# Abstract

# Introduction

In discussion paper “Policies to promote growth and employment in South Africa. Informal Discussion Papers on aspects of the Economy of South Africa” – J Lewis – 2001, discusses various aspects of South African economy for the period just after end of apartheid in 1994 to 2001, as well as strengths and challenges that lies ahead. We draw queues about the economy from the paper and discuss the key points this paper highlights.

## Current macro-economic background

South Africa is a middle-income emerging market with a abundant supply of natural resources; well-developed financial markets and institutions, legal, communications, energy and transport sectors. 2017 est. real GDP growth rate stood at 0.7%. In PPP terms 2017 GDP stands at $757.3 billion while $344.1 billion. Looking at demand side variables, the household consumption, key contributor, comprised ~60% of GDP, followed by govt. consumption and long-term investment 20.5% each whereas net trade balance -1%. Looking at supply side variables, services contributed ~67% followed by industrials ~30% whereas, agriculture contributed 3%. Inflation for the same period stood at 5.4%. prevailing prime rate is 5.75% (12/31/2014 onwards). Despite the fact that ~50% of its population is rural population, disproportionately low contribution of agriculture sector indicates stark income/ resource disparity. Despite high literacy rates it has very high unemployment rate (>25% of workforce). With revenues of ~$92 billion and expenditure of ~$103 billion, its budget deficit stood at ~3.2%, a considerable improvement over around previous decade ago. Mining is the major industry in South Africa (largest producer of Platinum, gold and chromium), automobile assembly, metalworking, machinery, textiles, iron and steel, chemicals, fertilizers, foodstuffs, commercial ship repair etc. 2017 etc. industrial production growth was ~0.5%. It has a well-diversified base of trading partners. Although structural deficiencies exists (high unemployment and income disparity), its monetary and fiscal health is at relatively sound. Ever since the end of apartheid 25 years ago, one of its key mandate of wider economic inclusion is yet a distant achievement. High crime rate, lack of social infrastructure, training and absorbing vast pool of unskilled labor, still remains a challenge. Through this paper, we attempt to paint a comprehensive landscape of South African socio-economic condition.

## Economic history

Earliest records of European settlements in South Africa date back to 1652, when the current day territory near Cap Town was established as a refreshment center for passing-bye ships on Europe-Asia trade route. The relations between various groups were relatively at ease. Diamond and gold discovery brought international attention and influx of foreign people and investments to its shores. The later part of the 19th century could for South Africa be characterized by gold-rush, wars, parastatals and general struggle among all groups of the society. The great depression of 1930s slowed down its mineral dependent economy. Soon enough all the sections of the society were affected by depression, including Europeans. This was in 1932, a period before black civil rights movement in the US. Amongst the measures recommended by Carnegie Corporation under The Commission on the Poor White Problem in South Africa, was segregation of various sections of the society for independent growth of every society. Post World War, with Labor-Afrikaner Nationalist Party in power, formalized this system of segregation under ‘apartheid’, lasting until early 1990s. This time again, the reason for change was mounting international sanctions couple with freezing investments in and out of the country. Thus, under president Frederik Williem, formal negotiations for transition began in 1990.

## Legacy of Apartheid based economy

In 1994, unlike other sub-Sahara African economies, South Africa was on of the wealthiest. With population of 42 million, its nominal GDP stood at USD 127 billion or USD ~3,024 per capita, making it one of the four middle-income income in Africa. It had sound market economy and financial sector, most industrially advanced economy in Africa.

However, decades of apartheid regime created stark inequalities amongst its majority African populations. As a result, Most of the capital was controlled by the minority Europeans, all the skilled employment was reserved for the Europeans, whereas, there was little (neither upwards nor lateral) mobility opportunities for black labor class population. This distortion was pervasive in every section of the economy as if there were two economies in one. Besides, South Africa has been highly urbanized; although nearly half the population is rural, agriculture comprises barely 5-6% of the GDP (and 9% of employment). Despite the disparity, agricultural and informal sectors have not grown much in the economy.

# A brief description of economic reforms

The mandate of democratically elected ANC govt. in 1994, was promoting economic inclusion and redistribution of resources (the later being the priority stipulated by the South African communists that supported Mandela to power). Unique characteristic about South African economy in 1994 was that unlike other sub-Sahara African or Asian economies that began from scratch, South Africa inherited the legacy of highly developed aspects of an economy *viz*., the market structure and policies, government institutions and authorities, financial institutions and capital markets, industry, infrastructure etc. were highly developed. The challenge was more so to achieve economic.

## Reconstruction and Development Program (RDP)

RDP was a comprehensive plan that was to be implemented to achieve economic inclusion. It laid out scope and an actionable plan to achieve this stated objective. It aimed at providing social infrastructure, developing human resources along with adopting socialistic goals of democratizing state and society.

Despite the far reaching populous goals laid out by the policy, implementing the program was another challenge. Its implementation required a fine balancing act between growing demands of public and simultaneously striving to reassure domestic and foreign investors and donors. Secondly, the inherent structural deficiency added to its upheaval. Since it was implemented through a separate ministry, what was whose duty and responsibility and who would be accountable and to whom, those lines were muddled. Besides, fiscal and monetary prudence was the need of time. GDP had slipped while inflation soared; fiscal deficit reached 10%. Besides it was obliged to carry out WTO-linked program for long-term trade liberalization and reunification of dual exchange rate system followed by progressively lifting exchange rate controls, which led to instability in Rand. All of the above discussed called building consensus among various stakeholders and committing to sound macroeconomic policies.

## Growth, Employment and Redistribution framework (GEAR)

In 1996, RDP was replaced by GEAR. The primary goal was to restore confidence in South African economy.

The following are the salient features of the GEAR framework:

1. Focus on fiscal deficit reduction.

2. Focus on budget reforms to strengthen redistributive thrust of expenditure.

3. Reduction in tariffs to contain input prices and facilitate industrial restructuring, compensating partly for exchange rate depreciation.

4. A commitment to moderate wage demands.

5. Exchange rate policy to keep the real effective rate stable at a competitive level.

6. A prudent monetary policy to curb rising inflation.

7. Continue global relaxation of exchange controls

8. Speeding up restructuring of state-owned assets

9. Tax incentive to stimulate new investment in labor absorbing industries/ projects.

10. Expansionary infrastructure program to make up for the backlog of social infrastructure.

# Review and critical analysis of the policy impact

## Effects of the program

Lewis, J., 2001. Argue that the policy achieved mixed results on following grounds:

1. In trade policy reforms, although the non-tariff barriers have been removed, the tariff structure is still discouraging. Further, an environment of anti-export bias for many commodities prevails coupled with lack of tariff rebate system prevents exporting firms to obtain inputs at world prices.
2. The labor market reform front, various discriminatory policy have been addressed, providing fair protection of workers’ rights and improving benefits and condition of employments. However, not enough have been done to create demand for jobs. Moreover, the majority of the South African work force that is unskilled, still has a very high unemployment rate.
3. Sectorial deregulation have preceded slowly, disappointing potential international investors and sending mixed signals regarding govt.’s commitment.
4. Capital flow imbalances. South African investment abroad have increased during the said period, but capital inflows haven’t grown much.
5. Challenged exchange rate stability; both due to international as well as domestic factors. Integration with global economy meant dealing with unexpected international ‘shocks’, particularly experienced during Asian Crisis. On the other hand, defensive interventions to support the rand during this period generated a net position in foreign exchange market that was 5× of its reserves. Although it reduced subsequently, it still remains a concern.

As a result of the above discussed factors, the economy failed to achieve its target 6% growth and create 400K jobs annually.

## Analysis of the capital, investments and financial markets

It is important to note that in emerging economies primary limits on sustainable long-term growth derive from supply side factors rather than demand-side factors. Therefore it is important to understand factor growth drivers, *viz*., land, capital and labor.

## Land

As part of RDP mandate, the new govt. adopted an ambitions land reform in 1994 that was designed to redress the apartheid legacy, foster national reconciliation, promote economic growth and reduce poverty. It is proposed of a). restitution to provide case or in-kind compensation to those removed from their lands after 1913; b). and tenure reform to improve tenure security by recognizing individual and communal ownership rights and creating an administrative infrastructure to improve access to previously disadvantaged group; and c). redistribution, to provide land to rural blacks through a market-assisted process that provides one-time grants to means-tested eligible participants and assistance in completing the process[[1]](#footnote-1).

As of 2018, perhaps the most alarming indicator for any investor, domestic or international, is the call for ‘land expropriation with compensation’, by the Marxist elements within the parliament. Dishonoring property rights will have detrimental effect on economy’s capital formation. If events in Venezuela and Zimbabwe offer any lesson for the country’s leaders.

## Capital

In a closed economy without foreign investment, investments equal domestic savings. And with integrated economy, domestic savings provide a cushion to absorb monetary shocks. On the other hand, lack of savings exposes domestic economy to external vulnerability. Domestic savings in South Africa are low by international standards; both Lewis, J., 2001 and J.W. Prinsloo, 2000 confer with.

Also, if the govt. and corporations saves more, private investors tend to save less (Ricardian evidence). Recent improvement reduction in govt. dissaving has been associated with lower private savings.

## Labor

The labor movement is quite inflexible and there is ‘insider-outsider’ dynamics in play. Most skilled jobs lie with the ‘insiders’, especially with the employers. The ‘outsiders’ mainly include unemployed and discouraged workers. Within the industrial labor relations system, trade unions have an upper-hand. As a result, wages and productivity don’t necessarily go hand-in-hand. Lewis, J., 2001 further argue the high growth in wages of unskilled (250%) and semi-skilled labor but not so in skilled (110%) and high-skilled labor (-10%) while almost no change in productivity factors implies vulnerability of unskilled and semi-skilled labor in the market. These have contributed to suppressed growth in employment in the economy.

# Recommendations

## Encouraging entrepreneurship

Thrust to SMMEs. These types of businesses exists largely outside formal economy and are often the largest employers in an economy. They have potential to play major role in growth, competitiveness and employment growth. SMEs tend to be more labor intensive , and can often meet demands of international competition more flexibly. Support eco-system that would encourage growth of SMMEs should be developed. Ready availability of finance and lower rate should be facilitated.

## Labor front

### Improving labor market flexibility

As mentioned above, the ‘insider-outsider’ dynamics should be done away with and performance based incentives should be encouraged.

### Skilling the manpower

As higher skills result in higher productivity per labor.

### Subsidizing employment creation projects

For instance, many emerging economies incentivizes multi-nationals to set-up labor intensive industries.

## Environment

South Africa is water stressed and by some estimates, the country could face critical water shortages by 2020. Water conservation and demand management holds tremendous potential to help region to meet its water needs. Urban and agricultural use in South Africa is highly inefficient. It is further estimated by making the current irrigation use just 10% more efficient could save 2.5 billion cu. mtrs. each year. If urban water use could be made 10% more efficient could save another 600 million cu. mtrs. per year.

# References

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2. Lewis, J., 2001. Policies to promote growth and employment in South Africa. Informal Discussion Papers on aspects of the Economy of South Africa.
3. Prinsloo, J.W., 2000. The saving behavior of the South African economy. South African Reserve Bank.
4. IRN, EMG, GEM, 2000. The Potential for Water Conservation in Southern Africa

1. Source: J Lewis - 2001 [↑](#footnote-ref-1)