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Time consistency and economic growth: a case study of South African macroeconomic policy

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**Abstract**

The numerous diagnostic studies and policy recommendations that exist for South Africa typically focus on microeconomic constraints to growth. Higher potential growth certainly requires structural reforms to boost productivity growth, in particular to allow private competition and investment in network sectors. But these reforms and others will also be more effective if macroeconomic policy facilitates the relative price adjustments and consequential factor allocations needed to achieve higher productivity. Sustained and large fiscal deficits, higher debt, and relatively high inflation all impede those price and factor adjustments. Looking back to the global financial crisis, different policy settings in fiscal, monetary and macroprudential policies, backed by structural reforms, could have supported higher growth outcomes and provided the fiscal space to respond to the current COVID-19 crisis more effectively.

**JEL classification**: E62, E63

**Keywords:** fiscal policy, policy mix, monetary policy, South Africa

# Introduction[[4]](#footnote-4)

In 2013, we published an article that identified some of the major obstacles to growth in South Africa, provided policy recommendations, and modelled their impact.[[5]](#footnote-5) Since then, South Africa’s structural impediments to growth have become even more binding and macroeconomic imbalances ever more challenging as economic performance has deteriorated.

## Heading

The economy’s growth rate decelerated steadily from 2011 to 2019. Unemployment has reached post-apartheid highs and educational outcomes remain poor. Manufacturing output continues to languish and export volumes have been largely unchanged over the last 10 years.[[6]](#footnote-6) Government debt reached 63% of gross domestic product (GDP) in 2019, before much larger deficits caused by the pandemic response, and may increase to more than 100% within five years. The few positive developments include a decline in inflation, helped by more effective monetary policy and also lower inflation globally, and a relatively high terms of trade giving lift to the commodity export sector.

### Heading

The COVID-19 pandemic and lockdown response has deepened the economic malaise, inflicting major supply and demand shocks to the domestic economy. Fiscal resources must be found and applied effectively to mitigate the health and economic costs of the pandemic, but in a time-consistent way: near-term fiscal and monetary policies need to remain consistent with longer term macroeconomic stability and the need to raise potential growth. In our view, short-term needs are critical, but so too is the long-term.

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4. We are grateful to David Fowkes and an anonymous referee for their comments and suggestions. [↑](#footnote-ref-4)
5. See Faulkner, Loewald and Makrelov (2013). [↑](#footnote-ref-5)
6. Economic growth slowed from 3.3% in 2011 to 0.2% in 2019 and unemployment increased from 24.8% to 28.7%. Manufacturing output in 2019 was only 3.6% higher than in 2007. [↑](#footnote-ref-6)