SOUTH AFRICA CAN FIND INSPIRATION IN DENMARK'S SOCIAL MODEL

Labour and business' participation in the social compact



A report by
the Inclusive Society Institute
in collaboration with
the Economic Council of the Labour
Movement (Denmark)





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1. Introduction

In his 2018 State of the Nation Address, President Cyril Ramaphosa floated the idea of formulating a written Social Compact (Presidency, 2018). The aim is to have the alliance drive the solutions to the country's most pressing problems, which pivot around South Africa's flailing economy. Together they will have to tackle record levels of unemployment, widening wealth inequality, deep-rooted poverty and an economy struggling to gain traction.

For the Social Compact to deliver successful solutions, the relationship between those involved must be underpinned by cooperation, trust and respect. Whether these characterise the current relationship between Business and Labour, is doubtful. On its part, Labour is quick to threaten with strike action when their demands are not met. Recently, these often included double-digit or above-inflation wage increases (Mkentane, 2022).

Business, on the other hand, often blames stringent labour legislation as an obstacle to expanding the labour force.

It's a hostile relationship (Israelstam, 2022). This is evident by a recent statement released by the country's largest trade union, Cosatu, in which they called for nationwide strike action. It described the protest as a 'pushback and a response by the workers to the ongoing class warfare directed at them by both public and private sector employers' (BT, 2022a).

South Africa's Social Compact is clearly flawed at a time when the country requires cooperation the most. Labour will have to navigate its stance on how to strengthen its relationship with Business, as Business will have to do with Labour, if the alliance is to deliver any meaningful results.

To this end, this article looks to the Danish social model to draw some inspiration on how to build inclusive growth within the framework of a social compact aimed at addressing the serious challenges confronting the present-day South African economy.

The Scandinavian labour markets have for many years been able to balance the aims of high prosperity and employment with the aims of low poverty and equality. They have found a way to combine economic dynamism with general economic security.

This is in large due to a well-functioning collective bargaining system, a generous public welfare system and a strong social safety net, combined with flexible employment regulation. These features are the results of fortunate circumstances and long historical struggles, which cannot easily be replicated by other countries. But still, the Scandinavian model for social progress can inspire other countries in their search for the right social and economic balances.

In this report, we describe the Scandinavian social model, with a special focus on Denmark; and we sketch out how South Africans could take inspiration from the organisation of the Danish society.



2. Literature Review: Social compacts, the current-day South African economic realities and the Danish Business/Labour cohesive model

A Social Compact is widely understood to be an agreement among organised members of a society, generally Business, Labour and Government, to cooperate to achieve certain social benefits (C-Span, 2018). These agreements define the reciprocal rights, obligations and responsibilities between the different parties (O'Brien *et al.*, 2009). It has also been the strategy which underpins economic models in many industrialised economies (Luiz, 2018). An efficient social compact has proven a successful contribution to sustained positive economic performance in the social democratic countries in Northern Europe, like Germany, and the Nordic Countries (Fabricious, 2020; Luiz, 2018). The South African Government now hopes a formalised Social Compact will deliver similar results for the country's sluggish economy.

2.1 Social Compacts in the South African context

In the past, South Africa has relied on social compacts in differing formats to achieve certain goals. Most recently, Government together with Labour and Business forged a partnership to ensure a nationwide Covid-19 vaccination campaign (Presidency, 2022a). Such cooperative campaigns are generally developed during negotiations by representatives of Labour, Government, Business and Civil Society at the National Economic Development and Labour Council (Nedlac). Formed back in 1995, it was used as a vehicle through which parties were compelled to collaborate in rebuilding post-apartheid South Africa (Nedlac, 2020). Its aim is to promote growth, equity and participation through social dialogue. It's also the body through which President Cyril Ramaphosa is attempting to establish a formal written Social Compact.

2.2 The new Social Compact

From his first State of the Nation Address (SONA) in 2018, Ramaphosa has been calling for a collaborative Social Compact to drive economic recovery (Presidency, 2018). During his 2022 SONA, Ramaphosa again pledged to forge a framework for a *new* Social Compact within 100 days in order to grow the economy, create jobs and combat hunger (Presidency, 2022b).

The conclusion of the agreement has missed the 100-day time mark and is yet to be finalised. According to reports, a draft document put forward by government was rejected by the Nedlac partners. The draft report has not been publicly released, but some reports by the media may provide a glimpse of some of its contents:



Business Commitments:

- Localisation targets
- Investment targets
- Employment targets
- Employee representatives on company boards
- Restrictions on retrenchments
- Increase in taxes to support a larger social security net, like a Basic Income Grant

Labour Commitments:

- Concessions for small and medium enterprises as part of restructuring the Labour market (specifically, legislation and red tape that governs hiring and firing requirements)
- Support the restructuring of state-owned entities
- Commit to a multi-year wage agreement in the public sector
- Lowering entry-level wages to match the global average

Government Commitments:

- Accelerating structural economic reforms
- Cutting red tape, especially for small and medium enterprises
- Improving governance and performance of state-owned enterprises
- Taking action against sabotage of economic infrastructure and corruption
- Expanding the presidential employment programme
- Employing more public servants to fill critical vacancies
- Expanding social security

(Mahlaka, 2022a; Paton, 2022)

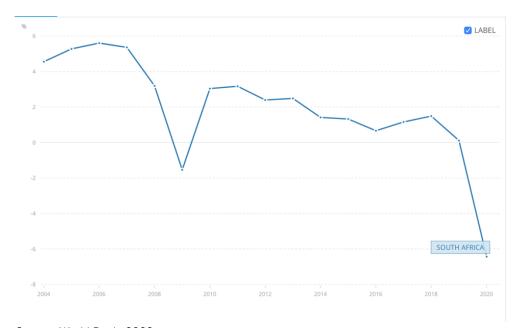
Both Business and Labour representatives at Nedlac have rejected the draft document (Mahlaka, 2022a). Business says government is asking too much, while Labour says it refuses to give up the hard-fought rights of workers. Discussions to finalise the compact continues.

2.3 The Time is now

Ramaphosa's call for the Social Compact framework comes as the South African economy is just scraping by. The country never recovered to the levels of growth seen prior to the 2008 financial crisis. In 2019, a year out from the Covid-19 pandemic, the economy plunged into a technical recession, the third one since 1994 (Sibeko, 2021). The lockdowns that accompanied the arrival of the Coronavirus led to further devastation; and the economy entered its deepest recession in a century (Naidoo, 2020).



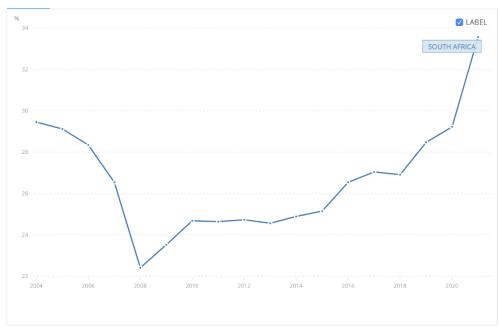
South Africa's annual GDP growth (%) 2004-2020



Source: World Bank, 2022a

The pandemic further added to the unemployment woes of South Africans. It's estimated that between 1,5 million and 3 million jobs were wiped out during the pandemic period (Casale *et al*, 2020). In quarter two of 2022 the country recorded an official unemployment rate of 33,9 percent (Stats SA, 2022a). When taking discouraged job seekers into consideration the rate is notched up to, 44,1 percent which translates to 11,6 million South Africans without a job (Stats SA, 2022a).

South Africa's annual Unemployment Rate (%) 2004 - 2021



Source: World Bank, 2022a



Whilst the domestic challenges have remained more or less the same over the past decade, South Africa is facing increasing international pressures. Inflationary pressures have accelerated globally due to increased consumer spending following the pandemic and Russia's invasion of Ukraine (WEF, 2022). In July, the country recorded a thirteen-year high CPI of 7,8 percent and PPI accelerated to 18 percent (Stats SA, 2022b). As central banks across the world move to stave off inflation by hiking lending rates, the South African Reserve Bank (SARB) has been left with little choice but to follow suit in order to protect the economy against capital outflows (Naidoo, 2022). The repo rate currently stands at 7 percent (as of 6 December 2022) (SARB, 2022), with further hikes to be expected. And as previously mentioned, in Q2:2022 the country recorded an official unemployment rate of 33,9 percent (Stats SA, 2022a).

Then there's the thorn in the side of any proposed economic recovery plan for South Africa: Eskom. South Africa continues to suffer rolling blackouts as the energy giant cannot supply sufficient electricity as a result of an ailing coal fleet — which wasn't properly maintained — together with deep-rooted corruption and the non-implementation of future energy plans.

By the end of August 2022, consumers have already been subjected to 100 days of varying stages of blackouts, the worst since the crisis started in 2008 (Volgraaff, 2022). Estimates as to the damage this may be causing the South African economy ranges from R500 million per day per stage of loadshedding to R600 billion annually (BT, 2021; Pieters, 2022; Bates, 2022). Government, together with Eskom, have provided a roadmap to address the crisis but, even if it is implemented successfully, it will take at the very least twelve months to be completely resolved, during which period the economy will continue to bear the brunt (Mahlaka, 2022b).

The South African economy is simply not performing well enough to uplift the millions living in poverty. Without a radical intervention, this seems unlikely to change in the near to medium future. The number of people classified as being poor, differ according to three income standards:

Upper-Bound Poverty Line
Person earning at least R1 335 (€75,28) per month

Lower-Bound Poverty Line
Person earning at least R890 (€50,18) per month

Food Poverty Line
Person earning at least R624 (€35,18) per month

(Stats SA, 2021)



South Africans living in poverty according to different poverty standards



Source: Stats SA, 2020

2.4 Social Compact buy-in

It is clear that urgent steps are required to support the expansion of the South African economy. President Ramaphosa hopes his new social compact can play a pivotal role in achieving this goal. For it to be successful, however, it requires the committed buyin from all participating parties. If past events are anything to go by, this may prove to be quite challenging, due to a strenuous climate between the parties involved. In this paper, we are focusing on Labour and Business' relationship with the rest of the involved stakeholders.

South Africa's Labour landscape is deeply rooted in the concept of collective bargaining. In 1924 the Industrial Conciliation Act was adopted, which made provision for the establishment of industrial councils (renamed bargaining councils in 1995), whereby registered trade unions could represent the labour force in negotiations with employers (Maree, 2011). This continues to serve at the core of collective bargaining in South Africa to this day.

By 1979, the South African apartheid regime was pressured to allow black trade unions, and therefore black members, to register, thereby allowing them access to the bargaining councils for the first time. By 1985, 33 unions formed a conglomerate under the Congress of South African Trade Unions (Cosatu), which assisted in breaking the stronghold of apartheid state (Cosatu, 2019). Cosatu formed the integral third arm of the tripartite alliance, together with the ANC and South African Communist Party (SACP) as the political heads (Cedras *et al*, 2013). While the ANC leads the alliance, it is understood that political and deployment decisions must be done in consultation with the SACP and Cosatu.

A poignant shift in the relationship between Labour and Government occurred on a small hill in 2012. Workers at the Lonmin Platinum mine embarked on a protracted strike when police opened fire (Al Jazeera, 2022). Thirty-four protestors were killed, and 78 workers were injured. A local miner's response in an interview reveals the depth of the distrust the incident created between Labour and Government (Butjie, 2017):



"Cyril was one of us, someone who had come through, understood. That's why it's all the more ironic that, 20 years later, Ramaphosa has emerged as one of the chief enemies of the miners he once led to freedom."1

It's been 10 years since the tragedy and despite no-one ever being held accountable for the incident, relations have seemingly stabilised somewhat between the two (Mahlakoana, 2022).

But labour-relations in South Africa continues to be among the worst in the world. According to a World Competitiveness Report released by the World Economic Forum in 2018, South Africa was ranked 136th out of 140 countries measured in terms of stable labour-relations (WEF, 2018). According to some experts this can be attributed to the low levels of trust between employers and employees (SBS, 2022).

The strained relations are further evidenced by media reports which depict a strenuous relationship between the two (Magubeni, 2022; Mungadze, 2022; Sithole, 2022). Protest actions, or the threat thereof, have become such an integral part of the negotiation process, that South Africa has a so-called 'strike season', named for the time of year when most wage negotiations take place (BT, 2022b). The general image of the relationship between Labour and Business, as portrayed in the media at least, is one of opposing teams focussed only on a win or lose outcome.

2.5 The Danish social model in contrast

First, a few facts about Denmark.

Denmark is a small country of 5.9 million people who are ethnically very homogenous. Denmark has been a collected and independent country for 1,200 years and is part of Scandinavia together with Sweden, Norway, Finland and Iceland. Denmark is the eighthrichest country in the world as measured by the gross national income per capita. This is due to a high level of productivity among workers in general. Denmark is not endowed with large natural resources and is not a free haven for the global elite. The income distribution in Denmark is fairly equal and corruption is almost non-existent.

In the box below, are the five basic features of the Danish social model.

¹ Cyril Ramaphosa rose through the ranks of organised labour. He served as both Deputy President and a non-executive director of Lonmin at the time of the Marikana massacre.

The Danish social model in outline

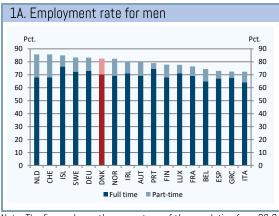
Five basic features mark the social architecture of the Danish economy:

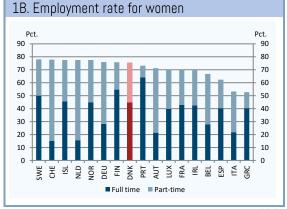
- A well-functioning collective bargaining system where large labour unions and employer organisations engage in a repeated wage-setting game underpinned by stable institutions. The collective agreements secure that social conflicts are resolved in a flexible manner. And most importantly, they secure that normal and low-skilled workers get a relatively high wage as well as employer-paid pensions.
- 2. A large, but highly productive public sector providing the citizens with a broad range of basic goods. In particular, healthcare, education, eldercare and basic social security are provided free-of-charge, and childcare is heavily supported. The quality of public schools is high, resulting in a relatively equal distribution of skills. The high public expenses are countered by a high tax burden, but taxes are generally levied on broad tax bases keeping the overall tax distortions at a low.
- 3. A flexicurity labour market i.e., a labour market with a high degree of flexibility for companies to adjust their production and for workers to move to more productive jobs; and a high level of income security for workers. The flexicurity system rests on three pillars: relatively lax rules for hiring and firing workers, relatively high replacement rates for laid-off workers, and compulsory public training programmes for the unemployed.
- 4. Good growth conditions for private businesses, including a well-educated labour force, high public spending on research and infrastructure, and well-designed regulations and tax rules that are enforced using third-party registration.
- 5. A high labour force participation rate among both men and women. This is underpinned by affordable public childcare.

2.5.1 The Danish social model ensures good living conditions for the broad class of workers

The Scandinavian labour markets are characterised by high employment rates among both men and women. This is a general feature of Northern-European countries and not something specific to Scandinavia, cf. Figure 1A and 1B.







Note: The figure shows the percentage of the population from 20-64 Note: The figure shows the percentage of the population from 20-64 years in employment. Data covers 2021.

years in employment. Data covers 2021

Source: ECLM based on Eurostat.

Source: ECLM based on Eurostat.

Normal workers in Denmark and the other Scandinavian countries receive a very high hourly wage. This can be seen by looking at the median hourly wage, that is, the wage rate in the middle of the pay-scale, where half of the employees earn less, and the other half earn more. The median hourly wage rate in the private sector in Denmark ranks number two among European countries, cf. Figure 2A. The other Scandinavian countries are also characterised by high wages for normal workers.

If one considers only low-skilled workers, a similar picture emerges. The typical lowskilled worker in Denmark earns a higher wage than in the other Scandinavian countries, cf. Figure 2B.





Note: The figure shows the median hourly wage in the private sector Note: We have applied same method as in Figure 2A. Unskilled workers (excluding agriculture and fishing) in companies with more than ten are defined as Elementary Occupations (group 9) in Eurostat's ISCOO8 employees according to Structure of Earnings Survey (SES), Eurostat. classification. Data covers 2018 and it is PPP-adjusted w.r.t. Danish For US we have used data from Bureau of Labour Statistics (BLS) and prices. Data for US is missing. Confederation of Danish Employees (DA). Data covers 2018 and it is Source: ECLM based on Eurostat. PPP-adjusted w.r.t. Danish prices.

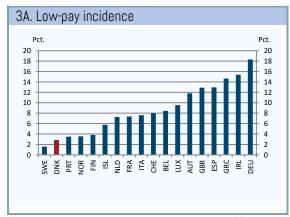
Source: ECLM based on Eurostat, BLS and DA.

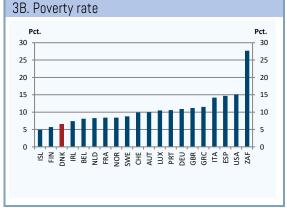
The high wages for normal and low-skilled workers means that the Scandinavian countries have very few low-paid workers compared to other countries. Low-paid workers are defined as wage earners who earn less than two-thirds of the median hourly



wage in the respective countries. The Scandinavian countries have some of the lowest rates of low-paid workers in Europe, as shown in Figure 3A.

Also, when panning across all citizens – whether employed or not – the Scandinavian countries have low poverty rates. In this region, citizens are defined as poor if their disposable income is below 50 percent of the national median; therefore, poverty thresholds vary across countries.





Note: The figure shows the ratio of wage earners above 30 years with Note: The poverty rate is defined as the ratio of the population with an an hourly wage less than 2/3 of the median hourly wage.

income below half of the median income in the specific country.

Source: ECLM based on Eurostat.

Source: ECLM based on OECD.

High wages – combined with redistributive taxes and generous social transfers – mean that the overall income inequality is low. Inequality can be measured by the ratio between the income of the poorest and the richest income groups. Figure 4 below, shows how much an average person from the richest fifth earns more than an average person from the poorest fifth.

In the Scandinavian countries, the richest fifth earns about 4 times more than the poorest fifth after tax and transfers. This income difference is low by international comparison. In the UK, the richest fifth earn 6.5 times more than the poorest, and in the US the richest earn 8.4 times more.





Note: The measurement for inequality is defined as the ratio between the first- and fifth-income quintile's equivalized disposable income. Data covers 2018 and 2017 for Iceland.

Source: ECLM based on Eurostat.

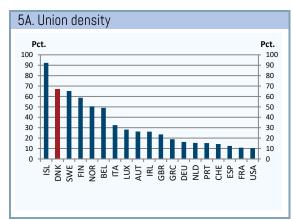
2.5.2 Strong social partners are a cornerstone in the Danish economy

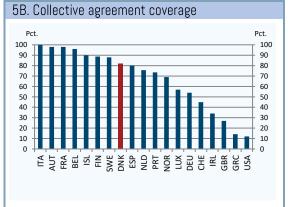
The Danish labour market model dates back to 1899 when the social partners agreed upon a basic set of rules regarding — on the one hand — the right of workers to unionise and strike under certain conditions and — on the other hand — the right of employers to organise their own production and hire and fire workers within the boundaries of collective agreements.

A prerequisite for the success of this model is that a large share of both workers and employers are organised in unions or employer organisations. Figure 5A shows the organisation rates of workers among 19 OECD countries. About two-thirds of Danish employees are organised in a union. Generally, the trade union movement stands strong in the Nordic countries, even though unionisation rates have been on a decline for the last 25 years.

The social partners have a strong voice in the political debate and are directly involved in the economic policymaking through formal and informal consultations with the government.







Note: The figure shows the ratio of employers who are members of a Note: The figure shows the ratio of employees covered by a collective union. Data covers 2020 or latest available observation for each agreement in 2018.

Source: ECLM based on OECD.

Source: ECLM based on OECD.

In the private sector, it is voluntary for employers to join the collective agreements, but many firms do so, sometimes due to union pressure. Overall, more than four out of five workers are covered by a collective agreement in Denmark. This puts Denmark in the higher end among the 25 OECD countries, as captured in Figure 5B. In the public sector, collective agreements cover all employees, whereas about three out of four are covered in the private sector.

The bargaining system is often referred to as a decentralised but coordinated bargaining system. Bargaining takes place on a sectoral level, where the more export-orientated manufacturing sector sets a wage norm which the other sectors then take into regard in their negotiations. Similar systems are found in Sweden, Norway and Iceland as well as in Germany, Austria and the Netherlands. According to the empirical literature on bargaining systems, such decentralised-coordinated systems are often able to combine economic dynamism with high income shares for normal workers (Aidt & Tzannatos, 2008; OECD, 2018).

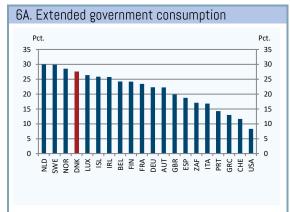
2.5.3 The Danish welfare state provides equal opportunities

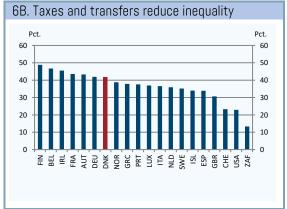
In Denmark, a relatively large share of the national income is redistributed among its citizens through public welfare and social transfers. The government provides a broad array of basic goods free-of-charge including healthcare, education, eldercare and social security. As a result, consumers can spend less on those goods. In a sense, the government expands the households' budget for consumption. In Denmark, government spending amounts to 27 percent of the households' extended consumption possibilities, as illustrated in Figure 6A below. By international comparison, this is a relatively large share.

The Scandinavian welfare states are to a large extent based on tax financing rather than insurance-based financing. Thus, healthcare, eldercare and many social transfers are mostly financed by general taxes as opposed to personal savings and insurances. This means that access is universal and that the quality does not depend on one's income. This has the effect of reducing the overall inequality.



Taxes and transfers reduce the inequality as measured by the Gini coefficient with 42 percent, illustrated in Figure 6B below.



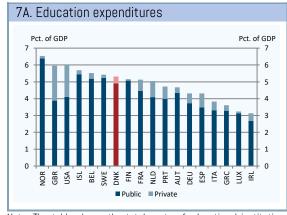


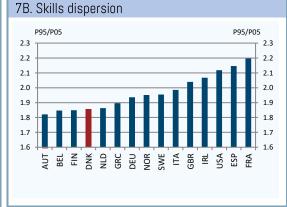
Note: The figure shows the extended government consumption as % Note: The figure shows the reduction of Gini in percent before taxes of households' total spendings. Thus, high extended government and transfers to Gini measured on disposable income. consumption indicates that the government provides many direct Source: ECLM based on OECD. transfers to "actual individual consumption".

Source: ECLM based on OECD.

In particular, public spending on education is high in Denmark. Education at all levels is provided free-of-charge, including secondary school, higher education and upskilling for employed and unemployed adults. Consequently, total spending on education amounts to 4.3 percent of GDP, which is almost exclusively government spending. This is shown in Figure 7A below.

The high level of public spending is countered by a high number of pupils and students, meaning that the spending per pupil is close to the OECD average. In international surveys of literacy and mathematical abilities, Denmark does not rank in the top perhaps due to "softer" skills being prioritised in the school system. However, the gap between the more and less skilled is relatively low. If we measure the mathematical abilities of adults and compare the scores in the top and in the bottom, the dispersion of abilities is relatively low in Denmark. This is shown in Figure 7B below. The dispersion is higher in countries with more polarised school systems such as France and the US. In this way, public schooling in Denmark is a cornerstone in ensuring equal opportunities.





Note: The table shows the total costs of educational institutions Note: The figure shows the dispersion in mathematical competences according to Education at a Glance 2022, OECD.

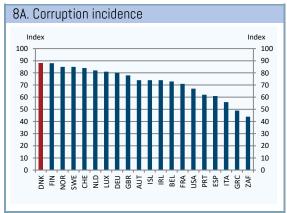
among adults according to the PIIAC survey, 2019.

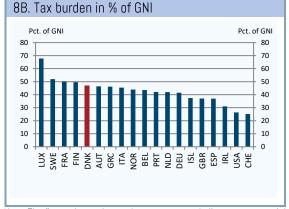
Source: ECLM based on OECD.

Source: ECLM based on OECD.

The fact that the public sector is relatively large in Denmark does not mean that it is ineffective. In spite of its size, the Danish public sector has a high effectiveness according to World Bank estimates (WB, 2022b). Furthermore, corruption is almost non-existent (see Figure 8A below).

The government expenses are countered by high taxes. This is reflected in the tax burden, which measures the share of total income that is administered by the public sector. As shown in Figure 8B, the tax burden in the Scandinavian countries is in the higher end among OECD member countries.





Note: Corruption Perceptions Index (CPI) is the most widely used Note: The figure shows the total tax revenue excluding taxes on social global corruption index and it measures how corrupt each country's expenditures in % of GNI. public sector is perceived to be.

Source: ECLM based on OECD.

Source: ECLM based on Transparency International.

'Flexicurity' is a recipe for a well-functioning labour 2.5.4 market

The Danish labour market is characterised by flexible regulation when it comes to laying off and hiring labour. In countries such as Germany, France and the Netherlands, firms face stricter rules when hiring and firing workers (see Figure 9A below). It is also relatively inexpensive to lay off employees in Denmark, compared to other countries, where substantial severance pay is more common.

This flexibility means that companies can adjust more easily to changing economic circumstances. It also means that companies face relatively low risks when creating new jobs. In this way, flexibility helps to ensure more job openings in the economy – even during bad times. This is also an advantage for employees.

But a high level of flexibility requires a strong social safety net for the employees. Without a social safety net in the form of unemployment benefits and tax-financed public goods, employees would demand longer terms of notice and higher severance pay. The safety net is an important reason why employees accept contracts with short terms of notice.

Compared to other countries, one gets a relatively high share of the lost salary income reimbursed if you become unemployed - at least if one is at the lower end of the payscale (see Figure 9B below). During the last decades, however, the replacement rate of



unemployment benefits for the average wage-earners has been hollowed out. This threatens the long-term balance of the unemployment system.





Note: The index measures the flexibility in terms of hiring and firing Note: The figure shows the net replacement rate in case of employees. The data covers 2019 and it is based on a questionnaire unemployment for low-paid workers (less than 67% of the average survey among business managers answering: "To what extent do wage). national regulations allow for flexible contracts in terms of hiring and Source: ECLM based on OECD. firing employees."

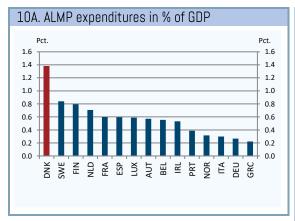
Source: ECLM based on World Economic Forum.

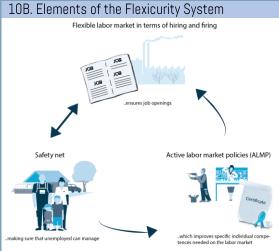
The relatively lax rules for assigning and dismissing workers and the relatively strong social safety net form two of the three pillars of the so-called 'Flexicurity' system. The last pillar consists of an extensive use of active labour market programmes to increase reemployment of the unemployed. Participation in various programmes of job search assistance, training and activation is required in order to receive unemployment benefits. Further, there are strict requirements regarding the number of jobs to apply for, when to attend meetings with the employment office, and which job offers one can turn down. These types of workfare programmes strengthen the qualifications of the unemployed and increase their chances of reemployment. In addition, public training for employees helps people keep their skills up-to-date and prevents job-losses.

Denmark is by far the country in the OECD with the highest expenditure on active labour market policies. The spending on active labour market programmes amounts to 1.4 percent of GDP. This is shown in Figure 10A below. Correspondingly, the share of unemployed participating in training and education is one of the highest among EU countries.

Figure 10B shows the three pillars of the flexicurity system – that is, flexibility in terms of hiring and firing, a strong social safety net, and an extended use of active labour market policies.







Note: The figure shows the average yearly expenditures to active Note: The figure shows the three essential components of the labour market policies (ALMP), 2015-2020.

Flexicurity model.

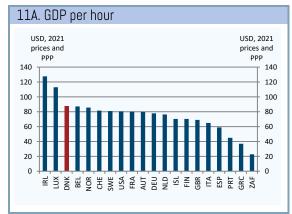
Source: ECLM based on Eurostat.

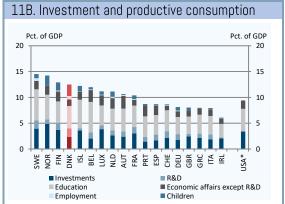
Source: ECLM.

2.5.5 It is easy to start and operate a business in Denmark

The productivity of workers and businesses in Denmark is high. Looking at GDP per hour, the Scandinavian countries rank top in the world (see Figure 11A below). This is mainly due to high public spending on infrastructure, research and development, education and spending items underpinning a high employment (affordable childcare and employment policies). The Scandinavian countries all have high government expenditures on investments and 'production-enhancing' consumption, as illustrated in Figure 11B below. Thus, firms have access to good infrastructure, technical knowledge and a welleducated workforce.

Historically, Denmark has pursued a quite liberal industrial policy, where government has not come to the rescue of companies in trouble. Denmark does not have large, subsidy-requiring companies within, for example, the mining and heavy industry.





Note: The figure shows GDP per hour worked in 2021. Please note that Note: The figure shows government investments and productive the GDP per hour in Ireland and Luxembourg are inflated by both consumption decomposed in six sub-groups. countries serving as tax-havens.

Source: ECLM based on OECD.

Source: ECLM based on OECD.



Furthermore, the costs and administrative burdens when starting a new business are relatively low. This is, for example, evidenced by the World Bank's data on the costs of starting a new business, which are indicated by an average index in the first column of Figure 12 hereunder. According to The World Economic Forum, Danish business leaders do not view government requirements as very burdensome, as shown in the second column of Figure 12.

Finally, even though taxes are high, they are collected in a relatively non-distorting way. In particular, they are levied on broad tax bases, which makes it possible to keep the marginal tax rates low. As a consequence, the high taxes only distort the incentives of workers and investors to a lesser extent, and therefore taxes do not hamper growth much. This is shown in the last three columns of Figure 12, where the tax rates on working an extra hour and investing an extra dollar are reported.

It is easy to start and operate a business in Denmark

The figure shows different parameters relating to the complexity of starting a business in selected OECD countries.

	t of starting iness		inistrative iirements		rginal tax on income		ginal tax on income		ginal tax on orate me
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П	0,1	监	3		32	+	39	•	-25
H.	0,2	Ш	3	Ш	36	+	41	П	-12
	0,2		4	H	39		43		-3
+	0,5	#	4	+	40		44		3
+	0,7	-	4		40	#	48	+	7
П	0,7		4	#	42		49	H.	8
#	0,8	H.	5	6	45		52	#	10
	1,0	П	5		45	#	53	П	10
≝	1,5	Ш	5	+	45	8	54	Ш	1
	1,6	#	5	+	45	H.	55	45	12
#	1,9		5	•	47		56		12
®	1,9	•	6	监	47		56	+	12
+	2,3	+	6	+	47		57	#	13
6	3,9		6		52	8	58		13
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П	13,8		9	П	65	П	68	噩	15

Anm.: 1) Cost of starting a business is measured in % of GNI (World Bank). 2) Administrative requirements are measured as start-up procedures required to start a business, including interactions to obtain necessary permits and licenses and to complete all inscriptions, verifications, and notifications to start operations (Worlds Bank). 3) Marginal tax on low income is the marginal rate of income tax for low-paid workers (less than 2/3 of average income). 4) Marginal tax on high income is the marginal rate of income tax for high-paid workers (more than 5/3 of average income). 5) Marginal tax on corporate income measures how an increase corporate taxes will affect incentives to reduce or increase investments in the company. A low marginal tax on corporate income implies higher incentives to increase investments.

 $Tabel: \bullet \ Kilde: AE \ based \ on \ World \ Bank \ and \ OECD \ ('Taxing \ Wages \ 2021' \ og \ 'Corporate \ Tax \ Statistics: \ Third \ Edition') \ And \ AE \ Bank \ Ba$

Source: https://www.datawrapper.de/ /lhINB/



2.5.6 Fortunate circumstances, social struggles and gradual adjustments

The Danish social model was built over many years and is, in many ways, a result of fortunate circumstances and specific power structures in the past. Although other countries can, surely, take steps towards a society more like the Danish, the process of getting there will not be easy and will not be fast.

In the global market, Danish firms have specialised in high-value-added products and services that do not rely on the availability of cheap labour. This is, to some extent, a consequence of unions raising wages across the board and the school system ensuring a high productivity among low-skilled workers. That is, of course, not a panacea for prosperity and equality in all countries. Nonetheless, the history of the Danish model might provide some useful take-aways for South Africans.

At the close of the 19th century, agriculture was still the principal industry in Denmark, and was dominated by a confident farming class, which organised a strong cooperative movement. 'Folk high schools' became a stronghold for general education. Around 1900, rapid industrialisation increased growth in the cities and created strong trade unions as a counterweight to private capitalist power.

From the beginning, the trade union movement and the Social Democratic Party were linked politically as well as organisationally. In Denmark and the other Scandinavian countries, the interaction between unions and the party became the key driving force in the development of a highly vital welfare model. The trade union movement secured better pay and improved working conditions in negotiations with the employers. But where collective agreements were unable to provide adequate possibilities, the political friends of the trade union movement took over. Economic inequalities were evened out through tax-funded services within education, healthcare etc., and through a system of economic benefits in case of unemployment, illness and old age.

The first great challenge — and also the first huge leap forward — was the Great Depression in the 1930s. Fearing that mass unemployment would spur uprisings and antidemocratic sentiments, the politicians agreed on a social reform that gave social welfare benefits to those in need as a right — not as alms.

In the middle of the 1900s, economic and social changes were generated by two vast changes: An extensive urbanisation and women entering the organised labour market. From the 1950s, the standard of living exploded and the share of a generation achieving a higher education increased dramatically. A significant part of this income growth was used for expanding public welfare.

The pursued economic policy supported growth in the private sector. Beginning from the 1950s tax legislation, giving the companies very generous depreciation possibilities on all kinds of machinery made a crucial contribution to the renewal of the Danish industrial sector. Furthermore, the prioritisation of public welfare created a domestic market, which gave Danish industry the possibility of becoming a global market leader in valuable niches such as medical products. Likewise, the demand for more environmentally sustainable energy supply after the oil crises resulted in government support for windmill technology, which made Denmark a leading producer of windmills.



After the oil price shocks in the 1970s, the unemployment rose dramatically and reached 11 percent in 1981. The rise was expected to be temporary, but it lasted throughout the decade, leading to a surge in the public debt and the current account deficit. At that time the relationship between the social partners was relatively cold and untrustful, although the rules of the bargaining system were respected.

Since then, two important aspects have been added to the Danish model.

Firstly, occupational pensions have been included in the collective agreements. These personal savings supplement the universal pensions and have meant a massive relief for the public finances. Further, the statutory retirement age is being raised in concurrence with the life expectancy. This is combined with early retirement schemes for the worn-out.

Secondly, the requirement that the unemployed participate in active labour market programmes was introduced in the 1990s. This reduced the unemployment rate significantly – from about 10 percent in the 1980s to about 4,4 percent in the 2000s. Other factors such as clever fiscal policies and lower unemployment benefits contributed to this development. But the introduction of workfare explains the lion's share of the declining unemployment rate (Kreiner & Svarer, 2022).

Regarding the relationship between the social partners, it has gradually improved, partly due to Labour and Business both prioritising job creation when jobs were scarce, and partly due to the government delivering welfare, social security and a fair distribution when Business would not.

In short, the Danish Model is not the result of one big master plan. Creating social progress for people with normal and lower incomes has been a long and gradual process — fighting and striking balances with employers and centre-right political parties. It has been a step-by-step process in interaction with the changing economic conditions, and sometimes the steps have led in the wrong direction.



3. Navigating the new Social Compact for a better future amid old problems

In 2020, President Cyril Ramaphosa tabled his Economic Reconstruction and Recovery Plan. Two years later, during his State of the Nation Address, he called on all stakeholders to commit to a new social compact to give effect to the plan. As we're nearing the fourth quarter of the year, the document is yet to be finalised. While the country's extensive economic problems are urgent, the drivers of the solutions are seemingly dragging their feet.

It's been 28 years since the first democratic dispensation, yet millions of previously disadvantaged black South Africans continue to live in abject poverty, with little to no hope of an improved future. The deep rootedness of corruption is visible in the country's decaying infrastructure, deteriorating governmental services and a state-owned energy supplier who can't keep the lights on. This has detracted from South Africa's attractiveness on the international stage, with other African and emerging countries doing a far better job of luring investors. It is investment the country can ill-afford to miss out on as the tax-base continues to shrink due to emigration, low levels of economic growth and increasing levels of unemployment.

Seeing as the state cannot create sufficient jobs to support the 11 million unemployed South Africans, with a projected economic growth rate of 2,1 percent in 2022 and 1,6 percent in 2023, urgent cooperative measures are required. Government, Labour and Business will have to pull together to see any plan bear fruits. This is, however, hampered by the low levels of trust characterising the relationship that Labour has with Government and Business. Labour is also known to negotiate with a frozen mandate, unwilling to be flexible in its demands. If Ramaphosa has any hope of driving economic recovery with the social compact at its core, Labour's often harsh stance will have to be reconsidered.

3.1 Labour's approach

3.1.1 Business' stance

Business is seeking a more immediate relationship with Labour. Some require Labour to move away from its continuous calls for widespread and inclusive consultations on every aspect before a plan can move ahead. The economic crisis leaves little time for lengthy deliberations. Instead, Business is seeking a bilateral approach, which it hopes will speed up these types of processes.

It further urges those Labour representatives to move away from long-held ideologies where the state is the controlling entity of an economy and allow for partial or full privatisation to take over where necessary. Labour has been quite vocal in its opposition against privatisation of state-owned entities. These include the unbundling and partly privatisation of the struggling Eskom.



Moreover, Business wants Labour to commit to an end goal of adding more employment to the economy. In one conversation, former Finance Minister Trevor Manuel's quote resurfaced:

'Jobs are bloody hard to come by, all, jobs, and the more adjectives you add, the harder it gets'

Some suggest that Labour needs to drop the adjectives when it comes to its demands for job creation. Examples include 'fair' or 'inclusive' as prerequisites for jobs being created. Understanding that getting people onto the income ladder is the core concern. This should however still be done in a regulatory and legislative environment, which prevents exploitative practices.

If job creation is embraced as the single goal, it may largely halt meaningless actions that cause further economic damage. One such example, is Cosatu, who recently called for a nation-wide shutdown with regard to the increasing costs of living. The stay-away gained little to nothing but it did remove a handful of people from their place of work, causing damages to businesses and ultimately the economy.

This is in line with one suggestion that trade unions move away from the current Positional Bargaining model to an Interest Based one, with the focus on a collective goal as opposed to entering negotiations with a frozen mandate. This will also reposition the process to have a win-win outcome, where currently the general experience is a win-lose situation.

Small and medium-sized businesses are viewed as the job drivers in South Africa. Yet, they say they are being strangled by stringent labour laws. Most notably, is a company's ability to retrench or fire an unproductive employee. South Africa's regulations that govern this process are notoriously complex and seemingly tend to give employees more benefit compared to the employer. There has long been calls for the relaxing of the so-called hiring and firing processes. It has been noted that these stringent regulations have led to companies limiting the number of staff they employ, thus hampering job creation.

Business understands it cannot operate without Labour. It also has a firm grasp on the social responsibility it has in a developing country such as South Africa. What it's calling for is more flexibility and accommodation from Labour, to allow for rapid expansion of Business to the long-term benefit of all in the country.

3.1.2 Labour's stance

Labour says it too understands its role in making the Social Compact work. Although Labour enjoys an amicable relationship with Business at a Nedlac-level, it's quick to add that it's not there to make friends. While Labour says it welcomes the opportunity for consultative processes on important matters, it has accused Government of delaying tactics, citing the conclusion of the Social Compact document as an example.

Labour representatives' further state that there is no need to seek red herrings as solutions to the country's economic woes. Instead, it believes that Government already controls the necessary levers to make a meaningful impact on the economy. Among



Labour's suggestions is the implementation of a wealth tax to support fiscal spending measures, which could stimulate economic growth. Another is the strengthening of the South African Revenue Service to better enforce tax compliance in the country. Labour says there are less contentious ways to go about creating growth in the economy than what is being proposed by some.

It is further clear in its stance that Labour representatives are there to protect and promote the interest of workers. This is done to ensure more inclusive economic growth going forward, while ensuring that workers share in the success they help to create. Labour fought hard to secure a minimum wage requirement of R23,19 p/h, which it believes will assist in narrowing the inequality gap that plagues South Africa. It often accuses management of big companies of displaying capitalist greed by paying their shopfloor employees pittances while the executives pocket millions in salaries and bonuses every year (Steyn, 2022).

This also strengthens Labour's argument that there cannot be any relaxation of the Labour laws, which are meant to protect employees. It's understood that the initial Social Compact document did suggest certain amendments to the hiring and firing process, with the aim to assist small and medium enterprises. This has since been removed from the draft document on the insistence of Labour that it will not agree to the suggested Labour law reforms.

One Labour representative says that the deep levels of distrust by some workers towards Business stems from South Africa's racial past. Some business owners are white individuals, while the working class is predominantly black South Africans. For many, this highlights the racial divide and the deep income and wealth inequality that continues to exist 28 years into a democratic South Africa.

Labour believes it's the only party currently providing credible solutions to the country's extensive problems, calling on both Business and Government to catch up. It shares a harsh view of Government's seeming inability to take control of the crisis, saying it lacks the focus required to lead the successful implementation of a strategic solution to the country's economic ills.

3.1.3 Towards Ramaphosa's Social Compact

South Africans are seeking a revitalisation of the economy, society and its body politic. The President is insisting a cooperative relationship is the way to bring this about. He has called on Business to take national strategic objectives into consideration in its decision-making process and Labour needs to promote the interests of workers while seeking business sustainability and job creation. From its side, Ramaphosa says Government will create an enabling environment while deploying public resources strategically. The President has emphasised that all parties need to come to terms with the trade-offs that may be required in the process. He faces a tall task, however, to get the required support, as the trust in Ramaphosa and his Cabinet has been watered down. This is largely due to years of inaction to curb gross corruption, the inability to uplift the majority of previously disadvantaged South Africans and the many failed attempts at implementing one or more economic turnaround strategies.



While Labour publicly supports the drafting of a Social Compact, when speaking to representatives its frustration is palpable. Meanwhile, Business has openly criticised the process, calling for the Social Compact to be put aside, saying the lengthy consultations are taking up too much time when what is needed is immediate action. It further suggests focusing instead on other strategies — like the President's Economic Reconstruction and Recovery Plan — that have already been finalised.

In principle, Labour and Business understand that a strong Social Compact is required. The specific drafting of one, however, is seen as yet another time-wasting exercise with little faith in the outcome.

In some corners, a successful Social Compact already exists in South Africa. A story shared by both sides is that of the Mining Sector. The tumultuous relationship between local mining companies and employees is well documented. In 2020, the Covid-19 pandemic shifted the dynamics, as it forced the formation of a single goal. Organised Labour, employers and communities had to work together in achieving safety for everyone involved. This forged a new relationship built on a shared outcome with mutual respect at the core, which they hope will set the president for future negotiations.

Perhaps Ramaphosa and the rest of the social partners can take a leaf out of mining's book. Dotting down shared goals, as opposed to finding common ground on every other aspect may be a far quicker process, as the problems South Africa face are clear: unemployment, inequality, poverty, and sluggish economic performance. Given the urgent nature of the problems, it seems Business, Labour and Government will have to find a way to work together even if a climate of distrust exists among some.



4. Drawing inspiration from Denmark's social model

4.1 Deciding South Africa's economic model

The South African economic model remains contested.

On the one extreme there is a push for the nationalisation of key industries, the establishment of a state bank, the preservation of State-Owned Enterprises (SOEs) at any cost and the central role of the State in engineering the economy. This seems the stance of organised labour and the more left-wing sections of the ruling party. The Danish model, albeit with a larger than average public service, suggests a smaller role for state-owned enterprises. So too, the creation of an enabling environment for the private sector to thrive, is central to Danish government policy. This is evidenced by their flexicurity labour market and well-designed regulations and tax rules that promote good growth conditions for business.

On the other side, the South African Reserve Bank, Treasury, and the more conservative sections of the ruling party — and the main opposition parties — lean more closely towards more neo-liberal economic policies to guide the South African economy. There is a higher reliance on trickle-down economics, than on debt-financing and expanded social safety nets aimed at improving society's standards of living. The Danish model has shown that generous social safety nets and a market economy can not only thrive side by side, but also puts more consumption spending in the pockets of the ordinary workers — which in itself stimulates GDP growth — and, given the safety net security, allows for a more flexible and productive labour market. The smaller role for SOEs is offset by strict regulation of monopolies and markets for infrastructure-like goods and by a political system that is quite robust to lobbyism and corruption.

Officially, South Africa has positioned itself as a developmental state, meaning that it is en route to its final economic destination. What that destination is, is not yet settled, albeit that it is constitutionally committed to the progressive realisation of socioeconomic rights, including the right to work, healthcare, security and education, amongst others. Denmark has developed a well-functioning welfare state, in which a vibrant free market co-exists with adequate safety nets to ensure a society generally free from abject poverty and severe inequality. It understands that social upliftment leads to economic growth, and that investment therein is not a choice, but an imperative. Although this requires higher taxation, quality services, delivered virtually corruption free, results in a content and productive society.

Step one on the way forward is for South Africa to agree and commit to its economic path; and for stakeholders, principally Labour, Business and Government, to enter into a pact to ensure its achievement. This paper suggests progression towards a social democratic welfare state is best to ensure social justice and equality.



4.2 Designing an implementation pathway

It needs to be understood that the achievement of the welfare state is not an event, it is a decades-long process. Denmark, now the eighth-richest country in the world, has been developing its welfare state since the early 1900s. It has progressively advanced by systematically chipping away at poverty and inequality.

The provision of tax-funded health services, education, elderly- and childcare, unemployment benefits and its pension regime was introduced alongside a growing market economy. Denmark shows us that comprehensive welfare benefits require two ingredients: higher tax contributions and low unemployment. Supplemented by good healthcare and education, which provides the foundation for a productive and a more industrialised and technologically advanced economy.

Thus, the lesson to be drawn from the Danish experience, is that a comprehensive set of safety nets need to be envisioned, designed and agreed upfront, and that an implementation pathway needs to be designed, whereby benefits are systematically introduced as and when economic conditions dictate. With the end goal in mind, the progressive tax and public spending regime can be designed and synchronised with the economic growth trajectory. Crucial though, is that a viable social safety net requires an effective public administration with extensive information on each social security recipient. Thus, the government administration needs to be improved as well.

That said: An important lesson from the Danish social model is that broader society must have the courage to start with the implementation of the safety net regime even when the economy is constrained, albeit within the country's fiscal means. It was within the context of the 1930 Great Depression, that Denmark agreed on a social reform that gave social benefits to those in need. The South African debate with regard to a Basic Income Grant (BIG) comes to mind. Whilst it is not within the country's means to introduce a fully-fledged social welfare system, the introduction of a more affordable BIG could serve as the foundation on which such a system can be built as the economy strengthens and more people enter the job market.

4.3 Developing an inclusive social compact with triangular commitment

The Danish social model tells us at least eight things:

- The nation as a whole must commit to the country's social model. Not only must
 they commit, but each sector must also understand their contribution in the quest
 to achieve that vision. For this the 'rules of the game' must be agreed upon,
 understood and respected by all in society.
- There needs to be a high level of trust between the stakeholders and between them
 and society as a whole. This trust is developed through the delivery of high-quality
 services within a virtually corruption-free environment. The Danish model has
 illustrated that people are prepared to pay higher taxes if they know they will
 receive quality services and that their contributions are spent with high fiduciary
 care.



- There needs to be a clear delineation between that for which the state is responsible, and the role of the market. In Denmark, the state is focussed on delivering the social services and the broader infrastructure of the state, and on the development of the regulatory framework for nurturing the free market. The state understands that a growing free market is the cornerstone for job creation and growing tax income, without which the delivery of welfare services will not be viable. Regulations are designed to ensure that it is relatively easy to do business, especially for SMMEs.
- In a similar vein, Business and Labour understand that one cannot succeed without
 the other. Both are committed to the system of bargaining councils, which, in turn,
 underwrite the notion that worker conditions need to be constantly improved
 within the limitations of enterprise affordability and the need for a fair return on
 shareholder investment. A discontented workforce neuters productivity, and an
 unprofitable business discourages the further investment required for growth and
 job creation.
- To find the consensus needed to implement the ideals set out above, requires a
 well-functioning collective bargaining system where large labour unions and
 employer organisations engage in a repeated wage-setting game underpinned by
 stable institutions. The collective agreements secure that social conflicts are
 resolved in a flexible and non-confrontational manner.
- The presence of welfare safety nets allow for less stringent and more flexible labour laws. This is made possible due to a worker being able to continue his or her life with relative financial security, post being made redundant. South African Business' insistence on more flexible labour laws should therefore be met with them embracing a more sustainable and comprehensive safety net regime for the unemployed.
- A comprehensive social welfare model requires less government involvement in the
 market. Its role should be limited to creating an economic environment in which
 the private sector can flourish. It should refrain from clinging to loss-making and
 unsustainable SOEs. The South African authorities will need to adjust their mindset
 from a penchant for over-regulation, to ensuring greater ease of doing business.
 For a safety net regime to thrive, the fiscus will require higher taxes, which will only
 be made possible if enterprises are allowed to flourish.
- Social welfare benefits must be considered a right not alms. This means that, as
 with all rights, obligations need to be attached to the benefits. In Denmark this
 includes, for example, the obligation of all workers and enterprises to contribute
 towards the fiscus through salary contributions aimed at financing the the welfare
 system (unemployment, retirement benefits, etc.), and by compelling the
 unemployed to seek work and continually upskill themselves. The introduction of a
 BIG in South Africa would do well in taking such an approach to heart.



5. Conclusion

South Africa finds itself in the perfect economic storm. It was never able to really get back on track following the 2008 financial crisis. The Covid-19 pandemic compounded its problems. Insufficient electricity supply coupled with national and international political and economic pressures are squeezing South Africans into an unmanageable position. It's a tight spot, from which the country can only escape if Labour, Business and with Government decide to pull in the same direction.

They need to understand not only the mammoth task at hand, but also their responsibility in finding the way out. Government needs to be focussed on developing the plan to get the country back on track. They will have to create a better environment in which business can thrive. Business will have to accept that it needs to contribute to a greater degree towards social upliftment and justice, with not just profit, but also social upliftment as a bottom-line goal. In turn, Labour must develop the art of continuing the fight for the betterment of the lives of workers, but in a more flexible and accommodating manner. And all three with the greater good in mind.

The Danish model suggests that Government, Labour and Business each have distinctive roles to play in building the nation, and that one cannot succeed without the other. The overriding approach is therefore to synchronise their interests in a manner that does not undermine each other, but which is agreed in accordance with the national vision, ethos and value system.

South Africa, the authors suggest, should draw inspiration from the Danish social model. It will require great coordination and new thinking. To which end it is proposed that Nedlac, also through the inclusion of civil society, be expanded to be more representative of broader society. And that a process be put in motion to agree the vision, the ethos and value system capable of broad public appeal.

It is recommended that in striving towards these goals, a half-measure approach should be avoided. Instead, the requisite social compact needs to be developed comprehensively, inclusively, in a properly structured manner, and to the benefit of all — the broader public through government, the workers through the unions, and business, through their investors.

In short, the national interest above narrow sectoral advantage.



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