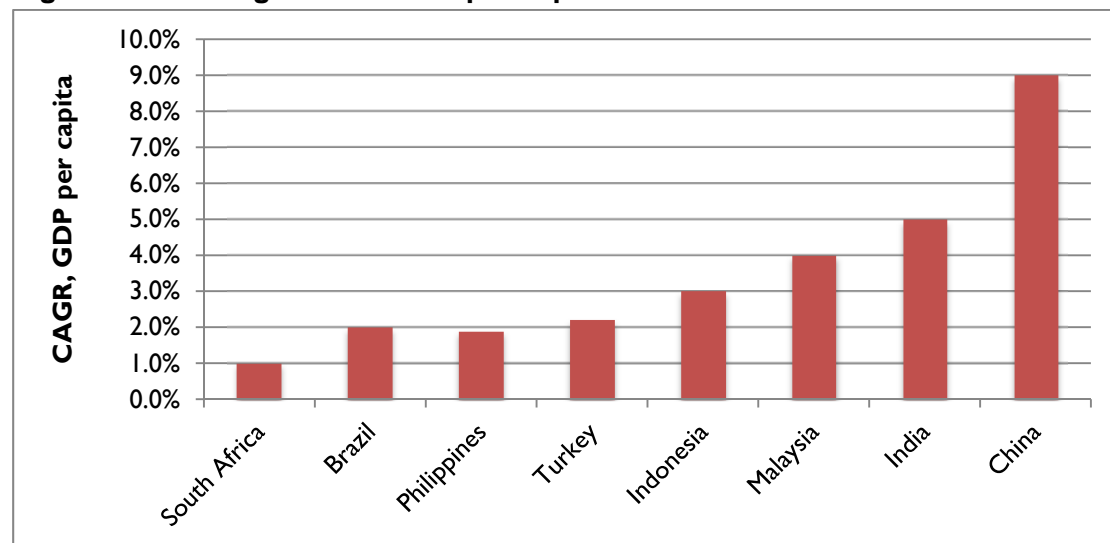
II: Growth, investment and productivity in post-1994 South Africa

As explored in detail later in the paper, accompanying the onset of democracy South Africa embarked on a far-reaching process of re-integration into the global economy. Insofar as this re-integration also involved liberalisation of trade, there inevitably were losers as well as winners. At the outset of the process, the hope was that the combination of a rule-bound reincorporation of the country into the global economy and social democratic/welfarist measures to spread economic benefits more broadly would unleash rapid, inclusive and productivity-oriented growth. However, as the data in this section show, more than two decades into democracy, it is evident that these hopes have not been realised.

Economic performance improved immediately in 1994 and, in spite of some volatility, achieved an average growth rate of over 5 percent per annum between 2004 and 2008, better than for any period since the 1960s. This was driven in part by the removal of sanctions, the normalisation of international relations, some broadening of

the middle class, and increased confidence by the 2000s. But growth was also propped up by a boom in consumer credit and the effect on export prices of the commodity super-cycle that followed China's accession to the WTO in 2002. The global financial crisis of 2008 brought both the credit boom and high commodity prices to an end and plunged South Africa into recession. The unemployment rate, which had declined from more than 32 percent in 2002, having declined to 21 percent in 2008, rose sharply. Economic performance in recent years has been very poor, exacerbated by weakening confidence. Overall, as Figure 1 shows, between 1990 and 2013 South Africa's per capita GDP growth has lagged that of other middle-income countries.

Figure 1: Annual growth of GDP per capita between 1990 and 2013



Source: Bhorat et al. 2014.

Low growth has been accompanied by low investment, underperformance in export markets, and deindustrialisation. Figure 2 contrasts South Africa's investment performance with that of other middle-income countries (and also South Africa's investment performance from the mid-1960s to the mid-1980s). Private sector gross fixed capital formation consistently exceeded 20 percent in the 1960s and early 1970s. However, after peaking at 30 percent in 1976, it fell steadily to 10 percent in 1993, after which it stabilised at a low level of between 10 and 15 percent for the post-1994 period, peaking at 16 percent in 2008. Public investment also peaked in the 1960s and 1970s, slowly rising again in the second decade of democracy. Total gross fixed investment has breached 20 percent sporadically since 2007, but levels remain mediocre. The South African economy also has remained relatively closed – exports are a sharply lower proportion of GDP than for almost all of the other middle-income comparators in Figure 3.

Figure 2: Private investment share of GDP

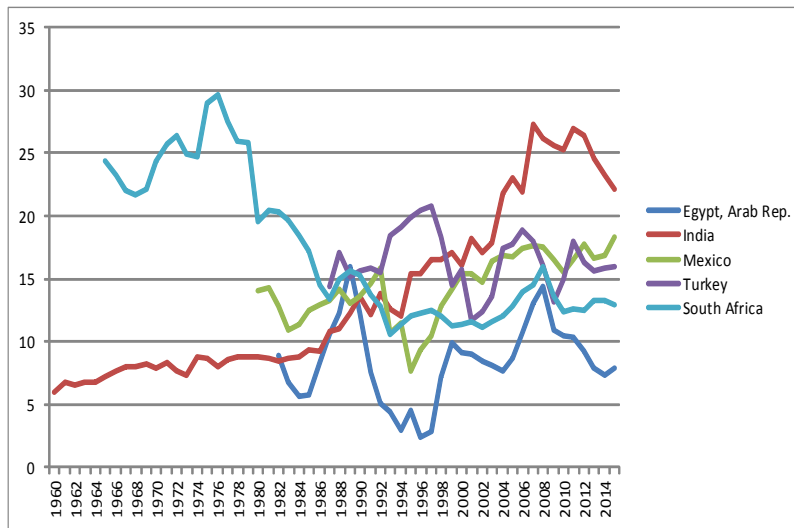
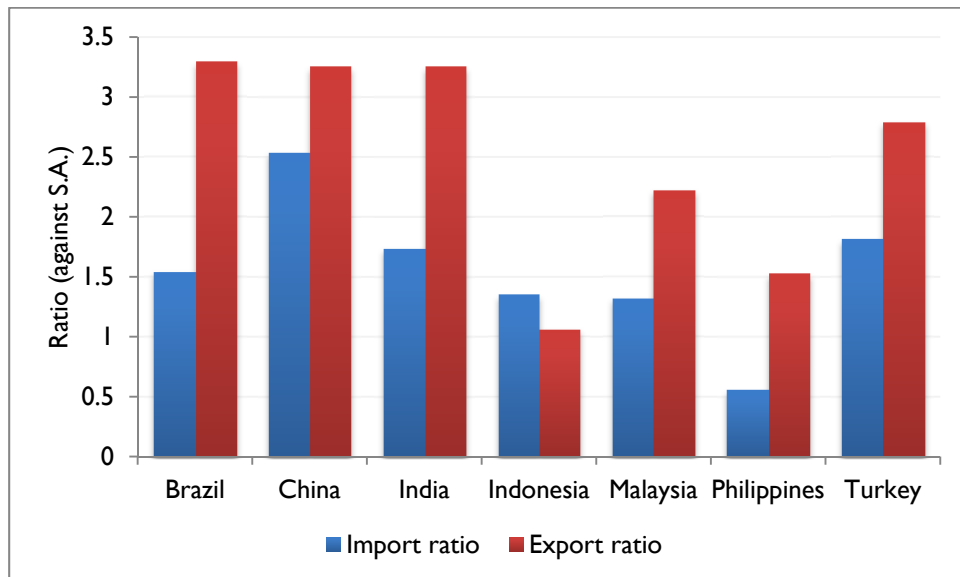


Figure 3: Ratio of exports compared with South Africa = 1, 1990-2012

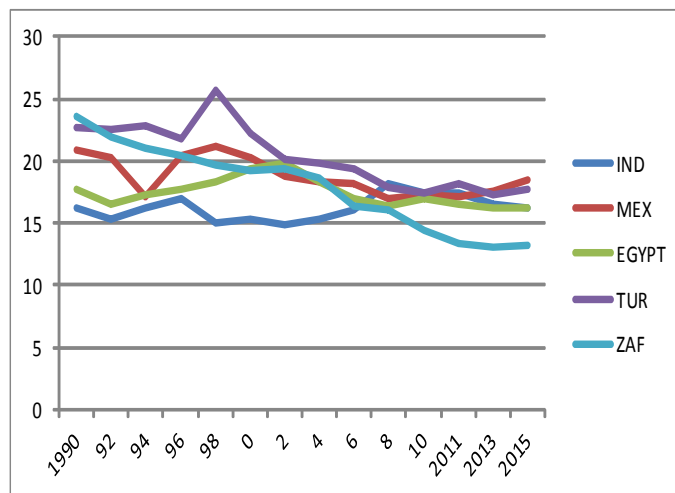


Notes: The average exports and imports (as a percentage of GDP) for the 1990-to-2012 period were calculated and a ratio was taken against South Africa.

Source: Borat et al. 2014.

South Africa also has experienced de-industrialisation – evident in the startling decline since 1990 in the share of manufacturing in GDP, from nearly 24 percent in 1990 to 13 percent in 2014. As Figure 4 shows, manufacturing shares also declined somewhat in three of the other comparator middle-income countries (Turkey, Egypt, Mexico) – but South Africa’s decline was far sharper.

Figure 4: Manufacturing share of GDP



As subsequent sections will explore in depth, multiple country-specific explanations account for the decline in manufacturing. Sanctions and import substitution tariffs had in effect protected a large and vulnerable clothing, textiles and footwear sector. The rate of decline in tariffs under the Uruguay Round was too rapid to allow firms to adjust their competitiveness. South Africa was not treated as a developing country under the WTO, and faced a harsh adjustment as it re-entered the world of multilateral rules. The domestic environment did not allow firms sufficient space and time to adjust—support measures to adjusting firms were weak, and were not used well by firms accustomed to protection; and with South Africa’s central bank pre-occupied with holding down inflation, the exchange rate strengthened instead of weakening with trade liberalisation. Labour productivity also has failed to outpace wage growth (except for a brief period in the late 1990s); Figure 5 illustrates with data for the 2007-2010 period.

Figure 5: Wage and productivity trends, 2007-2010.



The composition of exports is consistent with the above patterns – but the opposite of the intent of many in South Africa’s policy community that the shift to outward orientation would lead to a rapid expansion of manufacturing exports in general and,

within that, of higher-technology exports. As the top half of Table 1 shows, compared with other middle-income countries, South African exports are mineral-intensive, with relatively low shares for manufacturing. The technology content of most exports is relatively low, the main exception being motor vehicles supported by an expensive dedicated industrial programme. Only in the service sector has South Africa performed relatively well in non-traditional export markets.

Table 1: Ratios of export production relative to South Africa, average for the period 2000 to 2012

	Ores and metals exports (% of merchandise exports)	Manufactures exports (% of merchandise exports)
Brazil	0.47	0.90
China	0.07	1.75
India	0.21	1.32
Indonesia	0.30	0.87
Malaysia	0.06	1.36
Philippines	0.14	1.59
Turkey	0.12	1.55
Korea, Rep.	0.08	1.71
	High-technology exports (% of manufactured exports)	Insurance and financial services (% of commercial service exports)
Brazil	2.34	0.93
China	4.68	0.18
India	1.18	0.70
Indonesia	2.31	0.26
Malaysia	9.16	0.21
Philippines	11.69	0.13
Turkey	0.39	0.43
Korea, Rep.	5.40	0.56

Notes: High-technology exports are products with high R&D intensity, such as in aerospace, computers, pharmaceuticals, scientific instruments and electrical machinery.

Source: Borat et al. (2014).

Most fundamentally of all, over the past two decades, the South African economy has failed to address its deep-seated weaknesses of structural unemployment and a dearth of opportunity. In 1994, at the outset of democracy, South Africa's structural unemployment problem was among the largest in the world; close to 30 percent of the economically active workforce could not find jobs. Viewed from the perspective of this constituency, what mattered was, in the shorter term, the provision of a safety net and, over the long term, hope of a better future via participation in a thriving, vibrant economy. While the democratic political settlement has been successful in delivering the former, as we shall see, the latter has been more difficult.

III: Resetting the political and economic rules of the game

Some of the reasons for the disappointing outcomes laid out above can be found in features of the political settlement and associated package of economic reforms which were ‘baked-in’ from the outset. This section and the next use a ‘political settlements’ lens to explore how and why the economic reform agenda turned out to be uneven – bold in opening up externally, but with limited effort to complement opening with pro-active efforts to enhance competitiveness and productivity.

As this paper explores in depth, the dualistic economic structure inherited from apartheid, and the associated ‘skewness’ in the relative power and influence of key stakeholders, constrained the ability of economic policy-makers to put South Africa onto an inclusive trajectory of development, as the necessary economic complement to the country’s democratic political settlement. Policy-makers needed to accommodate the concerns of apartheid-era business (as well as political) elites and of core ANC constituencies (notably including organised labour) – and more broadly to assuage concerns as to the ideological orientation of the ANC. The result was that South Africa’s post-apartheid economy remained dominated by a small number of unusually large companies. Paradoxically, the isolated environment of the apartheid era of sanctions had promoted both protection and innovation. When the economy became more open, and these buttresses were removed, they were not replaced with an environment effectively driving and supporting competitiveness through skills development, domestic competition and innovation, and investment.

IIIA: The political settlement

The political economy of South Africa’s shifts towards market-based policies can only be understood within the broader context of the profound political changes of the early 1990s: the ending of apartheid; the commencement of negotiations between the white minority National Party government and its opponents; the democratic elections of 1994, won by the African National Congress; and the consolidation of authority by the ANC.

The story of the broader political struggles associated with the negotiation and consolidation of South Africa’s political settlement has been well told elsewhere,¹ and will not be recapitulated here. Rather, following the approach of both the broader ESID research programme and the comparative analyses of the political economy of market-based reforms in middle-income countries, of which this paper is a part, this section frames South Africa’s political and economic changes through a ‘political settlements’ lens.

Three sets of concepts are central to the ESID analysis of political settlements. First is the notion of an ‘*elite bargain*’ – a formal or informal agreement among elites to forswear violent contestation and work to achieve joint gains through co-operation. In the South African case, there is a clear historical moment in which the contours of

¹ See, for example, Mandela (1994), Sparks (1996), Marais (1998), Seekings and Nattrass (2005), Gevisser (2007), Welsh (2009).

the elite bargain relevant to the present study took shape – the unbanning of the African National Congress and release from jail of Nelson Mandela in 1989-1990, the subsequent four-year process of negotiating an interim constitution, the first democratic elections in 1994, and the formal promulgation of a constitution by the elected parliament in 1996.

As is explored further below, both business elites and organised labour were centrally involved in the construction of the elite bargain. It follows almost axiomatically from the necessity of crafting an elite bargain which would win the support of both the newly politically empowered ANC and incumbent political and economic elites that there would be some constraints on change from the outset. What is perhaps less obvious, though (and is a central question explored in this paper) is whether the commitment on the part of the parties to the details of the elite bargain would prove robust.

The second dimension of the ESID political settlement framework comprises the *inherited institutional legacy* -- specifically the ‘strength’ of inherited institutional arrangements; that is, whether rulemaking, monitoring and enforcement arrangements exist that are capable of supporting ‘impersonal’ rules of the game which apply and are enforced equally among all who have standing, or whether agreements are ‘personalised’ and apply only to specific individuals and groups. South Africa’s political settlement took the form of a robust, ‘impersonal’ order – the careful, detailed negotiation of a constitutional democracy, underpinned by South Africa’s historically resilient (especially for the white minority) justice institutions. As we shall see, impersonal rules were also central to the economic settlement. The extent of subsequent robustness of the commitment to impersonal economic rules of the game (and why) is a further central question addressed in this paper.

The third dimension comprises the ways in which *non-elites are incorporated* into the political settlement – the balance in the political settlement between inclusion and repression, and between broad-based, ‘programmatic’ service provision versus clientelistic modes of incorporation. As of the mid-1990s, South Africa’s principal actors had little doubt that the mode of incorporation would be via electoral contestation among programmatic political parties – with the ANC in particular enjoying seemingly deeply-rooted support from South Africa’s historically oppressed black population, and committed programmatically to ‘a better life for all’. Though the broad issue of the mode of incorporation of non-elites is not a central focus of this paper, its successful resolution is a necessary condition for the sustainability of the broader political settlement, and thus of the business–government economic settlement as well. We return to this theme in the concluding section of this paper.

IIIB: Crafting economic reform

All political processes are complex and most are more complex than they appear. The South African struggle for freedom and its resolution were no different. This section begins our extended exploration of the process through which some of the

economic dimensions of the overall political settlement took shape – focusing on some of the key actors and events in this process, their incentives and behaviours, with particular emphasis on their influence on the economic reform package which took shape in the 1990s.

The diversification of the South African economy, from farming and mining, towards manufacturing and services, had since the 1930s been built on the deployment of some of the surpluses of mining towards inward-looking development policies. Tariff barriers supported the growth of consumer industries, from clothing and textiles to automobiles, predicated on the increasingly prosperous white population. In the mid-20th century, politically victorious Afrikaner nationalists built a financial sector to compete with colonial and global finance, and successfully used state-owned enterprises such as the Industrial Development Corporation as an instrument of domestic industrial development.

As the limits of a protected market became increasingly constraining, the government's inability to leave the policy of racial inequality behind it inhibited the possibility of a transition to a more outward-looking competitive, diversified economy. Meanwhile, political change was accelerating. In the 1980s, the mass democratic struggle gained momentum domestically and, combined with the effects of sanctions movements and other pressures abroad, the South African economy became increasingly weak and vulnerable. In addition, the apartheid cheap labour model was no longer viable and domestic opportunities were shrinking. It seemed that the political crisis and the economic crisis were interlinked, opening up the possibility that the disjuncture of a political transition would allow for an economic transition too. (Gelb 1991)

In the mid-1980s, frustrated with the party political sphere, where whites seemed determined to hold onto privilege, and increasingly anxious about the weakening economy, business began to engage with the banned and exiled ANC. This was shortly before the government began secret discussions with the imprisoned Nelson Mandela. As of the mid-1980s, six conglomerate organisations controlled companies accounting for over 85 percent of the market capitalisation of the Johannesburg Stock Exchange (with the Anglo American Corporation alone accounting for 34 percent) (Hirsch 2005). Leaders from within these conglomerates (and from the business organisations which they helped finance) could thus credibly claim to be speaking on behalf of 'the business community'.

The nature of business engagement with politics in the late 1980s was primarily to bring the two contesting forces, the ANC and the National party, into discussion regarding a way forward. After the unbanning of the ANC and the release of some political prisoners, including Nelson Mandela, in 1990, a more formal process of negotiation began. The parties agreed that elections should take place, but only after there was agreement on a detailed interim constitution and other safeguards were introduced. In May 1996, two years after the first democratic election, a final constitution was adopted by the democratic parliament. It is a modern liberal/social

democratic law with proportional representation, third generation socioeconomic rights and a clear separation of powers between the parliament, the executive and the judiciary.

The embrace of impersonal, rule-bound processes as central to South Africa's political settlement filtered through to the negotiation of the economic order as well. It created the expectation that the outcome of a successful process would be agreement on a set of impersonal rules, to which all parties would abide – with South Africa's strong, independent judiciary providing the basis for credible commitment that the protagonists would adhere to the agreed-upon formal rules. The political process also provided an ongoing platform for 'learning to co-operate' – for multiple stakeholders, with competing interests, to work together to reach agreement on a negotiated outcome which all could abide by. Almost from the first this was incorporated into economic policy-making.

During the transition period of the early 1990s (when the pace of business engagement with the internal and external opposition to apartheid picked up further, rather than tailing off), the business community exercised soft power with great energy and dexterity. Without doubt, forward-looking business leaders helped to push the transition forward and helped to unlock deadlocks in the negotiations. They also engaged actively in working to shape economic thinking in post-apartheid South Africa away from state ownership and control towards more market-friendly solutions. The broader global and regional context supported these efforts. Globally, statist economic development paths became discredited in the 1980s, underlined by the capitulation of the Soviet Union in the Cold War. Regionally, the reputation of many African governments for poor economic policies added to a sense of caution of the ANC, as did the threat of capital flight. The result was the adoption of market opening reforms.

In 1990, representatives of government, business and labour signed the Laboria Minute, in which it was agreed that new labour laws had to be the product of negotiations of all three parties. This was one of the factors leading to the creation of a National Economic Forum in 1992 (Webster and Joynt 2014). The National Economic Forum became the transitional institution that allowed for the discussion and development of economic policy. Formally the three main social partners constituted it. Informally the ANC was also present, sitting within the labour ranks.

One of the achievements of the National Economic Forum was the reformulation (in parallel to the ongoing negotiations over the political settlement) of South Africa's offer to the General Agreement on Tariffs and Trade. The final offer which was accepted in the Marrakesh Agreement that concluded the Uruguay Round in April 1994 was formulated in the National Economic Forum, based on research conducted by the Industrial Development Corporation – a national development bank. These were not easy decisions. Whether or not, in retrospect, the details of the Uruguay Round offer were well calibrated, the ability of the NEF to come to a decision on

trade policy reforms that would inevitably be painful for several parties to the agreement suggested that some kind of developmental pact was possible.

The commitment to a fairly conventional set of economic policies continued to deepen under the first elected ANC government. Highlights included:

- The far-reaching commitment, described above, to tariff reduction and trade liberalisation, as part of the Marrakesh Round of global trade policy reforms.
- A broader embrace of Washington Consensus economic policy prescriptions (including conservative fiscal and monetary policies, and a commitment to restructuring of state assets, including privatisation) – as part of a home-grown Growth, Employment and Redistribution (GEAR) strategy, announced in 1996.
- In March 1995, the dual exchange rate was abolished and foreign exchange market liberalisation began, following an incremental path, favouring capital exports to Africa, and culminating in a relatively liberal exchange rate regime by 2003.
- A ramping up of domestic competition policy, including the promulgation in 1998 of a Competition Act, and the establishment of an independent Competition Commission with both investigative and prosecutorial powers.
- The central bank was given a conservative mandate by the constitution, to protect the internal and external value of the currency, and pursued money supply-driven monetary policies.

As of mid-1994, the intent had been to complement these measures with more pro-active industrial policy. In practice, for reasons that will be discussed in later sections, only quite limited pro-active efforts were made. Pro-active initiatives to foster black economic empowerment (explored in detail in Section IV) comprised an additional arena of intervention, which was beginning to find its way onto the economic agenda in the early 1990s.

A final dimension of the economic settlement, though not the central focus of this paper, must also be highlighted: the ANC did not shirk from its responsibility to the large proportion of the electorate which had brought it to power. The key forms of distribution in the first decade of the 'new South Africa' were the extension of infrastructure and social services to black communities. As government finances improved, with a growing economy and better taxation systems, social transfers grew rapidly as the third element of redistribution – in the form of social old age pensions, disability, child support and foster parenting transfer payments.

IIIC: Some limitations of the approach to economic reform

Overall, the economic reform package depicted above can be characterised as one in which business succeeded in maintaining the prevailing economic order by accepting the imposition of new, tougher trade and competition disciplines compared with the previously highly protected circumstances of the apartheid era. It also

accepted the need for the gradual incorporation of a black ownership and managerial elite. The ANC went along, but not necessarily wholeheartedly. When Mandela visited Washington DC in 1994, accompanied by a group of South African business leaders who had been prominent in the apartheid era, British ambassador to Washington Robin Renwick congratulated him on his magnanimity. 'Mandela replied, with understandable bitterness, that he forgot nothing, nor did he forgive, but that he needed them now' (Renwick 2015).

Regardless, the result was a collective commitment to rule-bound capitalism, and very little interference with the way business was done. Conglomerates streamlined into focused corporations and (with the 'artificial' constraints on international diversification as a result of apartheid-era sanctions now out of the way) refocused on global markets. Some examples of globalisation:

- South Africa's Gencor merged with Australia's Billiton, and eventually became BHP-Billiton;
- South African Breweries listed in London and became SAB-Miller, recently taken over by Anheuser-Busch-Inbev;
- ABSA Bank was brought into the Barclays network, who bought nearly two-thirds of its shares;
- South Africa's Anglo-American and De Beers essentially became British global mining companies.

An alternative model was for companies to expand regionally and globally, while retaining their South African domicile – as in Standard Bank, with its large African banking network, and Naspers, with its investments in an African pay-tv network and internet businesses across the world.

The suite of economic policies was strong on what was then called 'getting the prices right' and what we call 'disciplining reforms' and strong on redistribution through the fiscus; but somewhat weaker in the more interventionist kinds of market support programmes, such as innovation support, cluster development or industrial policy. The conglomerate-linked businesses had limited interest in proactive policies – both because their focus was on new opportunities globally, and because they were sceptical ideologically. Though some industrial policies were adopted, in the automobile industry and in clothing and textiles, the Treasury strongly resisted 'picking winners'.

Restructuring was also constrained by the approach adopted in the new competition law. Unlike anti-trust law in the US, for example, the Competition Act of 1998 punished proven anti-competitive conduct, but not concentrated structure per se. The giant apartheid-era conglomerates indeed restructured. They dismantled their earlier diversified structure, and rationalised themselves into globally oriented, industry-focused businesses. Streamlined they were, but they continued to retain a huge amount of market power (Aghion and Fedderke 2008, Wörgötter 2014).

Also contributing to concentration and weak competition was the failure to implement effectively government's far-reaching proposals, formulated in the early years of democracy, to restructure (and partially privatise) the state-owned electricity, telecommunications and transport sectors (Wörgötter 2014, Levy 2014). Some of these industries remained state monopolies, while others were partly privatised in the absence of a regulatory environment that promoted competition. The result was fertile ground for rent-seeking interventionists.

More broadly, political support for a rule-bound and market-based economic settlement was less robust than appeared at first glance. As a political party, the ANC straddled the left-of-centre to far-left ideological spectrum – encompassing both social democrats and a hard-line, pro-nationalisation, left wing. For many decades, the South African Communist Party (SACP) had been an 'alliance partner' within the ANC; its influence continued to be strong in the first ANC government. The decision to embrace Washington Consensus-style reforms was driven in large part by the desire of the country's new political leadership (notably including the urbane, internationalist, University of Sussex-trained Thabo Mbeki, as deputy president and then president) to signal to the international community that the country was 'open for business' – and (in a post-Soviet world) had embraced a specific set of ideas, namely the global pro-market consensus. Indeed, the 1996 GEAR programme was not elaborated through an adequate consultative process, and was announced defiantly as a 'confidence-building' measure by Deputy President Thabo Mbeki and the then-new Minister of Finance, Trevor Manuel.

Organised labour, a core part of the ANC's ruling alliance, was deeply wary of market reform – and this wariness was enhanced by the reluctant support of other stakeholders (especially key parts of the ANC government) for proactive supports to facilitate adjustment and the entry of new firms. The manner of the introduction of the GEAR programme (on which more below) weakened trust between the ANC centre and its allies, the Congress of South African Trade Unions (COSATU) and the Communist Party. COSATU resisted all efforts to modify labour laws in the direction of greater flexibility. And it relentlessly opposed efforts at privatisation – forcing the abandonment of efforts to introduce private participation into electricity, ports and other infrastructural services.

The established business community was supportive of the economic settlement in theory – especially insofar as a corollary of pro-market policies was protection of property rights (i.e. the status quo vis-à-vis ownership of economic assets). However, the economic benefits of support for rule-based economic governance need not be unmitigated. For one thing, the gap can be uncomfortably small between commitment to rule-boundedness, and inflexibility (rather than co-operation) in addressing the ongoing challenges of economic policy-making and implementation. For another, the gap between support in principle for rule-based economic governance and opportunistic engagement in deal-making can be quite large. As explored further in Section IVA, these complexities filtered through into the way business engaged in policy processes in the first two decades of democracy.

There was also the ownership question, and its consequences. Business elites were concerned about the socialist traditions of the ANC's allies, the South African Communist Party. Nelson Mandela's several references to nationalisation in the earliest years of the transition encouraged business to redouble its efforts to persuade the ANC and its allies to support orthodox market-friendly economic policies. This meant, particularly, not interfering disruptively in the ownership structure of the economy.

It was evident to most that it would not be politically tenable for the economic elite to remain lily-white. Big business began in the 1980s to recognise that an earlier process of incorporating Afrikaans-speaking whites into the English-speaking business elite needed to be replicated, in a manner, for black South Africans, in order to provide firm support for the economic order. Black economic empowerment in these terms meant the gradual incorporation into the elite of South Africans who were not white, largely through discounted and future-financed share transfers. There was also commitment to the promotion of some black professionals and managers, though this was a weak commitment in most sectors, compared with public sector transformation programmes. Over time, as Section IVB will detail, the process accelerated.

But perhaps the most fundamental obstacles to transforming the economy derived from apartheid's legacy of racial political polarisation and economic dualism. Both added enormously to the challenge of forging an inclusive development path.

The legacy of racial political polarisation resulted in a vast political and social gap between the varied elites, whose co-operation was key to forging an inclusive democratic future. Over the short term, a large gap needed to be navigated between incumbent (white, and largely Afrikaner) political elites who were negotiating away their political power, and newly-empowered political elites, largely within the ANC umbrella, whose legacy was one of exile, imprisonment and revolutionary struggle. Over the longer term, sustaining an ongoing capacity to co-operate between the new political elites and the powerful, pre-existing economic elites was central to realising an inclusive post-apartheid economic vision. But here, too, the political and social gap was very large. Inevitably, this lack of shared values, networks and understandings of the world added to the challenge of sustaining ongoing co-operation in pursuit of a more inclusive development path.

As for the legacy of economic dualism, self-evidently a dualistic economy has a 'missing middle', and thus limited opportunity for upward mobility, and inclusive development more broadly. But a 'missing middle' also has a political dimension. At the dawn of South Africa's democracy, big business and organised labour comprised the overwhelmingly dominant economic stakeholders (with the latter formally aligned with the ANC as part of the governing 'alliance'). Moving from dualism to inclusion involves a major push to create new work opportunities for the unemployed, and new opportunities for emerging small businesses. But the voices of both the unemployed and of small businesses were very faint. It was asking much to expect that big

business and organised labour, whose interests arguably were directly antithetical to those of the economically marginalised, would advocate on behalf of the latter. So it is unsurprising that, as we shall see, in the course of implementing economic reforms the concerns of insiders consistently were given priority over those of outsiders looking for a foothold.

In sum, from both a political and a developmental perspective, the foundations of the economic settlement were not sound. The settlement provided a platform for strong incumbents to thrive, while doing little to address the structural gaps of an economy characterised by an unusually large average firm size and an unusually weak small business sector (Kaplinsky and Manning 1998). The economy remained extremely bifurcated between a concentrated and centralised market economy and a feeble and fragmented economy of the urban and rural marginalised poor. South Africa was a dual economy, like a double-story house ‘without a connecting staircase,’ President Thabo Mbeki complained in 2003 (Pressly 2003).

IV: The play of the game

Coming into the 1990s, South Africa had been characterised by decades of domestic conflict, international opprobrium and economic sanctions. Against that backdrop, the seemingly miraculous achievement of a rule-based, democratic political settlement, plus a programme of market-based economic reforms, might have been expected to unleash rapid economic growth. Instead, as we have seen, the results have been mediocre. Why?

As Section III detailed, part of the answer can be traced back to the motivations for, and content of, the economic settlement itself. One might have hoped that over time the weak points in the initial economic settlement would become evident, and policy would adapt accordingly. But this did not happen. On the contrary, beginning in the latter 1990s, the broader context became increasingly unfavourable for economic-dynamism-enhancing reforms.

This section uses two in-depth illustrations to explore how and why the ‘play of the game’ exacerbated (rather than rectified) some of the key weaknesses of the economic settlement. Part IIIA focuses on the rise and fall of the ‘corporatist’ arrangements that were intended to give effect to many of the economic dimensions of the elite bargain at the heart of the settlement. Part IIIB explores the evolution of ‘black economic empowerment’ (BEE).

IVA: The rise and decline of a ‘corporatist’ elite bargain

Corporatism was a central part of South Africa’s process of economic policy-making during and after the 1994 political settlement. It also has a pre-history. Dating back to the 1920s, a fundamental objective of apartheid policies had been to use state power to tilt economic incentives and resources in favour of the country’s ‘white’ minority and (post-1948), within that, to the Afrikaans-speaking population. By the 1980s, these policies had been successful: the overwhelming majority of white South

Africans no longer perceived themselves as needing active state intervention to support their economic wellbeing. Meanwhile, the prevailing economic model had lost momentum.

Well before their engagement in the mid-1980s with the banned and exiled ANC, South Africa's business elites began promoting initiatives to further domestic economic and social policy reform. In 1977, business leaders led by Harry Oppenheimer, Anton Rupert and Clive Menell set up the Urban Foundation, with the aim of building up a black middle class with a proprietary stake in the urban economy. This strategy was seen variously as a path to gradual reform or as a buffer against the increasingly militant working class. Relatively liberal business leaders also supported the Progressive Federal Reform Party, a white party operating within the segregated parliamentary system. The South African Foundation acted as a kind of international public relations agency for South African business, as the credibility of South Africa's Foreign Affairs Department waned.

Business's central role in economic policy formulation during the transition to a new political and economic settlement was thus a continuation of a longstanding pattern. The pattern persisted into the democratic era, now buttressed by support from some of the ANC's key economic policy-makers (and their allies in organised labour), many of whom admired the corporatist arrangements for policy formulation in Germany and Scandinavian countries, which included formal roles for organised business and labour interests.

One of the first acts of the democratic government was to establish, in December 1994, a National Economic Development and Labour Council (NEDLAC) as a formal chamber for social partners. Its objectives were described as:

'The Council shall: (a) strive to promote the goals of economic growth, participation in economic decision-making and social equity; (b) seek to reach consensus and conclude agreements on matters pertaining to social and economic policy; (c) consider all proposed labour legislation relating to labour market policy before it is introduced in Parliament; (d) consider all significant changes to social and economic policy before it is implemented or introduced in Parliament; (e) encourage and promote the formulation of coordinated policy on social and economic matters'(Republic of South Africa 1994).

NEDLAC was organised around four chambers: the labour chamber; the trade and industry chamber; the macroeconomic chamber; and the development chamber. In the fourth chamber only, community organisations have representation. It was well-led by its founding staff, and quickly became a highly respected forum. Its promise seemed immense.

In NEDLAC's early years, its trade and industry chamber was actively developmental in orientation, drawing on a Japanese Grant Fund to conduct investigations into increasing South Africa's competitiveness and opportunities for diversification,

especially in export markets.² It also became the forum in which international trade deals were negotiated domestically. Several innovative programmes to support competitive manufacturing were developed. These included an export credit guarantee programme for small business, a competitiveness fund (a matching grant programme supported the upgrading of firms in the tradeable industrial sector) and a sectoral partnership fund (another matching grant programme, one where firms had to apply as a group, and derived shared benefits).

But these early gains were deceptive. Within a few years of its establishment, the influence and stature of NEDLAC began to wane. Part of the reason was that the ANC had now become the elected government. Direct, bilateral engagement with government became a natural alternative to the complex, multi-stakeholder dialogues between the apartheid government and its various antagonists which were used during the transitional period of political negotiation to engage on policy matters of pressing concern. The loss of trust in social partnership is traced by some, especially those on the left, to the manner of introduction and the nature of the GEAR (Growth, Employment and Redistribution Strategy) in 1996. Now enshrined in apocryphal accounts, this event was nevertheless very important. The context was uncertainty. Mandela had appointed two successive white financiers as minister of finance – men with credibility in the markets, but little political power. Three parallel and competing government initiatives on economic policy were emerging – in the finance department, the department of labour, and in the reconstruction and development ministry in the presidency. The rand was unsteady and there were rumours that Mandela was ailing.

In this context, the first ANC minister of finance was appointed. He was Trevor Manuel, a 40-year-old former civil engineer and anti-apartheid leader, who had demonstrated his economic nous in the ANC in the early 1990s.

The executive felt great pressure to give direction. In the context of a rising deficit, growing debt, ballooning current expenditure by government, and rising inflation, the GEAR took the form of a home-grown structural adjustment programme with some growth elements. The way that the GEAR was swiftly introduced into parliament without – in the opinion of the trade unions and the Communist Party allies of the ANC – enough consultation, weakened the trust between social partners. The structural adjustment was ultimately successful in many respects, but the prospects for inclusive, corporatist policy-making had dimmed.

There also were structural limitations to NEDLAC serving as an inclusive platform for economic policy-making. These limitations were especially evident in negotiations in NEDLAC's labour chamber, historically its most active. Upon its founding, NEDLAC was mandated to act as the forum at which labour law reform was negotiated. It was

² Hirsch's knowledge is enhanced, but his objectivity may be influenced by the fact that he was the government delegation's convener of the trade and industry chamber of NEDLAC from its inception early in 1996 to October 1998. He also participated in many of the broader social partnership negotiations between the early 1990s and 2012.

the site of negotiation of four major labour laws on industrial relations and employment conditions that passed through the NEDLAC and parliament during Mandela's presidency, as well as all subsequent labour laws and regulations. NEDLAC agreements on labour law (and other laws which are voluntarily negotiated through NEDLAC) go to parliament for further debate, but need to return to NEDLAC if any of the tripartite agreements is challenged in parliament.

The outcome of negotiations over labour law illustrates vividly the argument made earlier that the inherited power imbalances among economic stakeholders – with big business and organised labour disproportionately strong, and the voices of small business and the unemployed disproportionately weak – constrained the ability to put in place economic policy measures supportive of inclusive development. The strongest elements in the union delegation were the major industrial unions of COSATU, the dominant federation, closely aligned to the ANC. The leading negotiators and most of the team on the side of business were drawn from very large corporations, which had the resources to hire sophisticated industrial relations managers. The government delegation was composed largely of former officials of the leading unions. Small firms and competitive industries were thinly represented and their voices were faint.

Mahajan (2012) describes the firm owners, government and organised labour to be 'locked in a continual, rambunctious public tussle over the distribution of the high rents being generated under the system'. This triad is constrained by the bounds of labour regulation, competition policy, tax policy and equity considerations. The outcome was progressive legislation for industrial relations and employment conditions that aligned with the circumstances prevailing in large profitable firms. Exemptions for small firms were marginal, and only for very small firms. No formal allowance was made for labour-intensive firms in regions of high unemployment; on the contrary, it became accepted practice that sectoral agreements between unions and employers were extended by the minister of labour to 'non-parties' – in other words, the less competitive firms with lower unionisation, often outside of the major urban centres.

The ruling party publicly pushed for employment-friendly labour market policies, but found it difficult, within the environment of a strained but nevertheless critical alliance with the union movement, to materially counter trade union interests in terms of the direction of labour market reform. The result was that, while the trade and industry chamber helped to develop and implement a vision of a dynamic, competitive future for the South African economy, the labour chamber introduced inflexibilities and floor prices for labour that inhibited the expansion of a competitive industrial sector. The process created a barrier to entry for new firms that could create a more competitive environment and normalise returns.

Within the NEDLAC labour framework, the unemployed are left out, as are those who would like to see a greater proportion of rents being transferred into higher productivity, higher investment growth-enhancing actions. Firms in tradeable sectors

in South Africa have retained some activities which are competitive, but instead of investing broadly in the tradeable sector in South Africa, have invested in foreign operations, in Southern Africa and the rest of the world – increasingly insulating themselves from the contradictory policies of government. The outcome is an economy that performs below its potential.

NEDLAC's fiscal and finance chamber and the development chamber have had limited impact. The former was the source of dissatisfaction for social partners, especially labour, who felt that the preparation of the annual national budget should include substantive negotiations, or at least inputs from NEDLAC. The remoteness of decisions on monetary policy was equally frustrating.

The development chamber was the site of discussions and reports on social policies and programmes, but the community organisations – who were probably less representative than the three formal social partners – complained that they were not a part of key policy discussions. This led to more controversial matters being discussed in a plenary forum, but though debates were frequently heated, the formal power of the assembly was limited.

The quality of representation at, and discussion within, NEDLAC declined from the late 1990s. The staff leadership that succeeded the initial cadre also lost the respect of one or several social partners, because of perceptions of bias in favour of the trade unions. The ruling party's (ANC) close political alliance with and increasing dependence on the leading trade union federation (COSATU) increasingly challenged the perceived integrity of the social partnership. NEDLAC became increasingly dysfunctional as a decision-making forum. While a strategic review of NEDLAC pointed to ways of reinvigorating it blocking interests have triumphed. When a senior trade unionist was appointed minister for economic development in 2009, in a concession to the allies of new President Zuma, hopes for a growth-oriented social pact briefly flickered to life. Minister Ebrahim Patel managed to forge several sectoral social partnership agreements, but hopes for a broader growth and employment pact soon fizzled out.

IVB: Black economic empowerment

When it made its political transition to democracy, South Africa was a middle-income economy. But deep economic fissures underlay the aggregate numbers. Poverty and inequality were far worse than in other middle-income countries with similar per capita incomes (Levy et al. 2015); the economy was more capital- and resource-intensive; and industry was more highly concentrated (Aghion et al. 2008, Borat et al. 2014, Kaplinsky and Manning 1998). Further, the concentration of wealth and ownership along ethnic lines was extreme: essentially all wealth was concentrated in the hands of a white minority, which, as of 1990, accounted for about 13 percent of the country's population. As of 1994, only one-half of 1 percent of the shares on the Johannesburg Stock Exchange (JSE) were owned by black investors.³ Even if one

³ Carmody (2002), quoted in Plaut and Holden (2012).

were to set aside concerns of economic justice (which we do not), the disjuncture between, on the one hand, a shift of political power from a white minority to the majority of citizens within a constitutional democracy and, on the other, a continued monopolisation of wealth by the white minority, was politically untenable. As a ten-year retrospective, issued by the South African presidency in 2003, put it:

‘One of South Africa’s characteristics ... is the fact that the political leadership in government is quite distinct in terms of race, culture, background and lifestyle from the economic leadership. This has had some benefit in that the political leadership is not beholden to an established “Old Boys Club”. The disadvantage is that the kind of trust needed between the economic and political “elites” for high levels of investment was missing post-1994 South Africa’ (PCAS 2003).

Evidently, the ownership question had to be addressed.

This, however, posed a deep dilemma. While the ownership status quo was a recipe for political conflict and instability down the road, efforts to transform it risked unleashing destabilising influences of their own. There was the risk of uncertainty regarding future prospects of a kind which could undercut private investment. And there was the risk that, as political leaders and their allies jockeyed for access to economic assets, the discretionary use of political power could become the order of the day, weakening state institutions more broadly.

From the outset, the effort to address the dilemma posed by the ownership question had been incorporated into the effort to craft an elite bargain. These efforts played out within the ANC, where there had been a longstanding tension as to whether it was a nationalist movement committed to African advancement (including of an African business class) or whether it was a non-racial movement committed to broad-based economic transformation, with a distinctly socialist (and statist) flavour.⁴ Of more immediate relevance to the present paper, the effort to address ownership as part of a new elite bargain also played out in ongoing negotiations and improvised initiatives involving the ANC and the pre-existing business elites.

Some efforts dated back to the late-apartheid period, when both the private sector and government (within the confines of its ‘bantustan’ policy) embarked on initiatives to build up a black middle class as managers, professionals and entrepreneurs. In parallel, beginning in the mid-1980s, the National African Chamber of Commerce (NAFCOC, a membership organisation of black businesses operating within South Africa) initiated a series of formal and informal contacts with the leadership of the ANC in exile.

⁴ As part of the ESID project, Deborah Posel prepared a useful informal note on the ongoing tensions within the ANC, both during the period of exile and in its early years in government, as to how to reconcile its ‘African bourgeois’ and ‘non-racial, socialist’ tendencies.

Early in the political transition, the established 'white' business class moved proactively to encourage black economic empowerment, on its terms. Schemes to transfer white share ownership to black Africans started with the sale of National Sorghum Breweries in 1990. Another important deal was the sale in 1993 by the Afrikaner-dominated conglomerate, SANLAM, of 16 percent of Metropolitan Life to a black empowerment consortium, New African Investments Limited (NAIL), founded by Dr Nthato Motlana, a Soweto-based medical practitioner who built a hospital from his practice, and had been a brave political leader in the 1970s. NAIL was one of multiple examples of a process of transferring usually minority shareholdings in large companies to consortia of black investors, paid for with debt that would be wound down as dividends flowed in, and the voting power of these shares was frequently compromised. NAIL subsequently was floated on the JSE; purchased, at a discounted price, the industrial conglomerate, Johnnic, from the Anglo American Corporation; and had a market capitalisation in 1998, before things subsequently turned sour, in excess of \$1 billion (Hirsch 2005).

But deals were sporadic, and potential recipients became restive. In October 1993, six months before the first democratic elections, sixty representatives of the ANC met with two hundred black business people at the Mopani Lodge in the Kruger National Park. A foreword to the summit programme attributed to Nelson Mandela noted that:

'... to a large extent it is the white owned companies that are gearing themselves to exploit the expected [post-election] boom. As new opportunities begin to unfold, black business must brace itself to take up the challenge of taking its rightful share in this major economic activity in order to promote our development and total liberation' (Schneider and Ramashoba 1994).

The new generation of economic policy-makers who came to the forefront with the advent of democracy thus had to contend with a wide variety of actors with divergent goals and ideologies vis-à-vis ownership. There was an incumbent (white) business class which recognised the necessity of altering the ethnic hue of ownership and control, but sought to do so on its own terms. There were the disparate ideological factions within the ANC. And, as inevitably happens with transfers of power in many, many countries the world over, there were also new waves of political leaders, with strong incentives (paralleling those of an earlier generation of white, Afrikaner politicians) to use their newfound political power and control over state resources to open up business opportunities for their allies, including by ensuring that their allies would be the beneficiaries of efforts to transform the structure of asset ownership. (And, no doubt, from the first there were also opportunists who saw possibilities for self-enrichment.)

The initial response of those policy-makers and political leaders who were wary of the risks associated with BEE was to try and contain the struggle over ownership within a broader discourse around economic transformation – to seek out ways of addressing the seemingly contradictory interests of the various protagonists without undercutting the momentum of efforts to reincorporate South Africa into the global

economy, and more broadly to foster inclusive economic growth and development. Efforts generally focused on new firm development, affirmative action in the workplace and measures to support the enhanced education of black people who had the potential to be professionals, managers and business leaders. Indeed, the term ‘empowerment’ was not included in ANC economic policy documents before the 50th national conference in Mafikeng in December 1997, where the ANC called for:

‘National Empowerment Policy: The ANC should clearly articulate a National Empowerment Policy that will focus on those who have been historically disadvantaged and particularly black people, women, youth and the disabled and rural communities. The empowerment process must constitute part of a more radical and profound change in social relations. Changing ownership and workplace relations are part of this wider process of empowerment.

‘Within the National Empowerment Framework government should establish a National Empowerment Fund which must lead to the stimulation of saving, shift people from the informal to the formal sector, and from predominantly retail to more manufacturing SMMEs.

‘The ANC government should ensure the implementation of a vigorous affirmative procurement policy which will ensure that government and parastatals facilitate awarding of tenders to our people through approved mechanisms’ (ANC, 1997).

This was still a growth-oriented approach, focusing on new firm development, affirmative action and the skilling of black South Africans.

Increasingly, though, it became apparent that lower-key approaches to transformation were doing painfully little to transform the ethnic hue of ownership. Thus, subsequent to 1997, the BEE process accelerated – spurred in part, perhaps, by a 1998 stock market crisis which left black beneficiaries of initial rounds of deals with unmanageable debt, and led to a decline of black ownership on the JSE from 8 percent to less than 4 percent.

In subsequent years, BEE became increasingly central to the objectives of the ANC, and its protagonists and beneficiaries became increasingly influential within the party. Policies surrounding black economic empowerment may perhaps have been intended in part to provide a system of rules within which to manage BEE expectations and pressures. However, as the process unfolded, it injected uncertainty, discretionary deal-driven contestation among aspirant elites – and an increasingly racially-charged dimension into South African politics.

Milestones in the acceleration of efforts included:⁵

⁵ For details, see Hirsch (2005), Tangri and Southall (2008), Mpanza (2016), Plaut and Holden (2012) and Harvey (2016).

- The establishment in 1998, at the urging of the Black Management Forum, of a BEE Commission, with the task (as President Mbeki put it) ‘to answer the question – how do we promote the formation of a black bourgeoisie which will itself be committed and contribute to black economic empowerment’? Chair of the commission was Cyril Ramaphosa, senior ANC figure turned businessman (South Africa’s deputy president from 2014 to early 2018, and the country’s president since February 2018).
- The passage in 2002 of a Mineral and Petroleum Resources Development Act (MPRDA) which required owners of ‘old-order’ mineral rights to convert to ‘new order’ rights subject to conditions of meeting BEE imperatives.
- Finalisation of the BEE Commission’s report and release of an official strategy document in 2003, followed by promulgation in 2004 of the Broad-based Black Economic Empowerment (BBBEE) Act.

The ANC’s intention to change the colour tone of business was accompanied by an effort to transform the politics of business, broadening the profile of the formal leadership beyond its antecedents in apartheid-era ‘white’ business. In 2003, a top black business leader, Patrice Motsepe, working closely with President Thabo Mbeki, established Business South Africa (BUSA) as a peak organisation that would represent all of business. It was a peak organisation, not a unified organisation, and its roots and resources, relative to the sectional and sectoral business organisations which lay beneath it, were relatively shallow. Its leverage came from the fact that it was the designated gateway to the state on political issues.

As per its name, the BB-BEE Act went beyond a narrow preoccupation with ownership. Its implementing framework laid out a balanced scorecard which set targets for ownership and management control, for skills development and support for subcontractors and other small and medium enterprises, as well as socio-economic development more broadly. The expectation was that each economic sector would detail a quasi-voluntary sectoral ‘charter’ aligned with the framework laid out in the legislation. The only enforcement mechanism was that in order to have access to public procurement opportunities, companies needed to be BEE compliant. The results were mixed.

The telecommunications, construction and mining sectors illustrate how BEE processes played out in practice. BEE influenced all three of South Africa’s dominant telecommunications firms:⁶

- The ownership structure of MTN was shaped at the moment of political transition by deals involving its potential shareholders, the outgoing Nationalist government, and the incoming ANC. MTN emerged from these deals as the highest-profile BEE-controlled firm in South Africa and, in the 2000s, as a major player in mobile telecommunications markets across Africa.

⁶ For further detail of the evolution of South Africa’s telecommunications sector, and its institutional and political drivers, see Atiyas et al. (2017).

- The state-owned fixed-line operator, Telkom, has a more chequered BEE history. It was partially privatised in 1997 to the Thintana consortium, in which Southwestern Bell was a key partner. Telkom reverted to national control when Thintana exited in 2004 – with a local BEE consortium (headed by the former director general of the Ministry of Telecommunications, and dominated by close allies of then-President Thabo Mbeki) purchasing the majority of Thintana’s interest, with subsidised support from the state-owned Public Investment Corporation. Post-2004, Telkom was highly profitable, but investment lagged.
- As for Vodacom, the second major mobile operator, UK-based Vodafone, has held a controlling interest (no less than 50 percent) ever since the granting of Vodacom’s business licence in 1993. Only in 2007 did Vodacom initiate a BEE deal. Revealingly, after Thabo Mbeki lost an ANC leadership struggle to Jacob Zuma, the initially-proposed BEE consortium (headed by Bulelani Ngcuka, a close ally of President Mbeki and, as then director of public prosecutions, a lead actor in efforts to prosecute Jacob Zuma for corruption) was set aside in favour of a more politically neutral BEE arrangement with Royal Bafokeng Holdings.

As Atiyas et al. (2017) detail, the net result has been mixed: a vibrant mobile sector; but lagging investment in broadband infrastructure, offset in part by new companies who responded aggressively to a court decision which unblocked regulatory constraints on entry.

For construction, in contrast to telecommunications, public procurement is a core part of the business – and in this sector, formal rule-bound BB-BEE arrangements have played a central role.⁷ In South Africa and elsewhere, construction firms have a long history of building close formal and informal relationships with government. South Africa’s dominant construction companies had followed this pattern with the apartheid government, so with the transfer of power to the ANC they confronted a formidable challenge of repositioning themselves politically.

Even before the passage of the BB-BEE Act, the sector had positioned itself for engagement, via the establishment in 2001 of a statutory, multistakeholder Construction Industry Development Board (the CIDB). Co-chairs of the CIDB included the chief executives of the two largest construction companies. Additionally, one of the two companies (Murray & Roberts) moved quite rapidly to appoint leading ANC figures onto its board as non-executive directors. The other (WBHO) helped to establish (jointly with the Thebe Investment Corporation and the Batho Batho Trust, whose trustees included Nelson Mandela, Walter Sisulu and the Reverend Beyers Naude) Rainbow Construction, the leading black empowerment construction company in the country, and partnered with them on high profile projects, such as the construction of the Constitutional Court building.

⁷ For details, see Mpanza (2016), a dissertation submitted in partial fulfillment of the requirements for a Masters of Commerce in Economic Development at the University of Cape Town, supervised by Brian Levy.

Immediately following the 2004 passage of the BB-BEE Act, the construction sector initiated a process of negotiating its own sector-specific charter, which was finalised a few years later.⁸ As Mpanza's (2016) detailed review of four leading companies shows, firms have complied with some⁹ of the provisions of the charter in exemplary fashion. As of 2014, the black ownership percentage in both Murray & Roberts and WBHO was above 45 percent (with the other two, Group Five and Basil Read, also above the target of 30 percent). All four firms had met the charter's BB-BEE targets for providing capacity-building support to their subcontractors, and for enterprise development.

Viewed from the perspective of South Africa's broader development goals, the results of construction sector BB-BEE were perhaps more ambiguous. Over the past two decades, both Murray & Roberts and WBHO have repositioned themselves as global companies, with only a minority of their business in South Africa. Domestically, all South African leading companies participated in the construction bonanza associated with South Africa's 2010 hosting of the World Cup soccer championship. Subsequently, though, following an in-depth investigation by the independent Competition Commission, all of the companies confessed to extensive World Cup construction-related price-fixing, with an estimated inflation of procurement costs amounting to about \$4 billion (out of total contract values of \$40 billion). While there have been no prosecutions of public officials for involvement in these collusive practices, given the intertwined relationships in the sector between business and politics, the likelihood of behind-the-scenes deal-making is surely not trivial.

While in both the telecommunications and construction sectors, BEE can be interpreted as having mixed economic consequences, in the mining sector the economic (though not necessarily equity) consequences have been unambiguous: efforts to introduce BEE ratcheted up uncertainty, with the result that 'between 2001 and 2008, the longest sustained commodity boom in recent history, South Africa's mining industry contracted at a rate of 1% per year, while its closest competitors grew at an average rate of 5% per year' – and this notwithstanding a 2010 valuation by Citigroup of South Africa's proven mineral resource wealth at \$2.5 trillion, the largest in the world.¹⁰ The MPRDA-mandated process of converting 'old order' to 'new order' mineral rights proved to be rife with ambiguity and scope for ministerial discretion as to what entailed a BEE-compliant conversion, resulting in numerous instances of conflict (resolved juridically) involving incumbent and BEE companies, and discretionary government action. An attempted revision of the legislative framework via a 2013 Mineral and Petroleum Resources Amendment bill added to the ambiguity, with ongoing further revisions continuing as of the time of writing this

⁸ Strikingly, almost all of the core negotiators who were not already senior industry executives, were subsequently appointed as non-executive directors on the boards of leading construction companies.

⁹ The exception is 'employment equity' – as of 2014, all four firms had fallen well short of targets (which ranged from 25 to 40-60 percent) for black inclusion in senior, middle and junior management positions.

¹⁰ The quote, the information from Citigroup, and additional details of the difficult challenges of implementing the MPRDA can be found in Harvey (2016).

paper. Unless the question of rights to mineral rents is resolved decisively, the risk is high that South Africa could miss the next minerals boom as well

Overall, the accelerating implementation of BEE has coincided with a broader proliferation of discretionary, personalised deal-making. BEE aside, one spur for discretionary deal-making arose from the ANC's ongoing quest to fund itself as a political party.¹¹ Another spur, evident in governments the world over, comprised the abundant opportunities to direct lucrative public procurement contracts to favoured providers in return for side payments. Subsequent to 2009, the scale of the latter seems to have accelerated and, as a variety of notorious large-scale scandals attest, increasingly become associated with broader failures in the governance of state-owned enterprises, and the politicisation of senior government appointments.¹²

There is no straightforward way to disentangle the role of BEE from other drivers of the movement away from impersonal, rule-bound governance towards personalised deal-making. Nor can it be concluded that the impact of BEE on entrepreneurship and the professionalisation of business was wholly negative. There are companies led by black business leaders who had built them up, such as Patrice Motsepe's mining businesses, the Kunene brothers' industrial businesses, Herman Mashaba's cosmetic products and Zitulele Combi's financial services business. There are also numerous distinguished black senior managers and professionals in the private sector who obtained their fortunes and influence through talent and hard work. But a significant proportion of major beneficiaries of BEE shares are not active as executive business leaders and are most notable for their political connections. Nor (as the data in Section II suggest) was their 'connecting' function between the political realm and established businesses sufficiently robust to provide credible commitment of a kind capable of underpinning a new wave of private investment (Pritchett et al. 2018).

¹¹ Multiple controversial deals have included Chancellor House as a business partner; Chancellor House is the investment arm of the African National Congress. See Donnelly (2015) for one example, involving Hitachi Power Systems and the electricity parastatal, ESKOM.

¹² An especially egregious example was the firing of a well respected minister of finance, and his replacement by a more compliant (but largely unknown) political cadre. An often-repeated argument at the time was that the firing was done to facilitate closure on two large-scale deals of dubious broader developmental benefit associated with state-owned enterprises – the dominant electricity supplier, Eskom; and the state-owned South African Airways. The former included controversies over a variety of high-profile cases surrounding the procurement of coal for electricity by Eskom and, perhaps most centrally, controversy surrounding a proposed \$100 billion (!), sole-sourced arrangements to procure a fleet of ten nuclear power stations from Russia. For SAA the controversy centred around the financing arrangements for the procurement of a new fleet of airlines. In the event, the unknown cadre lasted less than a week as minister of finance, before a widely respected former finance minister (who was himself fired in early 2017) was parachuted back into the position. There have also been controversies surrounding the procurement of railway rolling stock by the Passenger Rail Authority of South Africa (PRASA).

Had the ANC been able to retain its focus on BEE as skills enhancement, affirmative action and new firm development – their original vision – the impact of BEE could perhaps have been directly growth enhancing. But the form ultimately taken by BEE failed to create a greater appetite for investment in competitive businesses in South Africa. Instead, the primary preoccupation of BEE was the transfer of ownership – largely, as it turned out, to politically connected, influential individuals. The focus on corrective actions was no doubt necessary for legitimacy and political stability, but it sucked the energy of both government and business away from initiatives focused on growth and employment creation.

The subsequent histories of two of the pioneering BEE initiatives described above – the National Empowerment Fund, and Business South Africa – illustrate the pattern. While the NEF was motivated by the ANC conference in 1997 to drive small firm development and formalise the informal sector (see above), it ended up spending a large proportion of its resources transferring shares from white to black owners and on support for already established black-owned firms. As for BUSA, once Motsepe and Mbeki left the scene in 2007, it began to lose influence. By 2012 business unity was crumbling and when the Black Business Council was launched, BUSA's statement was defensive:

'BUSA remains determined in its pursuit of promoting and implementing economic transformation. It therefore remains incorrect and unfortunate that allegations are made that BUSA represents white business interests and that, by implication, it is riding roughshod over black business interests.'

This defensive statement indicated how the politics of business had degenerated from attempts to bring the state and private sector together around visions for growth and employment creation to contests for the spoils of BEE. In 2012, BUSA was seen as representing white business and the already empowered. The ANC now had to deal with the next layer, the aspirant business elite (embodied in the Black Business Council), who demanded its share of the cake.

No end was visible. As of 2011, only 8 percent of shares on the Johannesburg Stock Exchange were directly owned by black investors (with an additional 9 percent indirectly owned by black investors through mandated investments, such as pension funds), and only 22 percent of the directors on boards of JSE-listed companies were black.¹³ Contestation over ownership continues – and how it will be resolved remains uncertain. What is clear, however, is that the contestation and resulting uncertainties have become an increasingly stormy cloud, shadowing South Africa's economic and political prospects. BEE increasingly encouraged competition for political power in order to obtain access to the sources of patronage; it weakened the coherence and credibility of the political system.

¹³ 'Crunching numbers on the JSE', Financial Mail, 13 October 2011, quoted in Plaut and Holden (2012).

V: A fraying political settlement

In this final section, we step back from the details of how South Africa's business–government relations have evolved and reflect more broadly on the patterns we observed, and their implications. We organise our reflections around the three sets of concepts we identified earlier as central to the ESID analysis of political settlements: the character of the elite bargain; the ways in which non-elites are incorporated into the settlement; and the balance between personalised and impersonal institutions.

Viewed from this political settlements perspective, as of the latter 1990s it seemed reasonable to hope that South Africa was well positioned for an era of sustained, inclusive economic growth and development. The country had successfully put in place what seemed to be a robust elite bargain, underpinned by strong impersonal institutions (including a democratic constitution and strong rule-of-law enforcement mechanisms). The governing ANC was a programmatic political party with broad-based support, and a strong commitment to inclusive policies. This political settlement had provided the foundation for a successful reformulation of economic policy along lines supportive of outward-oriented, productivity-enhancing growth – including a framework for the steady, incremental incorporation of newly empowered elites into the upper reaches of economic activity. The stage seemed to be set for a virtuous spiral of strong institutions, supportive politics, accelerating growth and a rising tide of optimism

But things have evolved more messily than had been hoped. Instead of a virtuous spiral, the elite bargain increasingly has frayed, putting pressure on impersonal institutions. This paper has focused principally on how interactions between the established (from the apartheid era) business sector and other stakeholders have influenced the way the economic bargain has evolved. As the analysis shows, the economic bargain has been fraying over the past two decades. Key drivers of this fraying highlighted in the paper include:

- An agenda of economic reform that was strongly influenced by the concerns of established, large-scale incumbents who were eager to expand beyond South Africa's borders (and hence supportive of market-opening reforms) – but who had less enthusiasm for a more proactive agenda to support productivity enhancement by newer and smaller firms.
- A set of negotiated agreements on labour law that balanced the interests of large-scale business and organised labour (with the latter at the core of the ANC's political alliance), but at the cost of failing to address the concerns of small firms and the unemployed – and, more broadly, contributing to the crowding out of a productivity-enhancing agenda by ongoing contestation over the distribution of rents between business and labour.
- The limited effectiveness of repeated efforts to provide a framework for black economic empowerment, anchored in predictable rules, that could be supportive of inclusive growth – and, instead, a growing tendency to address

BEE via discretionary, personalised deal-making that favoured political allies and, more broadly, engendered rising uncertainty. And

- As one consequence of all of the above, a progressive retreat on the part of the most productive firms from proactive engagement with South Africa's broader development concerns – increasingly responding less as 'national champions' and more as globalised firms looking to diversify beyond their historically central domestic market.

A not unreasonable implication of the above (and of the discussion throughout the paper) is that South Africa's ANC government lacked from the first a coherent and consistent vision of what economic development looks like. This is perhaps unsurprising, given the necessary priority (and enormity) given by the country's first president, Nelson Mandela, to the tasks of reconciliation and building the foundations of a just society – but a price was paid vis-à-vis economic management. Policy became more coherent over the course of the (1999-2007) presidency of Thabo Mbeki – but the global economic and financial crisis of 2008 knocked things off course again.

But perhaps more fundamental for the evolution of South Africa's political settlement than stresses within the elite bargain between business and government has been the second settlement dimension – the ongoing difficulty in incorporating non-elites into the political and economic settlement, and an associated diminution over time of hope that a better life would be achieved for all. To be sure, as Levy et al. (2015) show¹⁴, since the mid-1990s South Africa has been quite effective in providing services to the poor, and more broadly reducing absolute poverty. But Levy et al. also show that, relative to other middle-income countries, South Africa's economy is subject to a profound 'distributional cliff', with citizens in the top 20 percent of the distribution disproportionately well off, and those below the 30th percentile from the top disproportionately poor. A ladder of opportunity, along which families can improve their economic prospects over time, is largely missing.

The roots of this absent ladder of opportunity can be traced in important part to the dualistic economic structure inherited from apartheid and, related, the skewed distribution of political power and influence among economic stakeholders. Both the economic legacy and its political accompaniment have made it strikingly difficult to transform this structure, and provide a new platform of opportunity for South Africa's citizens. Also noteworthy (though not linked in any direct way to dualism) are ongoing challenges associated with strengthening the human resource base. It has proven extraordinarily difficult to address effectively the political, bureaucratic and educational constraints to turning around the inherited (anti-quality) apartheid-era system of bantu education. Further, while at the dawn of democracy very ambitious programmes were put in place to upgrade worker skills, these were dependent for success on complex, sector-specific multistakeholder formal governance arrangements involving business, government and organised labour. In most (though

¹⁴ In a companion ESID paper prepared for this project.

not all) sectors, the partnerships proved unwieldy; the result was weak accountability for how funds earmarked for skills-upgrading were actually spent. The abundant resources made available for training were misused, and little was achieved by way of actual skill improvements. South Africa remains a country where the majority of the country's children are not afforded the opportunity to acquire an education of the quality needed to become productive employees, where opportunities for skills upgrading are limited and where, more broadly, the economy generates limited opportunities for entrepreneurship, skilled employment and upward mobility.

One consequence of a weak economic ladder can be a turn to patronage politics and public sector jobs (and contracts) as an alternative political strategy for retaining power and, more broadly, maintaining stability. The turn to patronage appears to have accelerated over time, as evident in the evolution of BEE initiatives. A first generation of political activists was incorporated by the proactive initiatives of the late 1980s onwards by establishment business. A second generation (which could loosely be described as those associated with the networks of Thabo Mbeki) was incorporated through the BBBEE initiatives of the 2000s. But with the transition of political power to a new presidency (that of Jacob Zuma), the question arose as to how this new generation (and new set of networks) of aspirant elites would be incorporated economically. Increasingly, instances arose where economic policy decision-making seemed to be driven more by the desire for rent extraction, and opportunity creation for politically connected business, than by broader economic or political considerations. Two arenas of contestation that have been especially damaging economically were noted in Section IVB: contestation surrounding governance and procurement by infrastructure and transport-related state-owned enterprises (SOEs); and continued contestation over mineral resource rights.

This brings us to the third dimension of the political settlement, the quality of institutions. Table 2 presents data on the extent to which the combination of a fraying elite bargain and continuing difficulties in fostering economic inclusion have put stress on governance. As the table shows, since 1996 South Africa has indeed experienced a cumulative decline in both government effectiveness and control over corruption. But the table also shows that, even subsequent to these declines, the country's governance performance remains at the better end of the range vis-à-vis some major middle-income country comparators. Further, contrary to the tenor of day-to-day political discourse, the data showed very little change between 2011 and 2015, rather than accelerating decline.

One way to interpret this last finding is as evidence of 'dynamic tension' – namely that the institutional and political arrangements put in place in the 1990s have, so far, proven resilient enough to countervail patronage and predatory pressures. But a state of 'dynamic tension' is unlikely to be sustained indefinitely.

Table 2: Benchmarking South Africa’s governance

	Government effectiveness	Control of corruption	Government effectiveness	Control of corruption
	Score		Percentile rank	
South Africa				
1996	0.88	0.76	79	79
2003	0.68	0.34	74	67
2007	0.48	0.21	69	63
2011	0.41	0.03	66	59
2012	0.35	-0.16	64	55
2013	0.43	-0.12	67	55
2014	0.34	-0,11	66	54
2015	0.27	-0.04	65	55
Brazil 2015	-0.19	-0.43	48	41
Mexico 2015	0.21	-0.74	62	25
Turkey 2015	0.27	-0.11	65	55

Source: World Bank, Worldwide Governance Indicators.

The political and economic settlement put in place in the 1990s provided a quarter century of stability, and a platform for both poverty reduction and the achievement of economic gains on the part of elites (both new and old), through a combination of safety nets and engagement with the globalised economy. But the benefits of this settlement have largely bypassed the struggling middle. Consequently, with its limitations now evident, the settlement of the 1990s no longer offers a credible platform for economic dynamism or, more broadly, for hope among citizens that the life prospects of their children will be better than their own. In the absence of hope, the risks of a downward spiral loom large.

What is urgently needed is a renewal of the settlement to address systematically the economic challenges confronting the ‘middle’ of the income distribution – making resources available to this group in ways that improve their economic prospects, and strengthen the missing ladder of opportunity. As this paper has shown, there are formidable structural, economic and political obstacles to addressing these imbalances effectively. But in wrestling with the challenge, South Africa is perhaps only a more extreme example of a task which, it is becoming increasingly apparent, confronts middle- and high-income countries the world over.

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