South African Economic Development in the Light of the New Institutional Economics

HENRY KENNEY

The importance of institutions in shaping economic development is now widely acknowledged. Institutions matter because they affect incentives. The institutional framework of a society determines the degree to which its members will pursue wealth-creating activities. But the historical record shows that effective—that is, growth-promoting—institutions have been the exception and not the rule. In the nineteenth century, relatively few countries achieved sustained economic growth. Britain, the United States, France, Germany, and Japan come to mind. More recently, the East Asian highfliers—South Korea, Taiwan, Hong Kong, and Singapore—have grown impressively. But a country can achieve sustained growth and then lose momentum, lapsing into stagnation and even decline. Argentina is perhaps the classic example. Economic growth is hard to come by and easy to forfeit.

The new institutional economics has given us a way to understand why economic development does not come easy. This type of analysis began with Ronald Coase's insight that when exchange is costly, institutions make a difference (1960). In a world of zero transaction costs, institutions do not matter. Any assignment of well-defined and enforced property rights will result in an efficient outcome because different parties will have an incentive

Henry Kenney is senior lecturer in the department of business economics at the University of the Witwatersrand, Johannesburg, South Africa.

The Independent Review, v.II, n.2, Fall 1997, ISSN 1086-1653, Copyright © 1997, pp. 225–242.

to bargain with one another to capture the gains from trade. The property rights will ultimately be held by the party who can make the most profitable use of them. Neoclassical economic explanations are all we need, as Douglass North expresses it, "because the competitive structure of efficient markets leads the parties to arrive costlessly at the solution that maximizes aggregate income regardless of the initial institutional arrangements" (1990, 15).

Of course, transaction costs are usually positive, because information is costly. Goods and services have attributes that often are not immediately obvious. Buying a used car is a familiar example. Finding out about these attributes requires an investment in searching for information. Then comes the problem of enforcement, for "without institutional constraints, self-interested behavior will foreclose complex exchange, because of the uncertainty that the other party will find it in his or her interest to live up to the agreement" (North 1990, 33). Measurement and enforcement together determine the costs of transacting.

When it is costly to transact, institutions come into their own. Institutions are "the humanly devised constraints that structure political, economic and social interaction." (North 1991, 97). They consist of both formal constraints such as constitutions, laws, and property rights, and informal constraints such as customs and codes of conduct. According to North, "Institutions provide the incentive structure of an economy; as that structure evolves, it shapes the direction of economic change towards growth, stagnation or decline" (97). Effective institutions create an economic environment that encourages greater productivity.

North has devoted most of his academic career to applying the Coasean analysis to economic history. As he has pointed out,

> economic history is overwhelmingly a story of economies that failed to produce a set of economic rules of the game (with enforcement) that induce sustained growth. The central issue of economic history and of economic development is to account for the evolution of political and economic institutions that create an economic environment that induces increasing productivity. (1991, 98)

North distinguishes three general types of exchange. The type most common in the past has been "personalized exchange involving small-scale production and local trade" (1990, 34). Here the costs of transacting are low because the trading parties engage in repeat dealings among themselves, they are few in number, and they are well informed about one another. By the same token, production costs are high because there is little scope for specialization and division of labor. Personalized exchange entails limited markets and does not lead to sustained growth.

Under the second general pattern of exchange, the prospects of gains from trade improve substantially. This involves impersonal exchange where "the parties are constrained by kinship ties, bonding, exchanging hostages, or merchant codes of conduct" (1990, 34–5). But as production costs decline, transaction costs go up. As exchange extends far beyond the face-to-face dealings of a few parties who know one another well, the problem of cooperation has to be handled in different ways, hence such new institutional devices as merchant codes of conduct and the exchange of hostages. The state may also play a more prominent role, as in early modern Europe, where the protection of merchants brought with it clear prospects of revenue gains for the public guardian. "However," states North, "in this environment the role of the state was at best ambiguous, because the state was as often an increasing source of insecurity and higher transaction costs as it was protector and enforcer of property rights" (1990, 35).

A third form of exchange, impersonal exchange with third-party enforcement, has been crucial for modern economic growth. Here the increasing role of the state was essential to the emergence of advanced economies. As societies became more complex, monitoring based on frequent personal contact within small groups became less common, and the returns rose on "opportunism, cheating and shirking." A coercive third party was essential if growth was to take place. North (1991) asserts that "Historically the growth of economies has occurred within the institutional framework of well developed coercive polities. We do not observe political anarchy in high-income countries. On the other hand the coercive power of the state has been employed throughout history in ways that have been inimicable to economic growth" (14).

Even in the most economically developed countries the state has interfered obtrusively to favor interest groups with relative bargaining strength. Tariff protection, subsidies, and tax exemptions have proliferated in advanced Western countries. When the state is present, redistribution cannot be avoided. But the institutional mix still provided enough incentives for activities that resulted in net productivity gains and thereby created wealthy societies.

The obvious question is: How do such efficient institutions emerge? The answer is not obvious. North has questioned the standard public-choice portrayal of the role of the state as merely responding to the rent-seeking pressures of interest groups and lobbies. As he puts it: "It is no accident that economic models of the polity developed in the public choice literature make the state into something like the Mafia—or, to employ its terminology, a leviathan. The state becomes nothing more than a machine to redistribute wealth and income" (1990, 140). Yet if it is a Leviathan, it is a relatively passive one. It represents the largest concentration of power in society, but is at the same time subject to the pressures of the dominant political and economic groups.

North argues that we must look beyond the struggle for redistribution. The informal constraints such as customs, traditions, and codes of conduct give rise to ideologies: the subjective interpretations by which individuals impose coherence on their perceptions of the social world. Ideology modifies narrow maximizing behavior. Ideology economizes on the information costs and thereby helps individuals deal with the external world. North notes that "It is simply impossible to make sense out of history (or contemporary economies) without recognizing the central role that subjective preferences play in the context of formal institutional constraints that enable us to express our convictions at zero or very little cost. Ideas, organized ideologies, and even religious zealotry play major roles in shaping societies and economies" (1990, 43–44).

An obvious example of the role of informal constraints, to which North often refers, is the different fates of federal constitutions in the United States and Spanish America. Federalism worked in North America, arguably because of patterns of decentralized government and control that already existed in the colonial period. In Spanish America it soon collapsed as the centralist bureaucratic structure and tradition of the colonial centuries asserted themselves. Constitutional forms as such were not decisive. What mattered was that the inhabitants of the United States were already a free people when the Constitution was created in 1787, whereas the peoples of Spanish America had never experienced self-government when colonial rule collapsed early in the nineteenth century. Ultimately, the development of the two regions of the Americas reflected the whole preceding course of English and Spanish history, respectively.

South Africa before the Mineral Revolution

The economic development of South Africa has had a variety of rather special features, reflected in institutions that have attracted wide comment. Writing in 1938, S. H. Frankel observed of the sector of the economy mainly responsible for the country's growth: "The creation of the present European economy in South Africa possibly owes as much to the surplus wealth resulting from the peculiar organization which it has been able to adopt in exploiting its mineral deposits, as to the favourable climatic conditions which distinguish it from the northern territories" (13). And, in a wider context, "African economic development is governed by numerous monopolistic and sectional interests, by particular fiscal policies and by exceptional social techniques and institutions. Diverse politico-economic policies have in the past influenced, and continue to affect, the flow of resources" (15).

Western capitalism arrived in South Africa in a paradoxical form. For a century and a half after 1652, colonization brought about little economic development. Yet the occupying power, the Dutch East India Company, was the largest and most advanced capitalist institution of the time. Having ousted the Portuguese as the dominant power in the Spice Islands, it had proceeded to make huge profits through the single-minded and unsentimental pursuit of material gain, even waging war on its economic rivals in Asia. But the company's decision to occupy the Cape had little to do with any prospects of wealth to be extracted from that region. The company viewed its settlement at the Cape simply as a refreshment station for its ships returning from the East.

Conditions at the Cape did not favor economic development. Apart from the strategic location of the Cape peninsula, contemporaries found little to attract them. Beyond the peninsula itself and the immediately adjacent areas, rainfall was scant. The most promising economic activity appeared to be extensive stock farming. Attempts at movement inland from the Cape peninsula met with formidable obstacles. By 1700, only about 1,200 Europeans inhabited the Cape Colony. The place was a backwater.

The company compounded the economic disadvantages of the Cape by the policies it pursued throughout its period of rule, from 1652 to 1795. Arnold Plant speaks of "the warping effect on development of rigid monopolistic institutions under the Company which prevented the prompt and full adjustment of enterprise and resources to changing conditions" (quoted in Frankel 1938, 42). At first sight this situation presents a paradox: one of the great capitalist institutions of the day pursuing policies seemingly designed to make growth impossible. But the puzzle is only apparent. The company had no interest in the Cape's economic development, which was hardly surprising in view of its reasons for occupying the Cape. Its autocratic rule and its monopolistic policies offered little incentive for permanent settlement by enterprising immigrants from Europe. In fact, the company's reputation as an employer, wherever it ruled, was so bad that it had to recruit its servants largely from the less-prepossessing elements of Dutch and other urban societies. Europeans not employed by the company made the best of the limited opportunities available, most opting for stock farming. Land was the one abundant factor of production. During the eighteenth and early nineteenth centuries, trekboers moved into the dry interior, largely isolated from the limited Cape market, carrying on what was close to a subsistence economy and impervious to official attempts to limit the process of diffusion.

The institutional structure the company chose to impose at the Cape had one logical consequence: the introduction of slavery. Historians do not always see this connection. They tend to regard slavery as, in the words of South Africa's most brilliant historian, developing "by circumstance rather than by necessity" (de Kiewiet 1941, 21). C. W. de Kiewiet's explanation is that "For want of great staples and intensive use of the soil a true slave economy, like that of the sugar islands, could not develop. There were few compelling reasons and no climatic reasons why the Dutch and the Huguenots could not have remained a truly white society."

Afrikaner historians have embroidered on this tale, lamenting that in an avoidable fit of self-indulgence the company decided to base the colonial economy on an enslaved nonwhite labor force. After all, slavery was nothing new in the rest of its colonial empire. But from this decision, the argument goes, there was no turning back. At an early stage the white population of South Africa got hooked on the comforts of having the menial work done by nonwhites, with frightful consequences for the future. Had whites not come to accept the notion that certain kinds of work were incompatible with their self-respect, the whole course of South African history would have been different.

The most that can be said for this argument is that it is dramatically apocalyptic. It has entertainment value, but little more. Even de Kiewiet's restrained formulation does not consider the powerful incentive to introduce slavery that the institutions of company rule provided. The settlement had a labor problem; it could not be solved by the undisciplined and inefficient workers who found themselves, often without their own consent, at the Cape. The indigenous inhabitants of the Cape, the Khoi and the San, were slow to grasp the uplifting nature of wage labor. Nor could they readily be enslaved, for the cost of tracking down runaways would have been immense. For these compelling reasons, the company began to import slaves in 1658.

Slavery at the Cape never played the role it did in the antebellum South of the United States. It was not crucial to what was in any event a fairly stagnant economy, nor was it the foundation of a whole way of life dominated by substantial slaveholders. When company rule ended, slavery was the dominant form of labor only in the fertile southwestern part of the colony. Wine and grain farms in no way resembled Southern plantations. Most of them employed only ten to twenty slaves. Many slaves worked outside agriculture, employed in Cape Town as domestic workers, craftsmen, and laborers. As an institution, slavery in South Africa reached its limits very soon and showed none of the economic dynamism and expansionist thrust that so disturbed American abolitionists before 1860.

Yet in another sense it had remarkable staying power. Summarizing the experience of both the South and the Cape, the American historian George Fredrickson (1981) has written:

> More than any other single factor, it established a presumption

> that whites were naturally masters and members of a privileged group while nonwhites were meant to be their servants and social inferiors. Problems of group definition, arising from race mixture, remained to be worked out or clarified, and more elaborate and self-conscious rationalizations for white dominance emerged in response to the new intellectual trends and political developments of the nineteenth century. But a slaveholding mentality remained the wellspring of white supremacist thought and action long after the institution that originally sustained it had been relegated to the dustbin of history. (93)

Fredrickson probably exaggerates when he talks about "a slave mentality" in South Africa. It would be more appropriate to argue that, for a number of reasons, white supremacist attitudes became deeply rooted among European settlers in South Africa. This view comports with North's emphasis on the informal constraints that condition behavior. They derive from the subjective appraisals of the world that individuals inevitably have to make. If substantial groups share the same perceptions and feel strongly about them, they can serve as a powerful basis for collective action, a means of overcoming the free-rider problem. In South Africa we can readily identify how perceptions filtered through a white supremacist worldview encouraged certain kinds of group cohesion.

The monopolistic ways of the Dutch East India Company did not otherwise crucially shape the economic development of the Cape. Few opportunities for growth existed; the trekboers adapted themselves to the factor proportions by expanding territorially, utilizing the abundant land. Their movement was a natural trend, encouraged by the lack of incentive given them by the company to stay near Cape Town and farm for the local market.

As pastoralists with few links to the market economy of the Cape, the trekboers were hardly subject to the decrees of a government that attempted to control the process of expansion. Their labor relations resembled the white supremacy embodied in the slavery of the southwestern Cape. The structure of Khoi society had disintegrated in the face of European expansion. As the Khoi suffered demographic disaster and displacement from their land, they increasingly entered into the service of the trekboers. The trekboer economy was a semisubsistence way of life, adapted to an environment that appeared invincibly hostile to any form of economic progress.

When the British finally took over the Cape in 1806, they brought with them institutions that laid the foundations for future economic growth. The form of government remained autocratic, but the British were the pioneers of the early industrial revolution. Britain's rulers, post–Adam Smithians, were much less committed to monopolistic trade policies than their Dutch predecessors. They were happy as long as the Cape paid its own way. Controlling the sea lanes to protect the passage to India was their main interest. But the British also maintained order. They introduced reforms that served notice that justice would be administered in a more evenhanded manner. Ordinance 50 of 1828, which permitted colored persons to move freely without passes, has its own special place in the hall of infamy of Afrikaner nationalist historians. The slaves were emancipated in 1834. Civil magistrates and qualified judges were appointed.

On the frontier in the Eastern Cape, British efforts to establish the rule of law were not appreciated. By the 1820s, white frontiersmen and black pastoralists had long been engaged in conflict over the common scarce resource of fertile soil. Attempts to occupy the same lands led to an intensification of all forms of economic contact. As historians have often pointed out, the economic similarities between whites and blacks on the frontier were greater than their differences. But many of the Boers in the Eastern Cape did not like what they saw as the ultraliberal policies of a British administration that gave excessive protection to blacks. The costs of asserting and enforcing their claims to disputed territory rose. The backlash, which took the form of the Great Trek in 1836, was one of the two watersheds of South African history in the nineteenth century.

The flight of the Boers into the interior led to a change in the political structure of South Africa. It also resulted in a major realignment of property rights. Those with superior military power were the winners. Their triumph was reflected in institutions that made possible an economic development both substantial and singularly costly to those with little bargaining strength.

The establishment of state power was a necessary but not a sufficient condition for economic development in South Africa. The Boer republics that arose on the High Veld at first appeared even more economically retrogressive than the Cape under company rule. They were, after all, hardly more than

> a scattered community of farmers who...required very little administrative machinery, and preferred a minimum of government. It was literally true, as they said, that all they asked was to be left to themselves. Co-operation, even with one another, was limited to joint action against any disturber of their peace. (Macmillan 1949, 117)

Before the discovery of diamonds and gold, economic development remained confined largely to the Cape Colony. It took place within an institutional framework of government-maintained order and low taxes. There was economic progress, based on wool exports and arable production for the limited market at the Cape. However, the rate of capital formation was low and depended on the state of agriculture. Investment in roads rose markedly in the 1840s, but the construction of a railway network had to wait for the mineral revolution to make it viable. Even then the colonial government financed it by raising loans in London. The Cape economy seemed to be doing about as well as it could, given the resource constraints under which it operated.

One of the most publicized features of nineteenth-century history was what Frankel (1938) called "the relentless process of appropriating extensive areas of native land" (45). A major cause of the Great Trek had been the prospect of acquiring huge tracts of empty land outside the Cape colony. Yet the trekkers were ill informed: the country they entered was not as empty as they had supposed. The rise of the Zulu kingdom in the east had resulted in substantial depopulation and dispersion of smaller tribes in Natal. In the Transvaal the rise of the Matabele had produced similar effects. After the occupation of these regions by white settlers and the establishment of some semblance of law and order, Africans began to return. Their numbers increased markedly. Virtually from the beginning the settlers found themselves intermingled with blacks who vastly outnumbered them.

The property rights of the returning Africans were poorly specified. The problem arose not just because their previous displacement made it difficult for them to assert original claims to the land. Their system of communal land tenure differed from the private ownership of the whites. Hence, negotiations over the transfer of property from blacks to whites usually came to naught. Chiefs who were supposed to represent their people in such negotiations could not constrain dissidents. In the end, the absence of well-defined property rights meant that peaceful negotiation proved impossible. The superior might of the governments of the Boer republics and the British colonies of Natal and the Cape proved the ultimate arbiter in resolving disputes about the land.

The Cape was the main beneficiary of British colonial rule. By 1910 some progress had been made in assimilating nonwhites to Victorian institutions. In the Boer republics, of course, such considerations did not apply. In the other British colony, Natal, the preponderance of Africans was so huge that the white colonists did not even contemplate the limited political democracy of the Cape Colony. In all the political units of nineteenth-century South Africa, the need to maintain white control meant that decentralized, pluralistic institutions applied, at most, to individuals of European descent.

De Kiewiet (1941) provides a graphic summary:

> Between the native policies of the British colonies and the Dutch republics no very significant distinction can be drawn. In all of them the process which allotted the privilege of land to the Euro-

> peans and the duty of labour to the natives was similar. In the new society which was being created the possession of land was a badge, and dispossession was a stigma. The endowment of the whites and the disendowment of blacks obeyed the social and moral rules to which the ruling group was attached. (75–76)

The different governments of South Africa attempted a judicious blend of policies, which persisted up to the end of apartheid. The one objective was an adequate supply of black labor; the other was the survival of traditional institutions on a territorially separate basis.

Black Farmers and the Market

The process of colonial expansion had greatly extended the market for all products, especially for agricultural and pastoral ones. Africans had been quick to take advantage of the new opportunities. The emergence and later decline of a class of black capitalist farmers in Southern Africa has been one of the favorite themes of radical historians since the late 1970s. One of these writers, Colin Bundy, has documented "The Emergence and Decline of an African Peasantry" (1972) between 1870 and 1913. The growth of a colonial economy was initially accompanied by a highly positive African response to trade opportunities in all four provinces, particularly between 1870 and 1886. Increasingly, however, in the next quarter-century African commercial farming declined. As Bundy sees it, "The decline in productivity and profitability of African agriculture—and the corollary of greater dependence by Africans on wage labour—is in an important sense the outcome of the nature of capitalist development in South Africa" (371).

In particular, Bundy regards the postmineral period as one marked by the preponderant influence of white capitalists and farmers. Mineowners demanded and obtained laws, such as poll taxes, that put pressure on rural Africans to provide them with cheap labor. White farmers, nervous about competition in the marketplace from enterprising black peasants, put pressure on politicians for laws favorable to themselves and damaging to their competitors. Railways linked white agricultural areas to the ports and urban markets. Squatters' laws, culminating in the Natives Land Act of 1913, were designed to prevent Africans in "white" areas from being there in any capacity but that of laborers.

All this may be true, but it hardly follows that prospering African farmers were in some way harmed by inexorable processes of capitalist accumulation. Undoubtedly, influential white interest groups used their political clout to shape the rules of the game in ways that favored themselves at the expense of Africans. But in another sense, the institutional framework did not require the exercise of white political power to place black farmers at a disadvantage. The survival of communal tenure and the consequent blunting of individual incentives to raise incomes from land use were powerful causes of continued African economic backwardness.

The damaging effects of land expropriation were obvious, but we must distinguish between the effects of superior political and military power and the outcomes of an exchange economy. Bundy tends to confuse the one with the other. In fact, the growth of a market economy provided many blacks with scope for material advance, which they made the most of. There is plenty of evidence that Africans responded positively to market opportunities as they gained access to European practical education and agricultural methods. Also, those who suffered the greatest cultural and political disruption through European contact, such as the Mfengu and the Xhosa, responded most positively to the coming of a market economy. More isolated Africans, less subject to the shattering of their traditional ways, did not respond in the same entrepreneurial fashion.

The decline of the African rural sector was hardly avoidable, given the much smaller areas into which blacks were crowded in the course of European expansion. Their system of extensive farming and communal tenure required large unoccupied spaces, no longer available after mid-century. More rapid population growth followed the restoration of peace and the improvement of transportation, which eliminated subsistence crises. Population growth put additional pressure on an already burdened land area.

Minerals and Structural Change

The second great watershed of South African history in the nineteenth century was the discovery of diamonds and gold. The development of the mining sector transformed the South African economy. Until then only leisurely growth appeared feasible, despite the introduction early in the nineteenth century of institutions that favored market forces. Between 1886 and 1914, gold mining dominated the economy, exerting a powerful impact on other sectors and on all regions of the country as market forces broke down the transport barriers that had previously inhibited development.

The South African economy now began to experience structural changes typical of modern economic growth. Increases in real income per capita accompanied shifts of resources from primary production to manufacturing. The capital stock rose in relation to the labor force. The output share of the services sector went up, and manufactured exports increased. These trends typify a developing economy. But South Africa's proved a partial exception to typical structural changes, mainly because of the continued importance of gold mining.

Gold mining has been the leading sector of the South African economy for most of the last century, and its preponderance has imparted to the country's growth certain highly distinctive features. It has made possible a distinct if uneven rise in living standards and, not least, has provided a substantial share of the resources to accommodate the pervasive rent-seeking that has been a hallmark of South African history in the twentieth century. If South African economic development was, to repeat the words of Frankel (1938), "governed by numerous monopolistic and sectional interests, by particular fiscal policies and by exceptional social techniques and institutions," it was facilitated and substantially caused by the dominance of gold.

From Union to Apartheid

The coming of Union in 1910 established for the first time, in North's terms, a single third-party enforcer of impersonal exchange over the whole country. Ideally, the coercive power of the state would have resulted in the effective monitoring of property rights and enforcement of contracts. To a large degree, it did. But of course that has not been the whole story. The increasing role of the state brings with it the prospect of policies inimical to growth and aimed at redistribution instead. Even in the most developed countries the institutional frameworks have been "mixed bags." What is outstanding about the South African mixed bag is that so much of it has consisted of institutional components that have unabashedly promoted ethnic rent seeking by groups with bargaining power within the system.

From the beginning, laws were passed that benefited influential interests. Before Union, mineowners had repeatedly attempted to establish a monopsony for the recruitment of cheap and, incidentally, black labor. However, although after 1900 the gold mines had obtained the right to recruit from outside South Africa, attempts at monopsonization failed, due to familiar collective-action problems. But in 1911 a Native Labor Regulation Act was passed that licensed recruiting agents and prohibited the breaking of labor contracts by the offer of higher wages. The next year the desired monopsony at last arrived in the form of the Native Recruiting Corporation, which duly achieved a reduction in the cost of unskilled labor.

Of course, organized white labor has been, in Mancur Olson's term (1982), the main "distributional coalition" in twentieth-century South Africa. In 1911 the passing of the Mines and Works Act, more accurately known as the Color Bar Act, laid the foundation of white privilege in the mines. It provided that blacks could not legally perform a variety of skilled and semiskilled jobs in the Transvaal and the Orange Free State. White trade unionists, fearful of competition from blacks willing to accept lower wages, were the driving force behind passage of the act. Plainly it did not benefit mineowners, who preferred to hire black workers at market rates and in greater proportions than the law allowed.

From the end of World War I to 1970 the rate of growth of real GDP usually averaged over 5 percent per annum. But the South African economy became the scene of so much government intervention with market forces that its achievement of such rapid growth is something of a mystery. The vested interest groups with the greatest bargaining power at particular times with particular governments benefited from the interventions.

The Nationalist-Labour Pact government that came into power in 1924 looked askance at the capitalists' propensity for employing the cheapest labor regardless of race. It set about making South Africa safe for "civilized labor." Employers received a variety of incentives, when they were not actually instructed, to give jobs at artificially high wages to unskilled "poor whites," refugees to the towns from a backward rural sector, who would not otherwise have been able to compete with still poorer blacks in the marketplace. The "rate for the job" effectively prevented undercutting by members of the wrong race. Formal apprenticeship requirements made competition by blacks for skilled jobs impossible. In return, employers gained protection against foreign competitors and passed on their higher costs to consumers in the form of higher prices.

The backwardness of the agricultural sector also reflected the influence of the institutional environment. In the overpopulated African reserves, communal systems of land tenure and the ban on Africans' acquiring land in "white areas" prevented potential innovators from obtaining and investing in holdings big enough to allow higher productivity. The politically important white farmers received plenty of largesse from sympathetic governments, but insulation from the market brought its own penalties in the form of low productivity and out-of-date methods.

Up to World War II, gold mining provided the means to shelter white farmers, manufacturers, and workers from competitive economic forces. The familiar justification was that gold was a wasting asset. Where would the country be when gold was no longer there to provide an income? Obviously, the self-serving arguments went, resources yielded by mining should be used to stimulate other activities that would still provide jobs and incomes when the golden eggs were no longer being laid. The upshot was the diversion of resources from a mining sector that did not require government assistance to sectors that could not survive without tariffs, subsidies, and other forms of protection against market forces.

Rent seeking will occur in any economy. The best that can be expected is that the incentives embodied in the system of property rights will strongly encourage profit seeking rather than the competitive pursuit of monopoly rents. In this sense the economic rules of the game in South Africa had limited success. The rent seeking often took the form of mobilization of ethnic groups to obtain rents through the political process. As Jennifer Roback has argued, “Ethnic groups have certain advantages as rent-seeking coalitions. They are already organized for cultural and religious purposes and it is often inexpensive for them to become so for political ones. People can not easily change their ethnic identity in order to evade ethnic-based taxation or other costs” (1988, 67).

From Apartheid to the New South Africa

Racism as a form of rent seeking was prevalent before 1948. The arrival in power of the National Party in that year only gave a huge boost to a time-honored South African practice. The new rulers were committed to a far more strenuous enforcement of white supremacy than any of their predecessors. The Nationalist electoral alliance of white workers and white farmers required policies that entailed extensive intervention into the free labor market preferred by capitalists. They managed to achieve their objectives in many ways, most conspicuously in the form of controls over black migration from the black rural areas, known as the Reserves. The controls provided white farmers with relatively cheap labor, and white workers with protection against permanent-seeming Africans in urban areas.

In other forms as well the government ensured the continued support of its special interest groups. Farmers received state subsidies, marketing boards fixed favorable prices for their products, and the taxpayers funded agricultural research on an impressive scale. White workers obtained additional shelter through the reservation of the better jobs for themselves.

Clearly, “the apartheid state” was an interest-group state. As one of the exponents of this interpretation has stated the argument:

> The function of an interest group state is to specify and enforce property rights which maximize the wealth of politically influential groups, even if total societal wealth is diminished in the process. Regulations are enacted by the state if it perceives that the marginal gain to beneficiary groups exceeds the marginal disutility to loser groups. The political equilibrium is therefore determined by the relative effectiveness of competing interests at producing political influence—i.e. controlling free riding. (Lowenberg 1989, 62)

The story of apartheid then becomes a tale of the struggle between competing interest groups. Apartheid becomes transformed because the political influence of some interest groups declines and the influence of others increases. The state passively responds to the rent-seeking behavior of pressure groups; it is simply there to do the best it can for the groups with the most political muscle.

The problem with this approach is its assumption of state passivity.

North has described the rent-seeking literature as

> consistently an interest group modeling of the political process in which ideological constraints on maximizing at certain margins are not part of the argument.... The strength of ideology is the premium individuals are willing to incur not to free ride; in its absence—in a world of universal maximizing by individuals—the costs of contracting would be so great that economic activity would be limited indeed and the stability of institutions impossible. (1984, 37, 39)

But this argument is itself open to an obvious objection. The importance assigned to ideology is too often "a euphemism for ignorance": when something cannot readily be explained, invoke ideology (Rogowski 1988, 314). For a compelling argument, in each particular case the importance of ideology and the role it plays must be demonstrated, not merely asserted.

In South Africa ideology played an important—and specifically orchestrated—role. At first Nationalist power based itself on Afrikaner cohesion. As long as the government was pursuing goals viewed as in the overall interest of its ethnic constituency, above all, the preservation of Afrikaner rule, it had considerable independence in relation to particular interests. Later, especially after the Nationalist split in 1982, when the Afrikaner right wing broke away, the Government began to elaborate a "white" ideology to attract a solid English-speaking following. Here it had substantial success and therefore enjoyed, as before, a broad enough base of support not to be unduly responsive to the pressures of specific groups, as businessmen discovered again and again in the 1980s.

The Nationalist government could simply ignore dominant white interests. In some obvious, tautological sense apartheid ultimately went under because to the ruling whites its costs came to exceed its benefits. But ideology affected the timing of apartheid's demise. By the 1980s the traditional apartheid constituency may have waned, but the new constituency in which business interests could have been expected to be so important had surprisingly little effect on the determination of P. W. Botha's government to hang onto ultimate white control in a variety of unsubtle guises.

Until the 1970s, restrictions on the mobility of black workers grew steadily. Capitalists were the clear losers, so much so that as the costs to them of apartheid rose they became vocal in their criticisms of a system they had previously endured in silence. Increasingly, from the 1970s onward government policies appeared to reflect the growing importance of businessmen in the economy and the declining importance of white labor and agriculture. This was the time of "neo-apartheid," a more sophisticated version of discrimination that accepted black urbanization but still attempted to control and channel it in the interests of white survival and supremacy.

Yet oddly, in many ways the refurbished apartheid of the post-1970 years failed to suit the entrepreneurs of South Africa. The tighter influx control that accompanied the acceptance of the permanence of some blacks in the urban areas was scarcely designed to keep down the labor costs of employers. Strangely, the government appeared unmoved by criticisms from businessmen. After P. W. Botha became head of government in 1978, he attempted a rapprochement with businessmen, but it was one of the shortest honeymoons in history. His resentful and abusive response to their complaints became a feature of South African political life in the 1980s.

What happened in South Africa was more complex than it appears in the conventional explanations in terms of interest-group pressures or the need to appease capitalists. By the early 1970s, white South Africans had got hooked on growth and were not prepared to dispense with its benefits. Appeals by right-wing trade unionists that growth should adapt to the amount of skilled labor that could be supplied by the white population simply did not resonate with a materialistic white electorate. In 1972, in spite of strong right-wing pressures, the government refused to accept a lower growth target than that proposed by the Economic Development Program. Historically, governments have had only limited success with activist economic policies, but their ability to destroy or retard growth has been impressive. The decision by the Nationalists not to heed conservative demands for the appropriate restrictions on black labor laid the foundations of neoapartheid.

Growth policies had to favor businessmen in overt ways. The crux of the matter, however, was that the Nationalists had deliberately exploited ethnic consciousness to build a political power base that allowed them to flout particular interest groups with some ease if they wished to do so. During the 1980s the Government's independence of special interests was underlined by the constitution of 1984, which placed extreme power in the hands of the state president. That this was even possible reflected the Nationalists' success at evading the constraints of pressure groups. Control of the National Party was all that was needed to remain in power; whatever the theory of power sharing, the practice remained adamantly different. It was, of course, business as usual, but within the party power had become more than ever a one-man affair. What Botha did not realize was that he at least needed the National Party, however much it responded to its master's voice. When he resigned the party leadership in February 1989, he discovered that he had abandoned his only power base; the worm, or rather worms, at once began to turn. This event marked the beginning of the end for the "imperial president."

Why then did the government so suddenly and decisively go back on its past in February 1990? It seemed to have become a one-man show: what the man at the top said, went. There is little evidence that strong pressures by politically influential interest groups led to the change of course. F. W. de Klerk simply changed his mind in a hurry. Although he has not yet been effusive about what induced him to think so fast, it seems fairly clear that he had come to recognize what had eluded him only a short time before, namely, that the costs of apartheid exceeded its benefits to the white population. Yet, had de Klerk not taken the initiative, had he continued down the middle road as he had been doing all his political life, it is hardly likely that he would have faced a revolt of rent seekers and interest groups within the broad majority of the white population that had voted for some version of reform in September 1989. De Klerk's initiative confirmed once more the substantial scope for independent action of the top Nationalist leadership, flowing from the National Party's success at Afrikaner and, later, white mobilization. It is a safe bet that Botha would have responded differently. The ethnic ideology the National Party had so assiduously nurtured paradoxically made the transition to majority rule easier.

Of course, the rest of the world also played a role in the development and fall of apartheid. From 1985 on, South African apartheid was perhaps the great moral issue of the world community. The country became the target of global sanctions and a disinvestment campaign that was both sustained and vociferous. Yet it is difficult to assess the world community's effect in ending white rule. Perhaps foreigners helped make the apartheid regime realize its own folly, although, at least under Botha, any such realization was well concealed. The white community undoubtedly felt beleaguered by the rest of the world, but it is not clear to what degree this feeling was conducive to reformist sentiments. Also, there were sanctions-busters aplenty, alert to the lure of profits and indifferent to the wider moral issues.

In short, it appears more plausible to argue that apartheid was undermined from within. As Arthur Lewis has argued, the "most effective destroyer of discrimination is fast economic growth.... The disadvantaged and the subordinate have a vested interest in fast economic growth. Every reduction in the target rate for economic growth is also a reduction in the strength of equalizing forces" (1985, 44, 121). From the mid-1970s on, the South African growth rate declined markedly, but by then the damage had already been done. Black urbanization, and all that flowed from it, had become an irreversible feature of the South African economy.

Conclusion

South Africa's institutional framework was clearly compatible with a substantial degree of growth, especially after the discovery of minerals. But from the beginning of European settlement, political institutions resulted in a specification of the economic rules of the game that imposed huge costs on those without bargaining power. The assignment of property rights was especially inadequate. The property rights of whites, who could vote, were far more secure than those of nonwhites, who could not vote. The institutional framework made possible economic development, which eventually destroyed white supremacy. But its patent defects also made ethnic rent-seeking an obvious means of seeking redistribution in the interests of particular groups. In South Africa the state was too little a "protector and enforcer of property rights" and too much a "source of insecurity and higher transaction costs" (North 1990, 35). It may not have been a carbon copy of the Mafia, but too often it behaved in ways that would have impressed members of that formidable organization.

References

Bundy, Colin. 1972. The Emergence and Decline of a South African Peasantry. African Affairs 71 (October): 369–88.

Coase, Ronald H. 1960. The Problem of Social Cost. Journal of Law and Economics 3 (October): 1–48.

de Kiewiet, C. W. 1941. A History of South Africa, Social and Economic. London: Oxford University Press.

Frankel, S. H. 1938. Capital Investment in Africa. London: Oxford University Press.

Fredrickson, George M. 1981. White Supremacy. New York: Oxford University Press.

Lewis, W. Arthur. 1985. Racial Conflict and Economic Development. Cambridge: Harvard University Press.

Lowenberg, Anton D. 1989. An Economic Theory of Apartheid. Economic Inquiry 27 (1): 57–74.

Macmillan, W. M. 1949. Africa Emergent. London: Penguin.

North, Douglass C. 1984. Three Approaches to the Study of Institutions. In Neoclassical Political Economy, edited by D. C. Colander. Cambridge: Harper & Row, Ballinger.

———. 1990. Institutions, Institutional Change and Economic Performance. Cambridge: Cambridge University Press, 1990.

———. 1991. Institutions. Journal of Economic Perspectives 5 (Winter): 97–112.

Olson, Mancur. 1982. The Rise and Decline of Nations. New Haven: Yale University Press.

Roback, Jennifer. 1988. W. H. Hutt's The Economics of the Colour Bar. Managerial and Decision Economics special issue (Winter): 65–70.

Rogowski, R. 1988. Structure, Growth and Power: Three Rationalist Accounts. In Toward a Political Economy of Development, edited by R. H. Bates. New York: Oxford University Press.