An important question in development remains whether and to what extent economic growth is inclusive of the full spectrum of the income distribution. The literature has identified multiple potential transmission channels between inequality and growth, suggesting direct impacts, and indirect channels, and with causality running both from growth to inequality, and from inequality to growth, and in each instance with the nature of the association both benevolent and perverse. Settling the matter of causality has remained difficult econometrically, particularly for panel data. This suggests the importance of considering time series evidence on the relation between growth and inequality, since time series techniques allow questions of causality to be addressed directly.

In this paper I examine South African time series data to assess the nature of the association between growth and inequality. South Africa is pertinent since it has relatively reliable inequality and economic data over long time runs, it reports high levels of inequality, and policy post-1994 was sharply reoriented toward a prioritization of poverty and inequality. The South African evidence is considered in relation to the international theoretical and empirical literature, and descriptive data similarly provides comparative context.

Our core analytical finding is that growth and inequality benevolently co-determine one another in South Africa: growth lowers inequality and falling inequality in turn serves to stimulate growth. But there are additional statistically and substantively significant drivers of inequality in South Africa. Labor absorption (job creation) is the single most important of these. The opening of the South African economy post-1990, the lowering of credit rationing in the economy in the 1990s, and the fiscus all prove to exert important influence on the net inequality outcome also. The findings imply that the strongest policy levers suitable for raising average welfare and lowering inequality, are policies designed to stimulate growth, increase labor absorption, extending credit to entrepreneurs and ensuring household credit is broad-based, and amelioration of the disruptive impacts of globalization on labor markets. Policy successful in raising growth and lowering inequality, will likely have to combine a range of policy interventions, rather than focusing on single mechanisms.