O R TAMBO DEBATE SERIES

Concept Paper for O R Tambo Debate 7

The Economy, Inclusive Growth & Jobs

Lumkile Patriarch Mondi

Wits School of Economic and Business Sciences

22nd September 2016

Introduction

The key economic success measure identified in the National Development Plan is that South Africa achieves average Gross Domestic Product (GDP) growth rate of over five percent, and that by 2030 GDP per capita is more than twice the current level, export growth has accelerated, income levels have risen above the poverty line for all, inequality has been substantially reduced, and unemployment has been reduced from 25% to six percent.

These targets are achievable – many claim they are too modest - if South Africans can put all hands on the deck and get on with the job. The basic ingredients of inclusive economic growth are social and political stability. However, South Africa finds itself at a crossroads reminiscent of the period 1990 – 1994, where socio-political stability is somewhat elusive. The instability during the 1990-1994 period led to a protracted negotiation process on the economy for a democratic South Africa where various scenarios were presented at Mont Fleur.

The Mont Fleur Scenarios

In the Mont Fleur Scenarios 1992 – 2002, the starting point was the negotiation process. If there had been no political settlement, South Africa would have had a non-representative government with unsustainable stagnation, on-going political violence and increased racial polarisation. If there was a negotiated political settlement, South Africa had three options to tackle its challenges. The options were: 'incapacitated government', 'macroeconomic populism' and 'inclusive democracy and growth'. South Africa chose the latter, titled the *Flight of the Flamingos Scenario*.

Just as in the period before 1994, South Africa in 2016 is in an economic crisis. There is perceived lack of confidence in the relationship between the State President and the Minister of Finance. This has been exacerbated by the long-running failure to acknowledge personal benefits accruing to the President as a result of his homestead being rebuilt at taxpayers' expense, the unexpected firing of the former Finance Minister and his replacement by a back-bench MP, the findings of the Constitutional Court that the President had lied under oath, and investors' reactions to these developments as reflected in the volatility of the currency. Moreover, the failure of the Parliament of the Republic of South Africa to sanction the President has diminished trust in the institution to hold the Executive to account in the eyes of citizens. There is also mistrust in the role of security agencies – to the extent that this became an election campaign issue - in light of the continued investigations of the Minister of Finance. There is a view that the security agencies are playing a political role rather than enforcing the rule of law. This is also evident in the 'spy tapes' matter where the National Prosecuting Authority (NPA) is contesting the reinstitution of the charges against President Zuma, and taking the matter to the Court of Appeal in what appears to be an overly attenuated process. More reminiscent of the 1990-1994 period is the growing climate of intolerance and violence, that saw ANC and SACP members being killed execution style in the run-up to and aftermath of the 2016 local election. The state is yet to offer an apology to the widows or commemorate the Marikana Massacre. This and Mr Andries Tatane's death at the hands of security agencies, in the Free State during a service delivery protest, has also brought doubts to the actions of the State and its security agencies.

South Africa is Africa's largest economy and the country is a regional economic powerhouse. Robust growth of the South African economy has proved instrumental in improving conditions in the Sub-Saharan Africa (SSA) region as a whole. South Africa's economic achievements spread well beyond its borders to the rest of Sub-Saharan Africa. South Africa accounts for nearly one-third of SSA's GDP, and two-thirds of southern Africa's GDP. Studies have shown that a one-percent growth of South Africa's GDP is associated with a 0,4%-0,9% growth in the GDP of the rest of sub-Saharan Africa, independent of common shocks.

The current macroeconomic environment is challenging. South Africa's Reserve Bank Governor Lesetja Kganyago has forecast zero percent growth for 2016, 1,5% in 2017 and 1,7% in 2018. The sudden rise in GDP growth in the most recent quarter, to 3,3%, was a welcome break in a seemingly unendingly negative forecast. The increase in the GDP growth in the second quarter of 2016 was accompanied by a 0,1 of a percentage
point decline in the unemployment rate to 26,6% quarter-on-quarter. This resulted in a decline in the labour force participation rate by 0,8 of a percentage point to 57,9%. The labour absorption rate also declined by a further 0,5 of a percentage point to 42,5% due to a decrease in employment.

The Manpower South Africa's tenth annual Talent Shortage Survey 2015 indicates that about 31% of employers surveyed cited difficulty in filling job vacancies. This has worsened when compared to eight percent of employers surveyed in 2014 citing difficulty in filling job vacancies. The most difficult positions to fill were cited as "skilled trades, engineers, management/executive staff, accounting and finance staff, sales representatives, secretaries, personnel assistants, receptionists, administrative assistants and office support, drivers, technicians, teachers and IT personnel. The Survey also indicates that 57% of employers specifically attributed the failure of filling job vacancies to the deficiency of hard skills or technical competencies. (Mail & Guardian - SA's skills deficit has a negative effect on employment).

The National Treasury is in a fiscal consolidation mode focusing on keeping the debt to GDP ratio at 46%. This spells disaster for the country, particularly the unemployed. The rate of joblessness is expected to rise from its current level of nearly 26,6% due to rising input costs, lack of demand domestically and externally as well lack of competitiveness. This all raises the question about South Africa's readiness to meet the 2030 Agenda for Sustainable Development, including its 17 SDGs, and Agenda 2063, **(Link to SDG report, ORT 6)**. There is also doubt by rating agencies that South Africa can address its economic challenges of poverty, unemployment and inequality. Why are we in this position?

What are the main common drivers?

We are part of BRICS – Brazil, Russia, India and China. We share a lot of unfortunate features with many including high levels of corruption and inequality that are holding back economic development potential. Recently, the former President of Brazil Dilma Rosseff was impeached and removed from office for understating the country's level of indebtedness. The agendas of strong and corrupt ruling parties are distracting some BRICS countries from uplifting their people. This is true of the workers' party in Brazil, the African National Congress-led (ANC) government in South Africa, the Communist Party of China and the United Russia Party in the Kremlin. (SowetanLive - How ANC's path to corruption was set in South Africa's 1994 transition). The economic fortunes of these countries are significantly influenced by the parties ruling them.

South Africa is historically associated with fighting injustice and defending the oppressed. This enhanced the country's status and earned it the right to play a constructive role on the international stage. This goodwill in turn benefited its development path in the form of accessing international capital and positioning the country as an investment destination.

It was noted above that inclusive economic growth requires social and political stability. The South African economy has undergone substantial transformation since the advent of democracy. It recorded an average rate of economic growth of 3,3% per annum in real terms over the period 1994 to 2012, a remarkable improvement on the 1,4% average annual growth registered during the period 1980 to 1993. However, the pace of growth fell somewhat short of the 3,6% average recorded by the world economy, even in the midst of a global commodities boom. South Africa's gross domestic product (GDP) by 2012 was 77% larger in real terms about 1994, with the corresponding increase in the global economy having been 90%. On a per capita basis, the country's real GDP was 31% higher by the end of the period.

The South African economy recorded its fastest growth rates since the 1960s over the period 2004 to 2007, with real GDP growth averaging 5,2% per annum. From a global perspective, this period was characterised by a strong bull-market and booming commodities markets. With social and political stability, South Africa stood high in the African Union, the Group of 20 and other multilateral institutions. Of course, there were blemishes and errors. In the period that led to the recalling of former President Thabo Mbeki and the processes outlined above which has seen political and corruption scandals, accompanied by a shift in economic policy from ASGISA into the New Growth Path and adoption of state-led economic development, the ruling party unwittingly cemented a foundation for political and social instability.

The global economic environment has changed since 2008, reversing most of the gains made before the global recession; South Africa was no exception. But exaggerated expectations by the new political elite that BRICS offered better economic opportunities due to China's re-emergence has proved short-sighted. South Africa identified itself with controversy by fully aligning itself with China and Russia. South Africa lost the status of a country with an exemplary constitutional democracy and moral authority by failing to support the withdrawal of China from Tibet and Russia from the Ukraine.

In the continent, South Africa is friends with countries such as Angola that have a dismal human rights and governance record (Africa News & Analysis - Angola, activist calls for dos Santos daughter to step down from Sonangol). They are ruled by corrupt oligarchs where families of "big man" leaders accumulate untold wealth while the majority of citizens live in poverty. Given the friends we have chosen, we are going to have few allies to support our economic development and our fight against poverty and inequality. South Africa has taken sides with those countries to the detriment of its moral position in global affairs (RDM - Greatest disappointment of SA's foreign policy). Countries such as China, the UK and the US put their economic interests first. But South Africa has taken politically opportunistic positions rather than exclusively economic ones in search of a solution for a fast-growing and dynamic economic, with little to show for it.

What company should we be keeping? What are the better performers doing that we are not?

South Africa has been an upper middle-income country for a while. With appropriate policies and the required drive, the country should be in the company of countries like South Korea, Mexico and Malaysia. They developed largely because they moved up the global manufacturing value chain. Some scholars have argued that South Africa is stuck in the upper middle-income trap because it has been unable to move out of low-level manufacturing.

The manufacturing sector registered strong growth during the period 2004 to 2007, supported by robust export demand for some of its products and solid growth in domestic demand, although the performance of individual manufacturing sub-sectors varied widely. The manufacturing sector has been adversely impacted by the global economic downturn, particularly weakened demand in traditional markets such as Europe, as well as difficult trading conditions domestically. The sector is facing fierce competition in both domestic and world markets, while having to deal with substantial cost pressures and other competitiveness challenges such as electricity supply, currency volatility, skills constraints, productivity levels, and among other pressures.

To escape, it needs to change its industrial character. It must move into fabrication and high value added manufacturing and design. South Africa needs to move beyond offering assembly capability and towards products that are conceived, developed and manufactured in the country. To get there, a concerted effort and calculated investment in education and the sciences is critical. South Africa should put money into research and development to become an innovative economy. It has the framework. Education is key to all countries that have moved up the manufacturing value chain. If South Africa bungles its higher education, as it has done at the primary and secondary levels, it is doomed to fail. The signs are not good.

The other obstacle to growing the economy to meet the NDP targets is monopolistic domination in critical sectors like power, telecommunications and transport. These are key because they enable other businesses to flourish. But, they are held ransom by moribund state-owned enterprises such as Transnet and the power utility, Eskom. And, protracted sideshow battles over governance and leadership in these SOEs suggest a profound lack of urgency with regard to the goals of 2030. As a result, South Africa has become a high-cost economy and the NDP is compromised.

What can be done?

As argued earlier, South Africa is in a crisis comparable to the period before 1994. From the heights of average GDP growth in the period between 2004 and 2007 of 5,1%, South Africa now faces zero percent economic growth, albeit in a global environment of low GDP growth. The challenge is that many of the current challenges are homebrewed. The nine-point plan agreed with business, labour and government is a step in the right direction. However, policy choices have made the achievement of the NDP growth rates compromised but still achievable - if South Africa's leadership does the following.

1. The ruling ANC and the Executive must accept that the country is an economic crisis that is exacerbated by their own actions (and inactions) (Business Day Live - I would have asked Jacob Zuma to resign).

2. The Presidency and incumbent should provide the moral high ground South Africa needs locally and globally.
3. The party should address the concerns of the electorate, which is concerned by the current state of the economy, economic governance and the rule of law.

The ANC can no longer claim to have full ethical and moral control of the country unless it calls an early election, from which it gets a mandate to govern again. A political settlement, therefore, is a prerequisite for South Africa if it wants to restart robust, sustainable growth. Such a political settlement would have to be underpinned by strengthening NEDLAC where the economic agreement to 2030 will be cemented. This agreement will be underpinned by the following, some of which emanated from the *Flight of the Flamingos* scenario:

- A political settlement within the ANC that put the country and the people first.
- Constitutionalism, human rights and the rule of law.
- Human capability, competence and intolerance of corruption and racism.
- Sensitivity to Macroeconomic stability and fiscal discipline.
- Export-led Model.
- Business confidence due to certainty and consistency of policy.
- Increase investment and therefore employment growth.
- Growth and inclusive democracy for solidarity with the poor where their incomes grow by nine percent per annum while the wealthy grow by three percent.

The combination of a political settlement and broader agreement at NEDLAC will then help attain an average growth rate of five percent by 2030 as the NDP envisions. They are not sufficient conditions on their own, but they are necessary conditions.

Moreover, all the work of various stakeholders including government with the rating agencies dealing with sovereign risks seek to assess the capacity and willingness of a the government to service its debt within maturity dates. In accordance with the conditions agreed upon with creditors at the time the loans were contracted, these safeguards are being threatened by the actions of the Hawks and continuing political tensions within the ruling ANC. There is a self-evident need to de-politicise all security agencies and take party factionalism off the governance stage.

Each agency has its own rating taxonomy, generally on a scale of A, B, C and D. On the scale used by Standard & Poor's and Fitch Ratings, the top rating is "AAA" and the bottom "D", while with Moody's Investors Service the top is "Aaa" and the worst is "C". A lower rating reflects a higher probability of default and vice versa. Governments rated above "BBB-" or "Baa3" are known as "investment grade", while those below BBB- / Baa3, fall into the "speculative grade" category. International investors make use of credit ratings as one basis for selecting between investment options.

Since 1994, South Africa's credit ratings have steadily improved, reflecting progress in macroeconomic reform and economic conditions. South Africa was assigned an investment grade rating of Baa3 by Moody's Investors Service in 1994, while Fitch Ratings and Standard & Poor's assigned a speculative rating of BB. Sovereign ratings measure the risk of a country defaulting on its foreign currency debt service obligations. Relevant factors in determining a rating include the ability of the economy to generate foreign currency, the magnitude of short-term debt, total debt stock, and the level of international reserves as well as the ratio of external debt to current account receipts. Reduced debt service costs enabled Government to channel significantly more resources to expenditure on public services. This is at risk should South Africa be downgraded in the next few months.

As a start, the recent GDP data indicating that South Africa grew by 3,3% in the second quarter is encouraging. It highlights that when we work together, particularly since 9/12 we can attain some of the NDP goals. However, it is too early to celebrate that growth has now stabilised since there was an improvement in commodity prices in the second quarter, which led to steel prices also increasing due to low inventory levels. More collective action by business, government and labour is needed to restore confidence for a better life for all.

Perhaps the following questions are of relevance:

1. What is the status / progress since 1994, with respect to building an inclusive economy, creating jobs, and addressing inequality and poverty?
2. How are we currently positioned to meet the NDP's 2030 vision, in achieving the same?
3. What are the challenges that government and we as a country are facing presently that is hindering progress?
4. What is government's plan to ensure that we do meet the goals of the NDP?
5. The role of business, labour, civil society and academia in this plan?

References

Mondi Lumkile. (2016) South Africa can expect zero growth. Its problems are largely homemade. *The Conversation*, 25 July 2016.

National Development Plan 2030. (2013). Our Future – Make it Work, National Planning Commission, The Presidency, Pretoria.

#TamboDebates