The Economy

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The Zuma administration harmed economic growth in several ways. There was zero interest in the patient promotion of growth. Instead, elite enrichment by any means possible was the central focus. To the latter end, institutions essential to growth were hollowed out and partly repurposed for private accumulation. Revelations of outrageous corruption failed to lead to investigation and punishment. The quality of management and accountability in the state and state owned entities declined. Fiscal space was used up rapidly and the public debt to GDP ratio soared. Vague symbolic appeals to 'radical economic transformation' were used to divert attention from the increasing mess, increasing uncertainty.

The replacement of Zuma has brought a change in tone, but it remains to be seen how far attention to economic growth can be sustained in the medium term, given competing demands for attention in the form of political firefighting and the 2019 election. Still, if achieving economic growth requires persistence, so does the advocacy of measures to promote it. Accordingly, *FOCUS* publishes four articles on growth by leading economists in this edition.

The central point is that South Africa is stuck in developmental terms. **Johannes Fedderke** argues that potential economic growth (the speed limit for the economy in the medium term has dropped to below 2% since 2010. The International Monetary Fund concurs. Its April 2018 projection implies a potential growth rate of 1.8% in the early 2020s. Given a population growth rate of 1.1% in the same period, the tiny growth in real per capita incomes, if maintained, imply that it would take a century for living standards to double.

Fedderke shows that poor growth performance has long been a feature of the South African economy, arguing that unbalanced growth, product market distortions, a misconception of the relation between inequality and growth, and political economy constraints are responsible. Unbalanced growth under South African circumstances is concentrating labour absorption in low productivity sectors, making policy that drives up the real price of labour likely to be particularly counterproductive. Instead, supply side measures are needed, with particular attention to international competitiveness and access to world markets needed to increase competition in the South African economy. High levels of concentration in output markets lead to high mark-ups, lower productivity growth and they reinforce labour market inflexibility.

While there are endless studies on inequality, there is virtually no analysis of the relationship between inequality and economic growth. Fedderke finds that growth and inequality determine each other in a benevolent way. In particular, the impact of growth on labour absorption, and hence inequality is strong. He also finds that there has been erosion in the quality of governance, dampening economic growth.

The first duty of macroeconomic policy is not to impede growth. The second is to increase competitiveness, investment and efficiency. **Christopher Loewald** argues

that fiscal deficits, while appropriate in the immediate aftermath of the global financial crisis, should have been reduced from 2011 as the output gap disappeared. In the event, rapid growth of the public sector wage bill and rising debt service costs have crowded out public investment spending. By keeping inflation and interest rates higher than they should have been, fiscal policy appreciated the exchange rate and weakened the response of exports to recovering global growth. It has also undermined desirable adjustments in relative prices. Real depreciation of the exchange rate and lower domestic demand would have shifted production to tradable goods and services and domestic expenditure switching to non-tradables, reducing the current account deficit.

Accordingly, Loewald argues for macroeconomic policy settings which lower external imbalances and creates a more sustainable pattern of domestic production, with decrease dependence on debt and consumption. Moreover, the credibility of monetary and fiscal policy should be enhanced, with an emphasis on keeping the inflation rate in the middle of the target band instead of near the top, and a more rules-based fiscal policy designed to make the current commitment to counter-cyclicality, debt sustainability and inter-generational equity. Finally, macroeconomic policy should be more closely related to growth-enhancing microeconomic measures.

Instead, they advocate policies which emphasise openness, increase in new entrants, and orientation to future generations, moving resources to accumulation of skills, technological upgrading and shifting consumption to the future.

Vincent Dadam and Nicola Viegi consider the determinants of investment. Private investment has been weak for a long time, and is now about 20% lower than before the global financial crisis. Strong structural factors are at work, and they require a strong policy response to increase foreign direct investment and investment by South Africans in home markets. The most important determinant of investment is the expected size of the market. Given South Africa's remoteness, expanding markets require integration into the global economy, which also exerts competitive pressure on firms to innovate and become more efficient. Barriers to entry into domestic production create a disconnection between wages and productivity via the extraction of rent, creating the pressures for more protection and subsidy. South Africa has seen a widening of the productivity gap between best practice and actual production, sustained by inward looking policies.

At the policy level then, Dadam and Viegi see little hope that structural changes promoting investment will be the outcome of corporatism, which favours incumbents and rent sharing over greater competition. Instead, they advocate policies which emphasise openness, increase in new entrants, and orientation to future generations, moving resources to accumulation of skills, technological upgrading and shifting consumption to the future.

Like Loewald, **Andrew Donaldson** lays stress on the details of tax, spending and financial support programmes, the interactions between government actions and market dynamics, and the way in which public policy affects investment, trade and employment. Donaldson discusses three focus areas: urban development and housing, earnings, employment and social security, and network industries and state-owned companies. Noting that higher productivity in cities means that urbanisation is a powerful catalyst of growth, Donaldson argues that (i) greater priority needs to go to economic investment, trade, skills and enterprise development, (ii) the structure of local government finance and financial support from central government will have to change, in the direction of a blend of grant and loan based funding with private sector and Development Bank involvement, and (iii) revenue management should improve, with new settlements confined to planned and rateable areas.

Donaldson also argues for a more extensive employment subsidy than the youth employment incentive and for a more complete programme of social security and health insurance in order to increase household income security, contributing to sustaining productivity and competitiveness in more labour intensive industry. He also notes that technology and competitive adaptation have shifted against slow moving incumbents in network industries. Restructuring proposals have sought to bring better regulation and competition into the electricity, transport, water and telecommunications industries, but the complexities of transition and political resistance to privatisation has worked against progress,

In the end, proposals for pushing ahead with economic development are to be found in many places, including the National Development Plan. The problem lies with indifference to them, or active hostility, dressed up as resistance to 'neoliberalism'. What used to be known as 'cribbing' in examinations is now known to education theorists as 'rapid learning technique'. By the same token, corruption is rapid accumulation technique, and it will always be preferred to patient growth, unless it is stamped out.

As a nation, we are effectively more in love with the status quo than we care to admit, preferring to wait for a great wind to pick us up and take us to a desirable place to getting there under out own steam: to see, and work with, opportunities for improved growth requires a change in mentality with an accompanying realignment of interests. Think like economists, and get serious.