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The IRR's Blueprint for Growth 7:

"Open(ing) for business": South Africa's investment malaise and how to escape it

November 2024

Terence Corrigan

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"The common message we are taking to the annual meeting is that South Africa remains open for business and is committed to creating a conducive environment."[1] So said Finance Minister Enoch Godongwana as a government delegation was departing to the World Economic Forum in Davos in early 2024. The country being "open for business" is a well-worn cliché meant to announce South Africa as an attractive commercial destination. Its reiteration over the years, however, implicitly concedes that a perception exists to the contrary – that South Africa is in some way not open to business.

Doing business, of course, covers a wide array of activities, which may be divided into two broad categories: trade and investment. Trade is the buying, selling and bartering of goods and services. In a sense, this is the easy and accessible part of the business world, and one in which all people in a given society will tend to be involved. Investment, by contrast, involves the creation of those goods and services, or more precisely, creating the capacity for their production.

Investment is the key driver of economic dynamism. It signifies the commitment of wealth to activities in the expectation that this will yield benefits over some period of time. In brief, it is the commitment of wealth to an activity that will produce more wealth in the future. This is the concept of "capital", the use of wealth or the assets it procures to generate wealth.

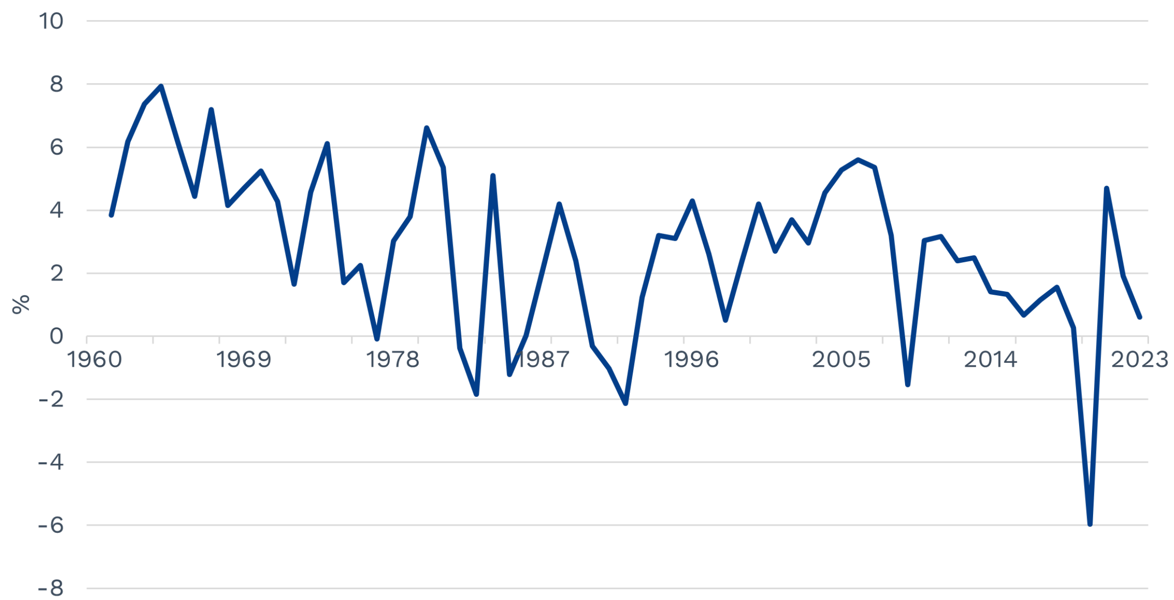
This study examines South Africa's trajectory regarding investment. It should not unduly pre-empt the content that follows to point out that the level of investment that South Africa has been able to attract has been insufficient to drive the economic progress that the country has craved since its democratic transition. The goal of this study is to determine why this has been the case and what could plausibly be done to increase investment in South Africa. It draws on data assembled by the Centre for Risk Analysis, on a series of articles previously published by the author on the IRR's platforms, on a review of publicly available information and analysis, and on a number of interviews with economic analysts and businesspeople. (Note that since many of the interviewees chose to remain anonymous, it was decided to be consistent with all, and identify them with an arbitrary set of initials and a descriptor of their background.)

The South African economy in perspective

Investment is the primary driver of the headline economic indicator, economic growth. Specifically, investment enhances the capacity of a jurisdiction to increase economic activity from one year to another. Invariably, annual Gross Domestic Product (GDP) growth is the reference point for discussing South Africa's economic challenges.

The table below shows trends in real GDP growth performance in South Africa since the 1960s. While the trendline is erratic, they show – broadly – robust performance in the 1960s and through much of the 1970s. In the 1960s, growth fluctuated, though showed a notable weakening towards the end of the decade. The early 1990s saw growth collapse, but pick up after the transition in 1994 and remain relatively strong (the period of the Asian financial crisis excepted) until the global financial crisis hit the country. Over the past 15 years, the growth rate has been indifferent, often failing to breach the 2% mark.

Figure 1: Real GDP growth, 1960-2023



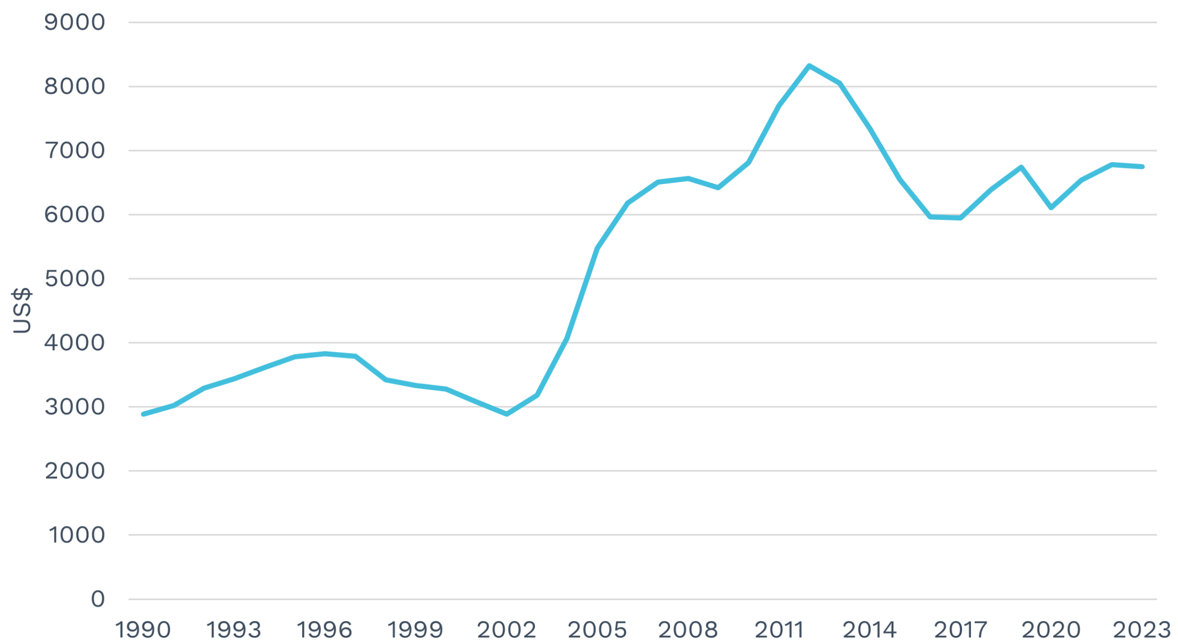
Source: World Bank[2]

As a baseline for analysis, the 2012 National Development Plan (NDP) envisaged real GDP growth of 5.4% per annum over a sustained period.[3] In the post-1994 era, this has been achieved in only two years, and in only one other has it managed growth of above 5%. This helps to frame South Africa's macro-level problem: the economy is not growing at anything like the level required to meet the needs of the population and the state's official ambitions.

To understand the dynamics contributing to this, it is useful to examine South Africa's place in the global economy. In international terms, South Africa has a sizeable but modestly proportioned economy. World Bank data – useful for comparisons across the world – put its GDP at US$377.8 billion in 2023. In these terms, it is 40th in the world, not dissimilar in size from jurisdictions like Hong Kong, Colombia and Nigeria. (The figure for the world economy, by the way, stood at US$105 trillion.)[4]

South Africa is classified by the World Bank as an upper middle-income country; that is, its per capita Gross National Income (GNI) – differing from GDP in accounting for income earned abroad – falls between $4,516 and $14,005. South Africa registered US$6, 750 in 2023,[5] ranking 105th in the world, coming in between Colombia and Azerbaijan. This is also significantly below the average GNI per capita for upper middle-income countries, which sits at US$10,588, and also only slightly above the average for the middle-income group as a whole (those with per capita GNI of between US$1,146 and $14,005), which stands at US$6,379.

Interestingly, South Africa's per capita GNI over the initial part of this period, on a long-running upward trend, has fallen markedly overall since 2012. In per capita terms, South Africa's GNI had fallen by US$1,570, or 19%.



Source: World Bank[6]

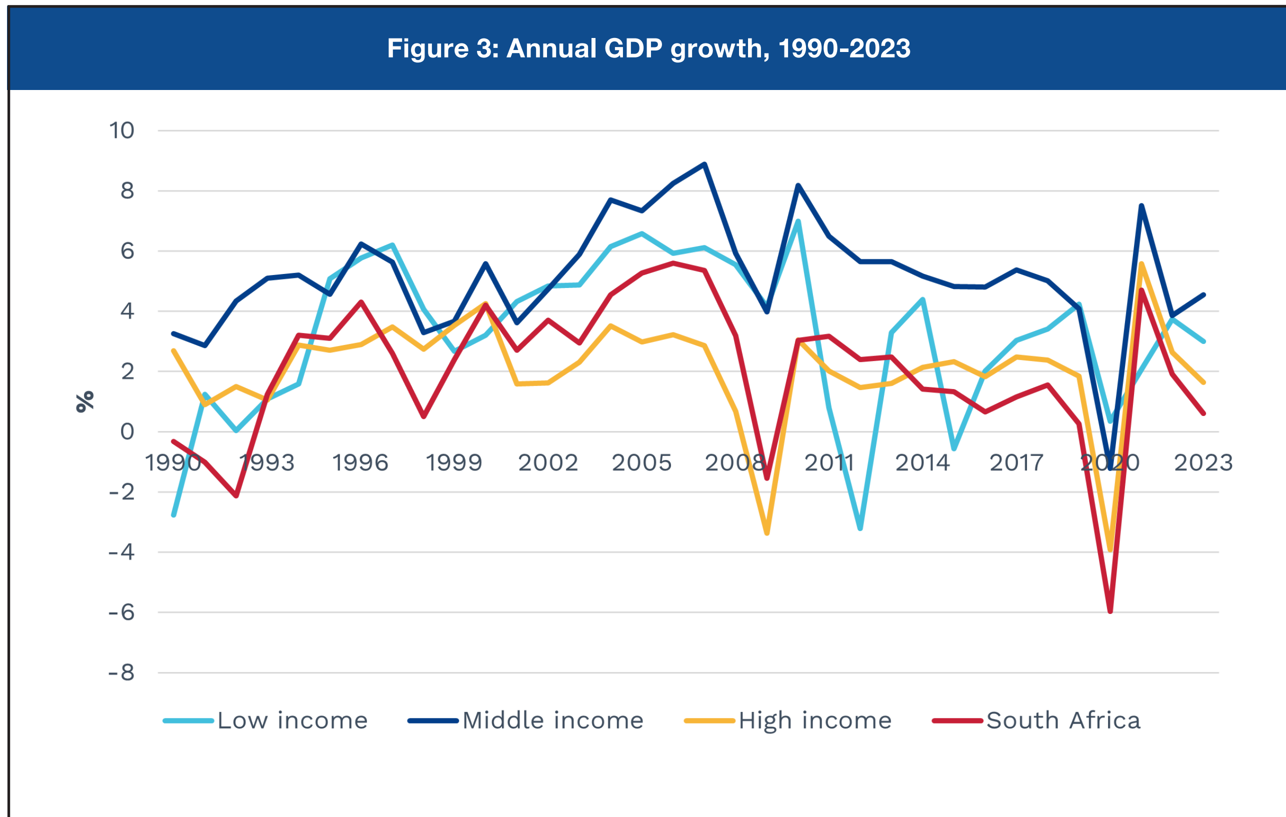
South Africa's economy and its economic challenges cannot be separated from the global environment, or what is termed globalisation. This is described by the International Monetary Fund as follows: "Economic 'globalization' is a historical process, the result of human innovation and technological progress. It refers to the increasing integration of economies around the world, particularly through the movement of goods, services, and capital across borders. The term sometimes also refers to the movement of people (labour) and knowledge (technology) across international borders."[7]

If anything, South Africa has been losing ground globally. Numbers tell important stories, and comparative numbers are especially illustrative. It would not be controversial to say that South Africa's economic performance has fallen short for a long time; what may be underappreciated is the extent to which it has fallen short in relation to its peers.

The world is undergoing a remarkable change. Recently, a column in the Financial Times drew attention to "the rise of the rest"[8] – the rapid development of a heterogenous group of non-Western economies, which cumulatively stand to reorient global industrial and financial power. A phenomenon noted in the early 2000s, it slumped in the 2010s, and now appears back on track.

This is entirely correct. As a rule, growth is simpler at the lower reaches of development. Poorer, less sophisticated economies grow by doing "more" of what they were doing before. More advanced economies tend to make their progress by doing things "better". Growth becomes most restrained in the most advanced economies, for numerous reasons: the size of economies means new activity tends to be reflected in relatively small percentage contributions and increases (and hence small percentage point growth increases), while economic progress demands undertaking "new" and innovative activities.

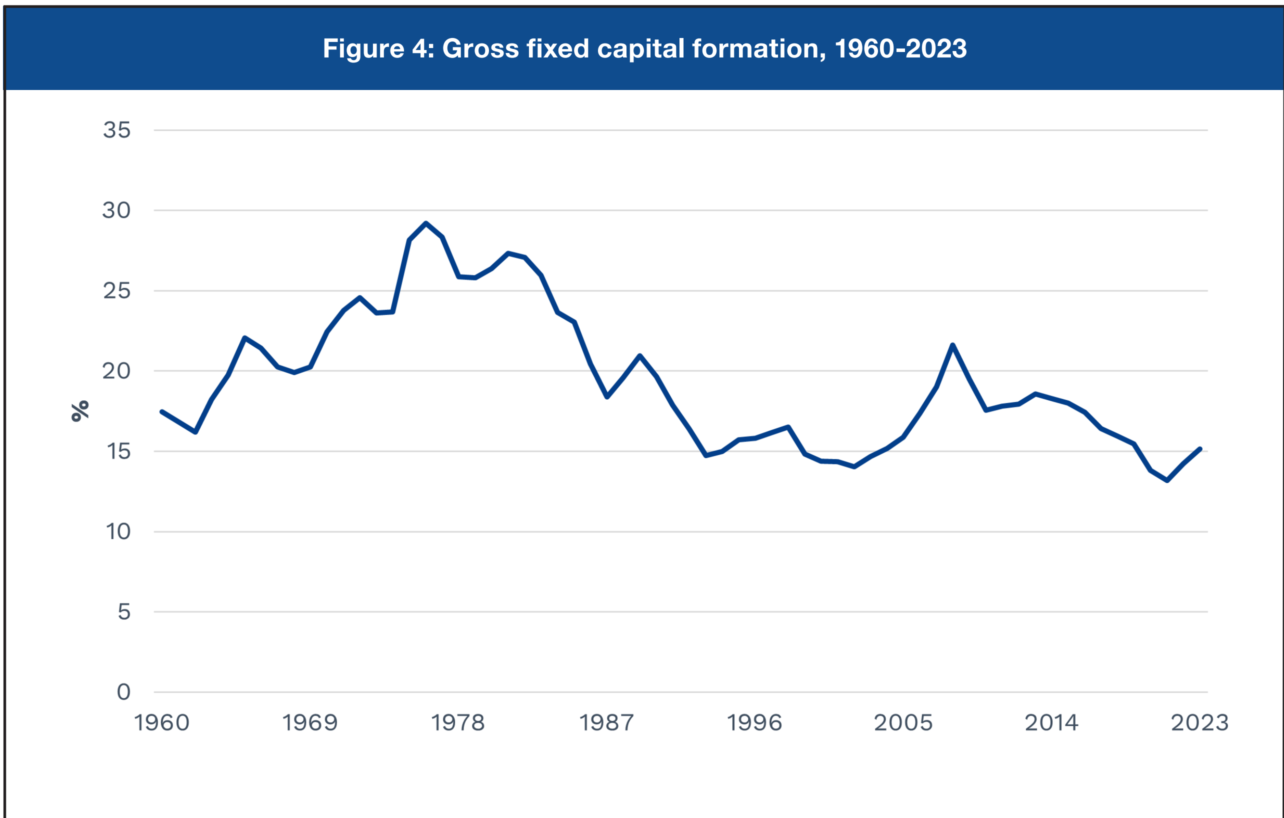
The biggest winners over the past three decades have been middle-income countries. With a combination of favourably priced and adequately skilled labour and satisfactory infrastructure, they have benefited mightily from the offshoring of manufacturing and increasingly of service industries from the more affluent parts of the world. It's a simple cost-benefit analysis. This is illustrated below.



Source: World Bank[9]

Concerningly, South Africa's record has been distinctly sub-par. It has tracked at around half – if not less – that of other middle-income countries. In that last decade, it has even fallen below that of high-income countries, which it would be expected to exceed given its own level of investment. Its middle-income peers have consistently outperformed all their competitors; South Africa's performance makes it an underperforming outlier.

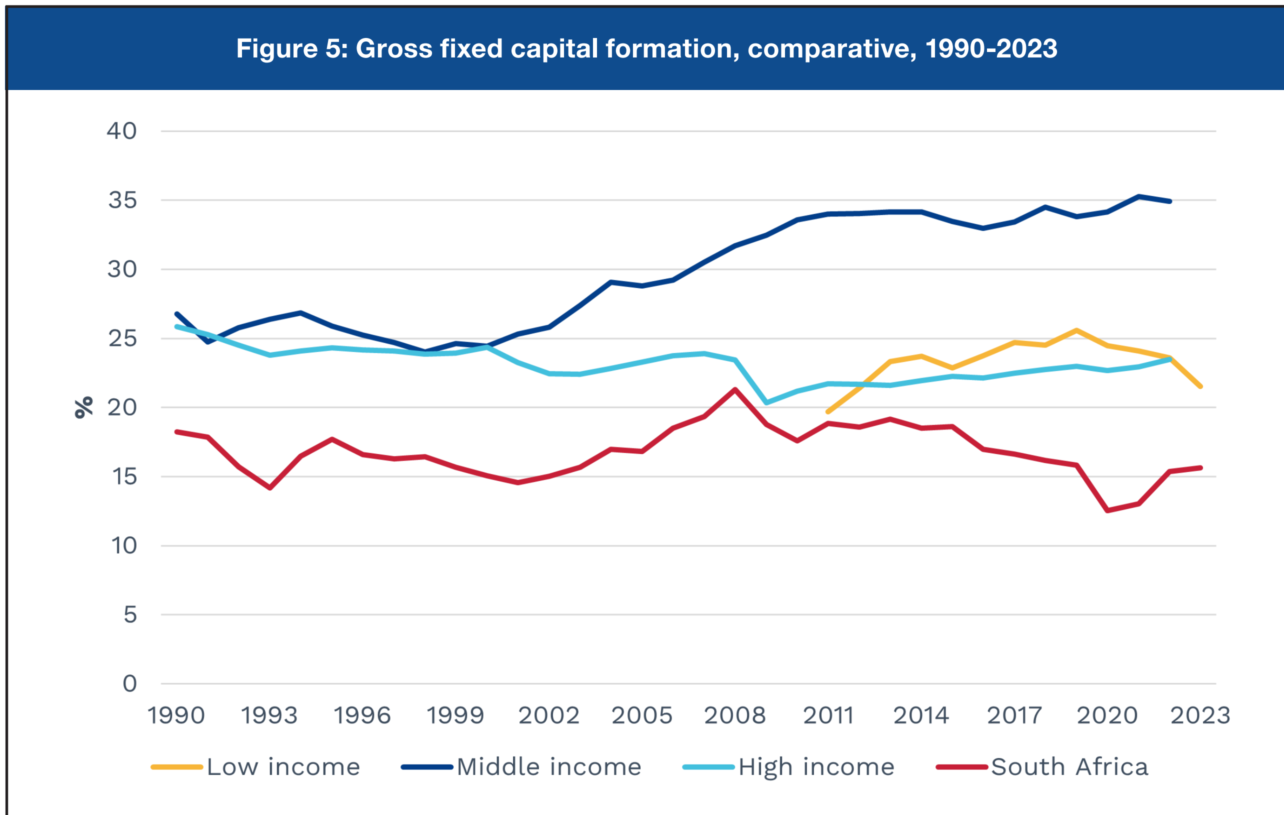
Behind this lies the level of investment. This is the funds sunk into factories, supermarkets, roads, railways and so on. South Africa's long-term trajectory is shown in the table below. The correspondence to the levels of economic growth shown above are obvious. Relatively high levels of investment were recorded in the 1960s and 1970s – this includes investment in mining and in infrastructure, not least in energy assets – with the levels of investment declining overall in subsequent decades. A moderate exception attended the early years of the 2000s, but the overall trend is clear and concerning.



Source: World Bank[10]

Here again, global trends tracked by the World Bank over the past three decades put this into perspective. Middle- and high-income countries entered the 1990s with near identical rates of investment, a little above 25% of GDP. By the start of the millennium, a clear divergence was taking place, and the middle-income group went on strongly to outperform their high-income peers. Middle-income economies have managed investment rates in excess of 30% for well over a decade. Data for the low-income group is patchy, but it lagged behind the middle-income group. (This probably reflects the better economic growth and widening circles of opportunities in middle-income economies, as well as an increasing capacity for endogenous investment in them.)

South Africa, however, invariably fell short of each of these groups. It entered the 1990s with an indifferent level of 18% – unsurprising, given the prevailing instability and uncertainty – and has never been able to gain the traction that would elevate growth sustainably. The NDP envisaged getting an investment rate of 30% of GDP per annum, to drive its envisioned growth agenda. Yet, it has only managed a level of investment of over 20% in one year since the 1990s. In 2023, investment was less than 16% of GDP.

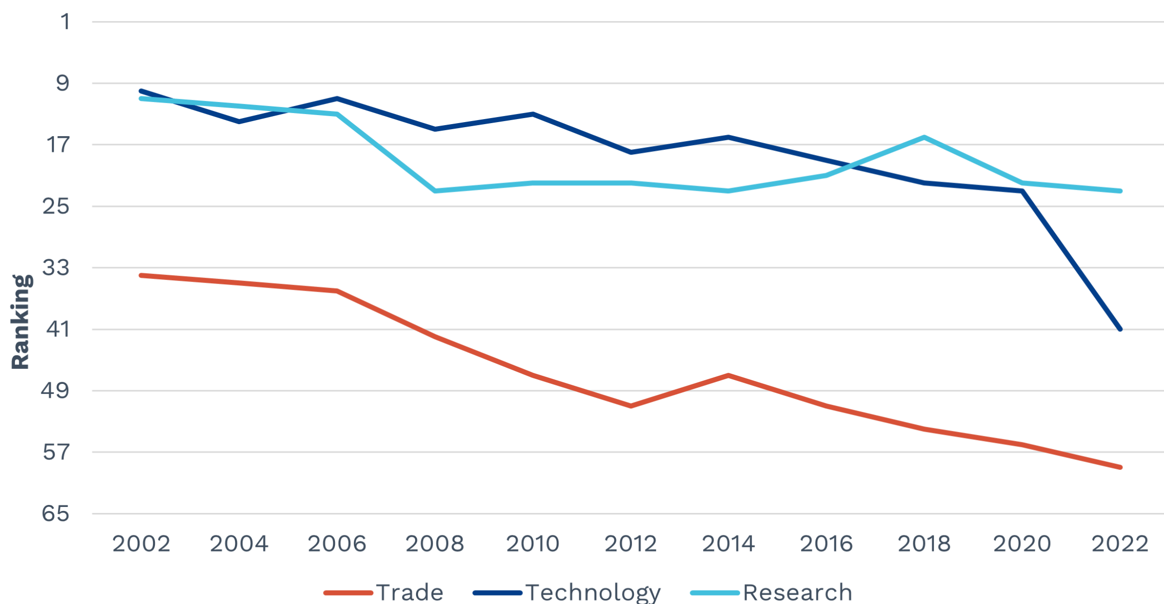


Source: World Bank[11]

South Africa remains stuck on a low-growth path, fundamentally because of a failure to secure the investment that would drive it. And as long as this persists, it will forgo whatever opportunities might exist to profit from the “rise of the rest”. Indeed, it might well see not only its chance at rapid gains eroded, but so too its status as a middle-income country, as its peers become ever more prosperous and today’s less affluent societies position themselves to step into opportunities that these economic shifts create.

One consideration in the latter respect is the complexity of its economy: how adept and competitive a given jurisdiction is in multiple areas of activity. Complex economies are able to leverage diverse opportunities and, crucially, to engage in innovative and higher-value adding activity. The latter is critical for competitiveness in today’s global economy.

The invaluable Observatory of Economic Complexity presents data over decades on economic complexity across a number of fields. In 2002, South Africa was ranked 34th globally for trade, 10th in technology, and 11th in research. By 2022, these had declined to 59th, 41st and 23rd respectively. While these are ranks (and therefore relational), in each case the underlying scores used to determine South Africa’s standing had also fallen.



Source: Observatory of Economic Complexity[12]

The sum of all this is reflected in the direction that the economy has travelled over recent decades, in other words. South Africa's economic performance has been distinctly sub-par, and it shows evidence of regression relative to its peers.

However, before proceeding, an important caveat must be noted. While the broad picture shown above is of a country in severe economic distress, one element remains imperfectly understood. This is what is variously described as its "informal economy" and its "township economy". These are activities that carried on outside the full regulatory reach of the state. Since at the least the 1980s this has been recognised as a significant contributor to South Africans' livelihoods[13] (this is not uncommon around the world[14]). A significant degree of economic activity takes place in this space and may not appropriately be captured by official data. Indeed, in a 1998 study, it was argued that around a fifth or more of those officially defined as unemployed were in fact active in the informal economy.[15] More recently, this theme has been taken up by the work of GG Alcock, a business advisor and expert on this part of the economy – which he popularised through his book Kasinomics.[16] He has argued, for example, that while official statistics put South Africa's unemployment rate at around a third of the workforce (or over 40% if the "expanded" definition is used), the real rate is closer to 15%, if one accounts for various informal activities and income streams.[17] The "informal sector" or "township economy" is hardly incidental to South Africa; but it is an analytical wild card for South Africa. This study has attempted to factor the dynamics of this part of the economy into the overall analysis.

South Africa's investment malaise

Investment needs to be understood properly. Too often, investment is read to mean foreign investment; but in reality, local businesses make a large contribution. South Africa's investment failings are as much a matter of a lack of domestic investment as of a failure to attract foreign capital. As Dr Mark Mobius, then of Franklin Templeton Investments, commented on South Africa a few years ago: "They've got to make South Africa a much more attractive place for investment... I'm not only talking about foreign investment. I'm talking about local investment."[18]

For years, it has been an ongoing complaint from the government that business has refused to invest – the so-called "investment strike".[19] This has been eagerly taken up by many of the "left". It feeds a narrative of business as unpatriotic, selfish, and even malign. Implicitly, it suggests that business is undermining the governing order by stoking socio-economic deprivation. It is a seductive argument for politicians with a predisposed hostility to business, and raises suggestions for state measures to penalise firms for "hoarding" liquidity.

This mistakes the nature of business and of investment. Businesses are motivated by the prospect of returns on their investment – in other words, the expectation that they will be able to make wealth by leveraging their existing assets. If there is a reward to be had in a business venture that exceeds the outlay involved in undertaking it, there is a rational reason to do so. It is under these conditions that investments will be made. This is influenced by assessing the economic incentives and disincentives – potential rewards versus possible costs – by non-financial risks that may exist (whether a country is politically stable, for example, or is in danger of serious collapse), and also by the comparative attractiveness of a jurisdiction (the prospective rewards in one country being better than those in alternative destinations, and so how it would appeal to investors alongside its peers).

Making an assessment of costs and rewards is highly context dependent. Extractive industries are limited by geology and nature to those jurisdictions where particular resources occur. To get at these, the costs (and risks) may well be extreme, but are taken on because of the limited alternatives available. Mining has been a mainstay of South Africa's global presence since the discovery of diamonds, gold and the mining of coal in the 19th century. Even where the environment is highly unpropitious to doing business, the simple availability of a mineral deposit may make an investment in a jurisdiction necessary – for example, the mining of coltan in the Democratic Republic of Congo, or the drilling of oil in South Sudan. Much the same could be said of agriculture, where soil quality and climate are vital, although since quality farmland is a more widely available resource, the constraint is less noticeable here.

As activities become more complex, greater varieties of factors influence the viability of an envisaged operation – and hence the attractiveness of a proposed investment. A manufacturing plant may not be inherently limited by geography, but factors such as the availability of water, the reliability of electricity supply, and the proximity of markets would be considerations. As production processes become more complicated, larger initial investments will be required, and the quality of skills demanded will escalate.

Technology has meanwhile made it possible to integrate production processes across the world, and to seek out efficiencies in a way that would not have been possible even a generation ago.

It is by finding advantages in this milieu that emerging economies have been able to make their progress. Simple manufacturing processes, for example, can be performed cheaply and efficiently in relatively unsophisticated markets, provided the basic inputs and logistics are in place. For this reason, a great deal of the textiles and clothing used worldwide is produced in countries like China, India, Vietnam and Cambodia. These are not ideal jurisdictions to do business in – and were far less so when their economic acceleration began – but they offer sufficient advantages to make the necessary investments attractive.

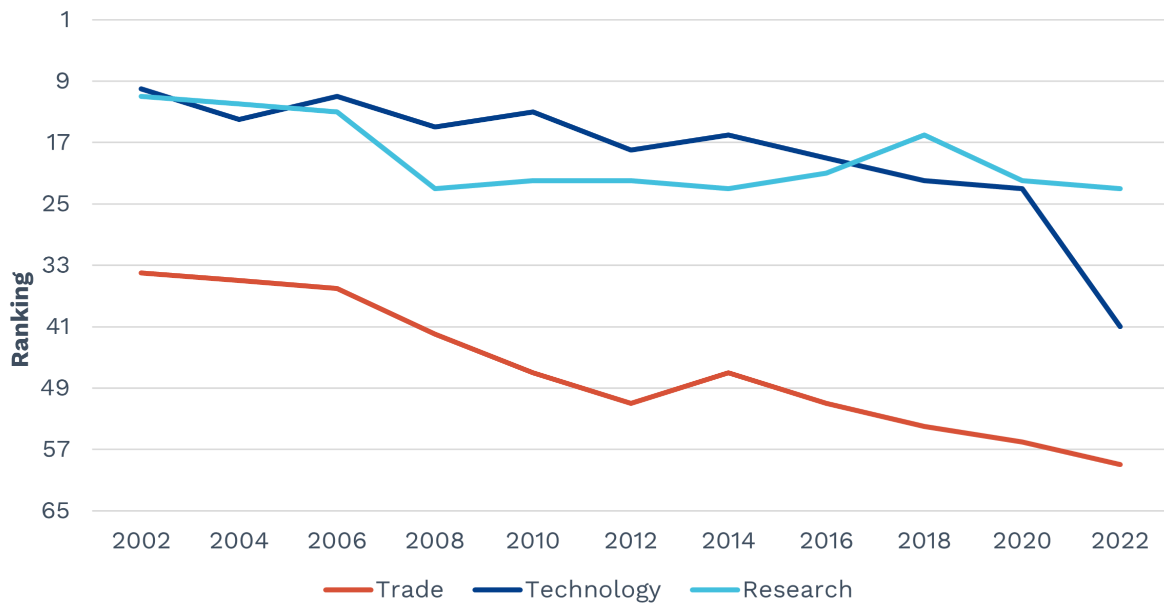
As these simpler value-adding processes endure, as the initial investments are showing their value, as authorities of the country begin to understand how their conduct impacts on economic activity, the economy in question is posed to enter a virtuous cycle. The process is termed “agglomeration”: as more companies establish themselves, so too do related industries to service them. This creates not only a greater quantum of economic activity, but a greater variety of it, with a consequent demand for a wider range of skills, and for entrepreneurial thinking to catalyse innovative projects.[20] This is exactly what has taken place in centres like Chennai in India or Shanghai in China – or for that matter in the Johannesburg area in South Africa.

What, then, has gone wrong in South Africa?

One answer to this has to do very simply with the country’s positioning as globalisation began to accelerate. South Africa entered the 1990s with a partly isolated and protected economy, industrialised, though not fully so, and still heavily dependent on its mining sector. Fixed investment was indifferent during the early 1990s – actually falling noticeably between 1990 and 1993, which was understandable given the political turmoil and uncertainty that attended the transition. The prevailing assumption in many quarters was that with South Africa re-stabilised after the transition to democracy had been completed, and once more a full member of the international community, investment and growth would reassert themselves.

For various reasons, this is not what happened. Investment remained subdued for the rest of the decade, and only picked up in the second half of the first decade of the 2000s, on the back of the global commodities boom and the approaching 2010 FIFA World Cup. Nevertheless, South Africa was simply not as attractive an investment prospect as many of its peers. China had emerged as the world’s wage-favourable workshop after a decade of growth, and was transitioning into innovative and higher value-adding activities. Other countries – India, Indonesia, Mauritius and Vietnam – were chalking up impressive records. This is illustrated in the table below.

Figure 7: Gross fixed capital formation (% of GDP), selected countries, 1990-2023



Source: World Bank[21]

Something that each of these countries had in common with the others was a willingness on the part of their governments to learn the lessons of their own (and others') histories, and to adapt accordingly. This meant being willing to part with long-held orthodoxies. China[22] and Vietnam,[23] both nominally communist societies, had opened themselves up to private enterprise, albeit while keeping tight political control in the hands of political oligarchies. India steadily reformed its inefficient dirigiste economic management system – the so-called Licence Raj, and planning bureaucracy – even in the face of stiff resistance from entrenched interests.[24]

Each of the world's developmental success stories also involved an appropriate level of competence in administration. This amounted to what the Harvard Scholar Merilee Grindle termed "good enough governance".[25] In essence, this means that minimum conditions for particular societal activities exist, even if they co-exist with corruption and failures: bureaucratic systems can process permissions; revenue authorities can collect taxes; infrastructure is maintained sufficiently to enable trade.

Again, what constitutes good enough governance is situational. What is adequate for one country may not work for another. Generally, again, as greater sophistication is required, better governance outcomes are necessary. For a society like China to move from low-wage mass manufacturing to an economy that is increasingly engaging in innovation has been possible because the government that has overseen it has been able to provide increasingly effective outcomes, for example, in terms of the execution of projects and the education of its young people.

It is precisely this that the world's successful emerging economies have been able to capitalise on. They initially offered a satisfactory environment for operations that were becoming uneconomical in wealthier countries – Indonesia may not have measured up to Swedish or Canadian standards, but it was adequate for producing primary goods such as wood, oil or agricultural produce or moderately value-added products such as pulp and paper, textiles and foodstuffs, which could be produced cheaply and exported reliably.

On this basis, and with a growing, educated middle class and an expanding community of entrepreneurs, more advanced and innovative activities, such as electronics and aviation-related manufacturing, could be embarked on. Today, Indonesia's manufacturing sector is larger than that of the United Kingdom or Russia. Its government has become increasingly adept at managing the requirements of a modern economy. Making Indonesia 4.0, its current official economic strategy, sees a future in increasingly high-tech activities (including in relation to its abundant natural resources), upskilling its population, and supporting research and development.[26]

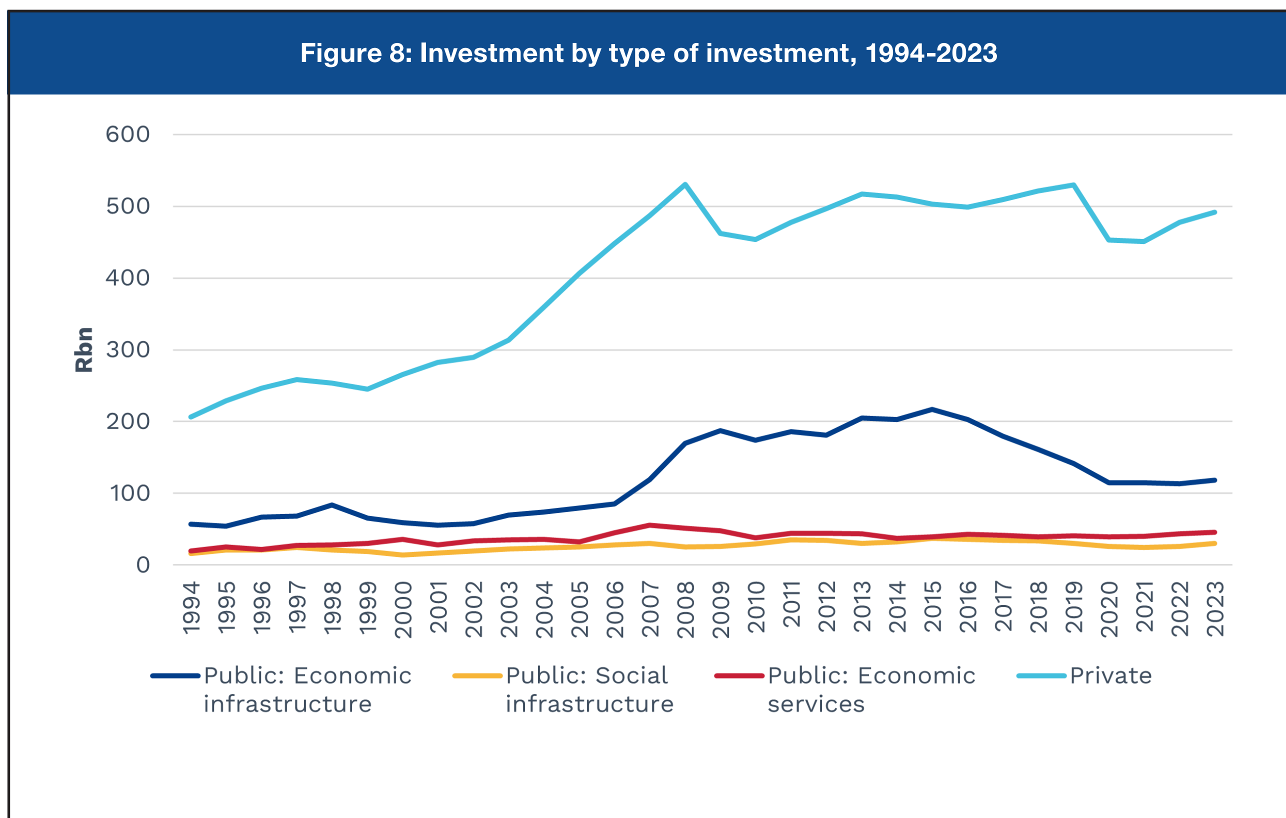
South Africa makes for a poor comparison.

South Africa's investment profile[i]

Before examining the factors that have influenced the investment environment in South Africa, it is useful to set out some of the key trends.

Figure 8 illustrates the trends in investment by type of investment from 1994 to 2023.

Figure 8: Investment by type of investment, 1994-2023



Source: South African Reserve Bank, Centre for Risk Analysis[27]

Investment in public economic infrastructure increased steadily after the government change in 1994, continuing through the late 1990s. However, public economic infrastructure investments took a back seat after 1998, likely caused by a combination of internal and external factors, amongst which is the 1997-98 Asian financial crisis. The crisis hit developing countries hard, including South Africa. In response to the crisis, the South African Reserve Bank (SARB) raised interest rates to protect the value of the Rand, which made it costly to invest.

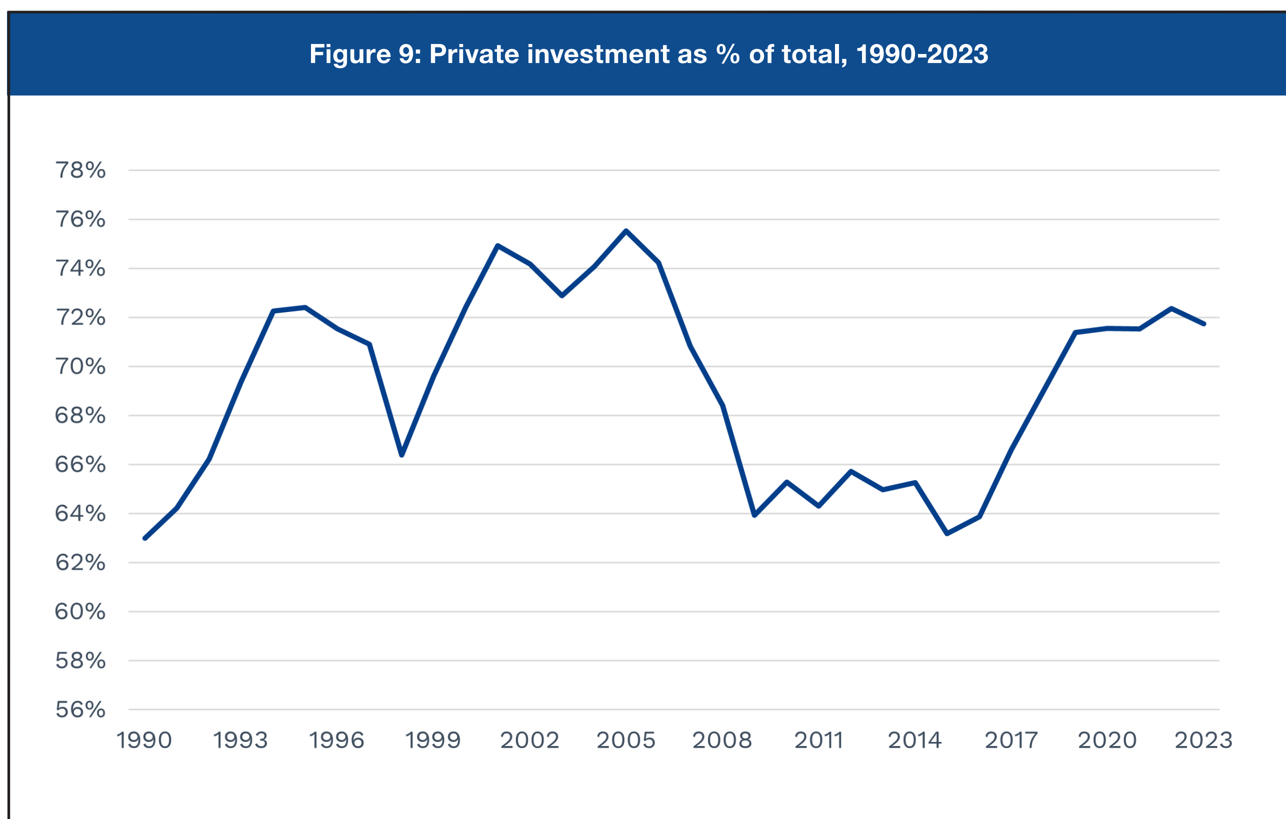
In the early 2000s, investments levelled off. Slight fluctuations in investment can be seen until 2006, when there is a rapid increase in investment by the government in economic infrastructure, likely reflecting the preparation for the 2010 FIFA World Cup and a general public investment drive by the Mbeki-administration with Trevor Manuel as Minister of Finance. This continued until the 2008 financial crisis caused a slowdown and investments levelled off, again with fluctuations throughout the following decade. 2018 marked the supposed end to an era of state corruption and, as a result, the start of a decline in public economic infrastructure investments.

Private investment showed rapid growth after 1994, and it continued into the mid-2010s. As a result of the financial crisis, it also plateaued after 2008. Noteworthy here is that while public economic infrastructure only levelled off in 2008, private investment decreased substantially. It showed no real recovery afterward (which was during the Zuma administration, and likely reflects the private sector's low confidence in the administration) and dropped further in 2020 with the Covid-19 pandemic, as lockdowns hit businesses hard. Note that private investment – contrary to the narrative of an "investment strike" – has consistently outperformed that of the public sector.

There is a clear disconnect between public investment goals and private sector investor confidence.

To illustrate this disconnect further, the following graph shows the proportion of private investment as a percentage of total investment from 1990 to 2023.

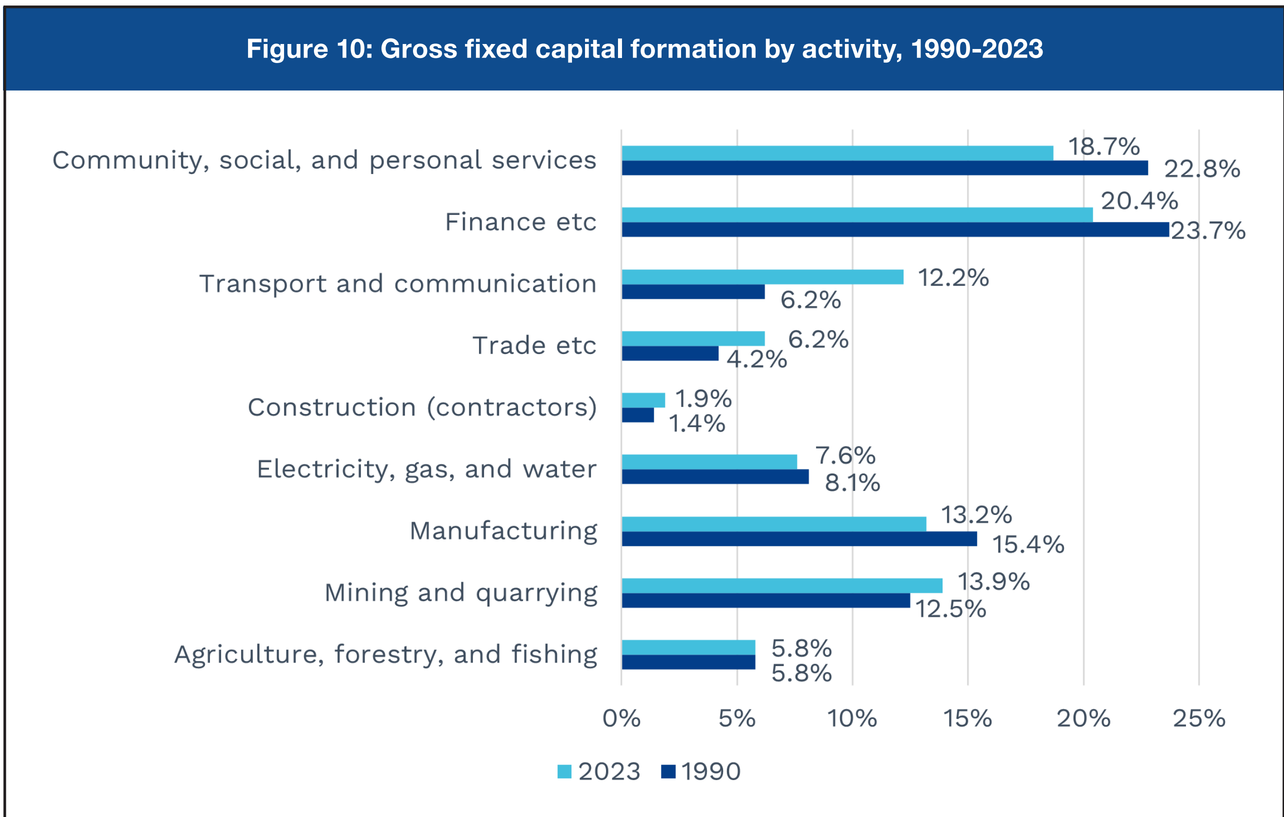
Figure 9: Private investment as % of total, 1990-2023



Source: South African Reserve Bank, Centre for Risk Analysis[28]

Throughout the entire period, the private sector contributed something in the region of two thirds of investment. It underwent a particular surge during the commodities boom, and fell as the global financial crisis hit. Interestingly, during the early state capture period, state spending took up a larger proportion of investment.

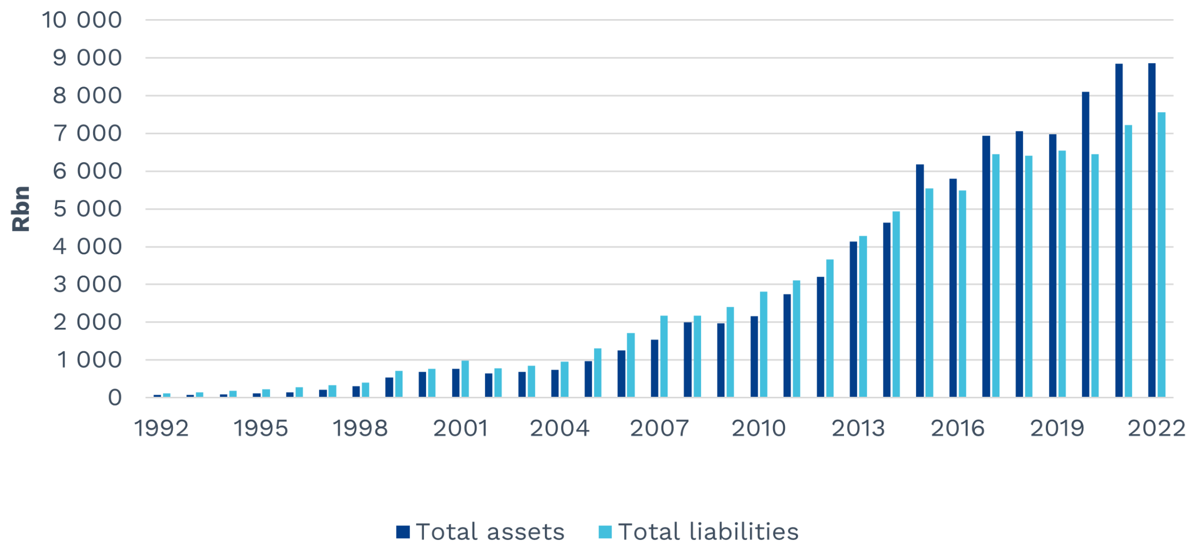
Figure 10 shows the proportion of GFCF allocated to different economic sectors in SA from 1990 to 2023. GFCF represents investment in fixed assets, such as infrastructure, machinery, and buildings.



Source: South African Reserve Bank, Centre for Risk Analysis[29]

GFCF expenditure on transport and communication, trade, and mining and quarrying (in order of magnitude) increased between 1990 and 2023. GFCF on all other activities decreased, most notably GFCF for community, social, and personal services.

Figure 11 illustrates the growth of South Africa's total foreign investment in terms of all types of assets and liabilities across a broad range of investment categories (direct, portfolio, and other investments) from 1992 to 2022. Foreign assets are investments South African companies, banks, or government bodies, hold abroad. Foreign liabilities are investments in South African businesses, government bonds, or real estate that foreigners hold.



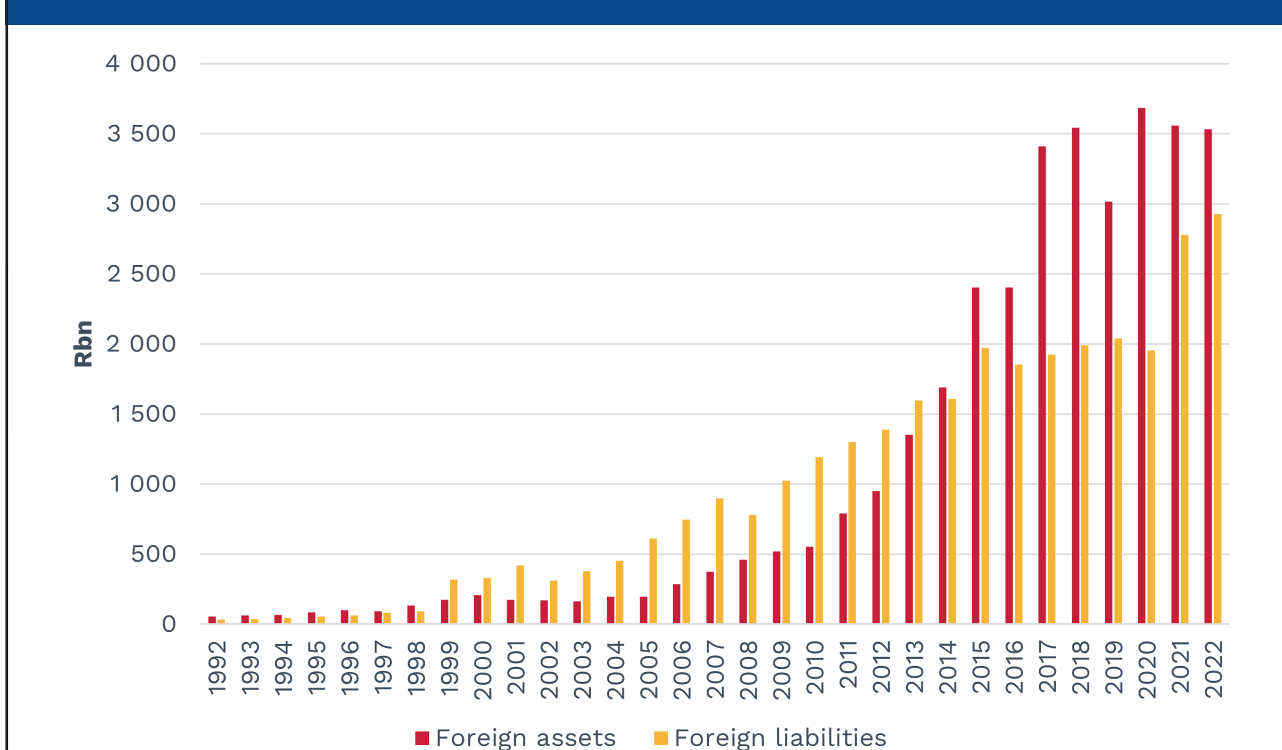
Source: South African Reserve Bank, Centre for Risk Analysis[30]

Both foreign assets and liabilities have shown substantial growth over the period. After apartheid ended, investment levels showed signs of improvement going into the late 1990s. Liabilities still slightly exceeded assets (meaning that more foreign investment flowed into the country than investments were made abroad.)

The 2008 financial crisis barely slowed growth in investment. It only slightly slowed foreign asset growth, but growth in both foreign assets and liabilities resumed afterward, and assets began to close the gap on liabilities between 2010 and 2014. Since 2015, assets increased by more than liabilities, and nearly reached R9 trillion in 2021/2022. (This means that South African entities are investing abroad at a faster pace than foreigners are investing in South Africa. This speaks volumes of the low investor confidence from foreigners.)

Figure 12 on total direct foreign investment shows the evolution of South Africa's long-term foreign investments, specifically on investments focused on strategic, long-term stakes in businesses and infrastructure. These types of investments are generally more sensitive to economic and political shifts.

Figure 12: Total direct foreign investment, assets and liabilities, 1992-2022



Source: South African Reserve Bank, Centre for Risk Analysis[31]

In the early 1990s, direct foreign investment levels were low, but by the mid-2000s, it had increased sharply. This trend continued through the global financial crisis of 2008 (again not slowing down growth). The high levels of foreign liabilities, which peaked between 2015 and 2019, indicate a strong foreign presence in the economy.

Since 2014 and more so in recent years, there has been a convergence between foreign assets and liabilities. This signals a cautious approach from foreign investors following ongoing economic and political challenges, including regulatory uncertainties, the energy crises, corruption, currency volatility and low growth.

South Africa's economic "transformation": the intersection between governance and the economy

The preceding discussion illustrates that bountiful opportunities exist – at least in principle – for middle income countries in the current global economy. It also demonstrates that governance is a key variable in making this possible. Governance here should be understood to mean the continuum from policy to legislation to administration, the worldviews animating action, and how they are acted upon.

In 1994, South Africa's economy was in a parlous state, having experienced several years of stagnation, and a fiscus under severe stress – as shown above, investment as a proportion of GDP had fallen from 18% in 1990 to 14% in 1993. The African National Congress (ANC) had long been committed to a programme of aggressive redistribution through state control. Its lodestar document, the Freedom Charter, had called for widespread nationalisation, a posture fortified by

its association with the South African Communist Party (SACP), as well as the patronage it had received from the erstwhile Soviet Union. It also came to power amid expectations of rapid socio-economic upliftment. The parlous state of the economy had, however, become apparent to it. The failings of socialism globally – and hence the palatability of a platform advocating the seizure of private assets – as well as the lobbying efforts of business and diplomatic interests moderated the ANC's position on this matter, reducing it to a question of the "balance of evidence".[32]

In power, the approach that the ANC took towards the overall management of the economy under the presidencies of Nelson Mandela and Thabo Mbeki was cautious. Alan Hirsch, who headed economic policy in the Presidency between 2002 and 2012, described it as follows:[33]

> The ANC government followed a consistent economic philosophy that had the following elements: at the centre is a social democratic approach to social reform – it is the state's job to underwrite the improvement in the quality of life of the poor and to reduce inequalities, but with a firmly entrenched fear of the risks of personal dependency on the state and of the emergence of entitlement attitudes. The state exists within a market economy that depends on private investment, and therefore a successful state creates an environment that supports high levels of private investment. This does not require the state simply to step aside for business, but rather that it should work with business and labour to develop growth-oriented strategies. The expectation was that because of the limitations of the domestic and regional markets, much of the growth would be driven by exports to major foreign markets. This required both measured trade liberalisation and effective industrial development strategies. Welfare initiatives were to consist mainly of the extension of infrastructure services such as transport, housing and communication, and on the expansion and improvement of social services such as health and education. All this would take place within a responsible macroeconomic policy, as the ANC did not wish to entrust international financial institutions or international banks with the country's future.

Hirsch further notes the attractions that many in the ANC found in European-style social democracy with a strong emphasis on welfare provision, and the East Asian model of state-supported, though fundamentally market-driven, growth and industrialisation.[34] These approaches were a satisfactory normative substitute for those who may have hoped for a socialist order in South Africa, and offered the prospect of rapidly improved quality of life to its constituency along with what the ANC viewed as politically essential reforms to the economy.

As time went on, the interventionist impulse asserted itself. The ANC's 2007 Strategy and Tactics document declared that the party intended to build a "developmental state" – a concept that owed much to the East Asian record – which would power the economic direction of the country:[35]

> It seeks to build a developmental state shaped by the history and socio-economic dynamics of South African society. Such a state will guide national economic development and mobilise domestic and foreign capital and other social partners to achieve this goal. It will have attributes that include:
>
> - capacity to intervene in the economy in the interest of higher rates of growth and sustainable development;
> - effecting sustainable programmes that address challenges of unemployment, poverty and underdevelopment with requisite emphasis on vulnerable groups; and
> - mobilising the people as a whole, especially the poor, to act as their own liberators through participatory and representative democracy.

Having won a handsome majority in the 1994 election, the ANC embarked on an ambitious programme to reform and restructure the economy. This included the creation of the National Economic Development and Labour Council – the relevant legislation was passed in 1994 – to establish a forum for cooperation between business, labour and the government. Remarkably, South Africa lacked a proper economic policy after the transition – the Reconstruction and Development Programme was rather a broad vision for social welfare, which was expressed in such things as the construction of "RDP houses", the provision of free school meals and the expansion of access to medical services. The introduction of the Growth, Employment and Redistribution (GEAR) strategy was intended to position South Africa for growth. It would address negative trends in South Africa's public finances, rein in inflation, stimulate trade and encourage investment by both the public and private sectors. The intention was to see this produce a growth rate of 6% along with 400,000 jobs per year. It would see investment reach the equivalent of 26% of GDP by 2000. Particular stress was put on enticing foreign capital. "The integrity of this growth strategy is therefore dependent on maintaining a favourable investment climate, in order to attract foreign investment," it stated.[36]

GEAR was arguably most successful in addressing the country's public finances. The fiscal deficit, for example, went from 4.1% of GDP in 1994/95 to 1.9% in 1999/2000, and to a small surplus in 2006/07.

On investment, however, the achievements were unimpressive. Although clearly influenced by the 1997 Asian financial crisis – a "black swan" event – investment as a proportion of GDP actually fell slightly between 1996 and 2000. GEAR was also something of a political liability for the ANC, as its allies in the SACP, the Congress of South African Trade Unions (Cosatu) and many in civil society attacked it as "neo-liberal" (a term that signified abuse rather than analysis, but denoted undue deference to business), and for having failed to produce the employment and socio-economic upliftment they demanded.[37]

While economic policy in the macro-sphere may have been regarded as business friendly, in other areas, it deferred to key constituencies represented by the ANC. The ANC's leadership was firmly focused on delivering legislative wins, its take on the economy refracted through a political lens. Arguably the most far-reaching of these was in the labour sphere, predictably given the ANC's historically left-wing orientation and its alliance with the SACP and Cosatu. In short order, a new dispensation was introduced for labour management (the Labour Relations Act, 1995), for labour standards (the Basic Conditions of Employment Act, 1997), for mandatory contributions for training (the Skills Development Act, 1998), for racial preferencing in employment and promotion (the Employment Equity Act, 1998) as well as the establishment of such institutions as the Commission for Conciliation, Mediation and Arbitration (CCMA) and a system of bargaining councils which could set conditions for the entire sector. All of these imposed burdens on a business community operating in an uncertain environment, with a workforce in which skills were often lacking. GEAR had, incidentally, raised concerns about the labour regime, although little was done to accommodate this concern.

Perhaps more importantly for the investment climate over the long term was the social engineering of the country, the so-called "transformation" agenda. The 1996 Constitution had made provision for restitutionary measures for people or groups of people who had been disadvantaged by past policy. In practice, this came to mean black people – broadly defined as Africans, coloured people and Indians, with South Africans of Chinese ancestry being added later – as well as women. The Employment Equity Act established this principle in employment in both the public and private sector (small firms excepted).

The public service was to be brought into line with the country's racial and gender profile (reflecting the "major characteristics of South African demography") and imbued with new values and competencies.[38] In business, the intention was to ensure the "empowerment" of black people – this became known as "Black Economic Empowerment" (BEE) and subsequently "Broad-Based Black Economic Empowerment" (B-BBEE). The latter was legislated through the Broad-based Black Economic Empowerment Act of 2003, as well as a number of sector specific charters which sought to ensure that particular benefits flowed to particular groups. In state tendering, for example, advantages would accrue to firms owned by black people (and perhaps more so to those owned by black women) or to "white" firms that could demonstrate sufficient achievement in empowerment. The sector charters set goals for ownership, management, supply chain development and so on. This imposed another responsibility and complication on doing business.

Parallel to the foregoing, the ANC introduced a programme to secure its "hegemony" over the state and society. Known as cadre deployment, this entailed placing party activists in positions of power across the state and society. This would be necessary to exercise control over "all levers of power". While the operation of this system remains opaque, there now exists a general recognition that it enabled the effective capture of large parts of the state and of the country's state-owned enterprises (SOEs). To an extent this reflected a drive to exert political and ideological control over these institutions, and was clearly also associated with the distribution of political and pecuniary spoils to the great detriment of public ethics and state efficacy, particularly at municipal level.[39] It was condemned by the Zondo Commission into State Capture as lacking a constitutional or legal basis, and being integral to the systemic corruption the commission was investigating.[40]

Cumulatively, these political and policy orientations – in the state and party – constituted an approach to the economy in which the private sector was viewed as the default engine of growth, although under the scrutiny of an intrusive state and "hegemonic" party. From this followed the idea that the economy was largely to be viewed in socio-political terms. Economic of business rationales ("profit") were often of secondary interest to policy makers. Investment has often been viewed from the vantage point of opportunities for empowerment deals or for driving particular industrial policy imperatives.

Moreover, despite the acceptance of a "capitalist" economy, there remains a very notable strain of suspicion towards private enterprise on the part of the ANC, which at times finds its way into the state. ANC documents speak in such terms as a relationship of "cooperation and contestation", and warn of the dangers of political leadership being seduced by business.[41] Senior politicians have at times been given to intemperate attacks on sectors like mining[42] and private medical care,[43] or accusing businesses of being "unpatriotic".[44]

Such attitudes bespeak a lack of understanding as to the manner in which business operates, and help to explain the lacklustre investment performance that has characterised South Africa's economy for decades.

South Africa's Three Ages

The Institute of Race Relations has argued that conceptually, South Africa's post-1994 history can be divided into three broad periods, or "Ages".[45] The First Age corresponds to the incumbencies of Nelson Mandela and Thabo Mbeki, from 1994 to 2007. This was a time of fiscal consolidation, reform of the revenue authorities, and the gradual uptick of real GDP growth rate. This in turn made the expansion of South Africa's welfare grant system possible. All told, this was a fairly good time for the country; the role of the state could be considered "developmental", albeit imperfectly so.

The Second Age began in 2008 with the takeover of the ANC by Jacob Zuma and his associates, and of the state the following year. It continued through his presidency and its tail has extended into the presidency of Cyril Ramaphosa. This opened up parallel to the Global Financial Crisis, and it could be argued that the country never really recovered. It was also a period in which the country nominally switched over into more state-centric economic models: the New Growth Path, which aimed to foster industrialisation, employment creation and greater equality in economic rewards,[46] and the National Development Plan,[47] which set out a long-term vision which relied on the contributions of a capable state (which it recognised needed to be built) as an enabler. Growth declined over time, infrastructure failings became apparent, and concerns were increasingly voiced about the state of the country's public finances and the regular reshuffling of the executive. Corruption scandals, while hardly a new phenomenon, took on grim proportions and delivered the evocative phrase "State Capture". The state had lost the capacity reliably to perform large areas of its responsibilities, even as it continued to make regulatory demands. At this point, it could best be described as "detrimental".

This is illustrated from an investment perspective over the post-transition period.

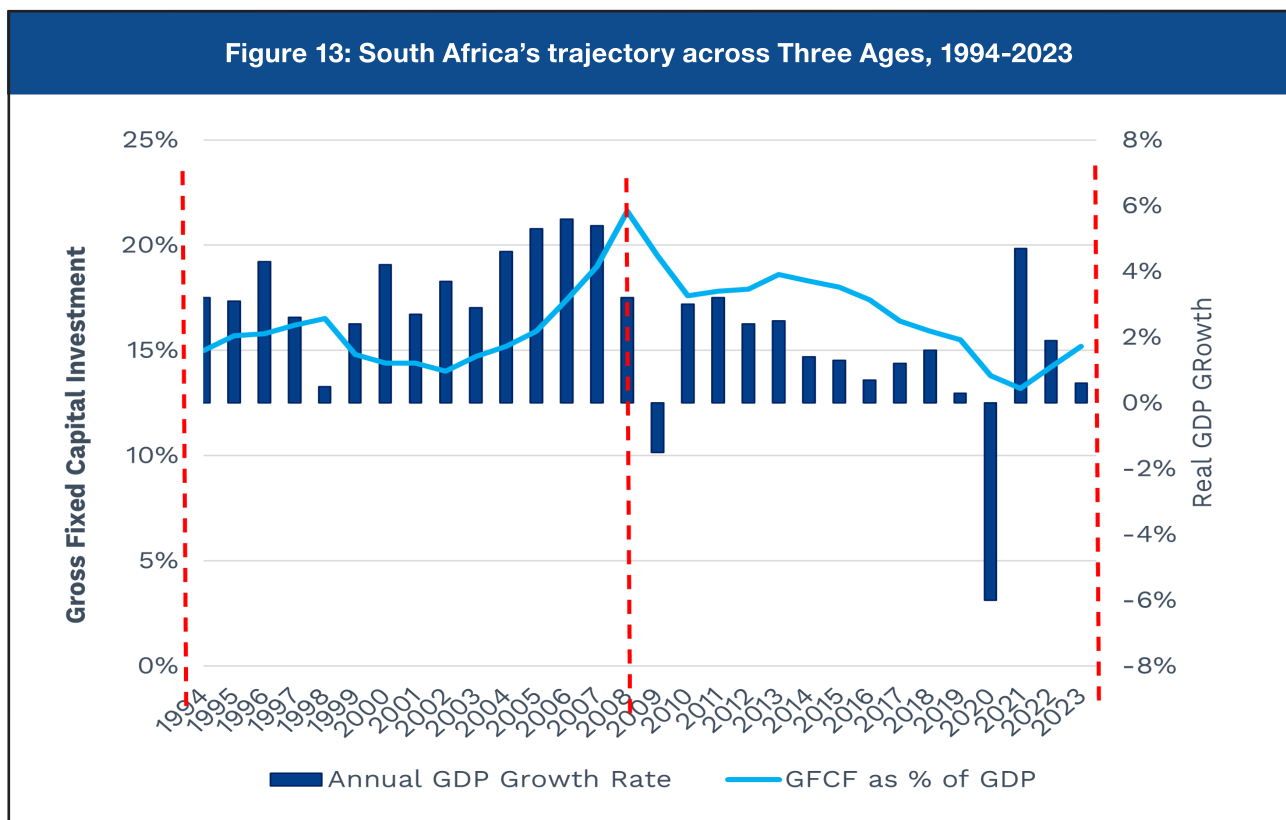


Figure 13: South Africa's trajectory across Three Ages, 1994-2023

Source: Centre for Risk Analysis[48]

What is notable is that in the initial years following the transition there was very little improvement in the level of investment. Indeed, a Reserve Bank Report from 1994 called attention to the fact that capital stock had been ageing, and that investment at this time was committed to addressing this.[49] Much of what followed in the years thereafter represented a "reset" as the country adjusted to the new political order and to its opening to the global economy. There was no rush to invest, and the posture adopted by both domestic and foreign businesses seems to have been to "wait and see". It bears noting that some of the jumps in inward foreign investment in 1999 and 2000 reflected the listing of South African firms abroad and therefore did not signal the commitment of funds and assets to South Africa.

However, as confidence in the direction the country was taking set in, there was a steady increase in investment. It rose steadily across the following decade, peaking at 21.6% in 2008. Had this been sustained, South Africa would be in a much more robust position today.

The "Second Age" sustained a surprisingly high level of investment during its early years. This was, however, buoyed by generous spending by the country's state-owned enterprises. This accorded with the ANC's commitment to the "developmental state", which envisaged using the country's SOEs to drive this agenda. The SOEs, however, frequently spent funds unwisely or corruptly, and were beholden to policy agendas such as B-BBEE (which ultimately mitigated against value-for-money spending) and were penetrated by criminal interests. The outcome was that much of the investment made over this period was ultimately unproductive.

The case of the power station builds at Medupi and Kusile serves as an illustration. Originally conceived in 2007 to address the energy crisis in the country, the costs were initially put at some R163 billion, with completion envisaged in 2015. But by 2019, estimates presented to Parliament indicated that Kusile alone would cost close to this amount (R160 billion), while Medupi would come in at another R146 billion. Chris Yelland, one of South Africa's foremost energy experts, described this as an underestimate: adding additional construction processes, unauthorised expenditure and capitalised interest, he estimated Kusile's costs at R226 billion, and Medupi's at R234 billion.[50]

Despite pledges by President Cyril Ramaphosa to turn the situation around – the "New Dawn" following the "nine wasted years" – many of these pathologies persist. The nominally reformist orientation of President Ramaphosa's administration (now the Government of National Unity) has made limited headway. Its initiatives have been directed at administrative bottlenecks (through Operation Vulindlela) rather than on significant policy change. It has also sought to retain a central role for the state in economic decision making, such as through industrial policy, through amendments to employment equity legislation that impose harsher penalties, and in seeking to create a social compact between business, labour and itself – though the latter failed to gain traction, arguably because the state has lost credibility.

The National Planning Commission remarked in a review of the NDP: "A significant challenge and contradiction that goes against the developmental state aspiration of South Africa identified is the rejection of meritocracy in the country's public service. Persons are appointed to jobs in State-Owned Entities and the public service without the requisite experience, skills or gravitas as a result of inappropriate political involvement in selection and performance management."[51] In an oblique acknowledgement of the severity of the problem, the government has committed to a turnaround strategy for the public service, revealingly entitled A National Framework towards the Professionalisation of the Public Sector.[52] The admission that the public sector must be "professionalised" – not "upskilled" or even "reprofessionalised" – raises a host of awkward questions as to how a government that was vocally committed to using the state in an activist and developmental mode could allow the current situation to develop over three decades of constitutional rule, and around the damage that it would have inflicted on state capacity.

This has led South Africa to the "Third Age". Its nature remains to be revealed, but indications are that the state might now be described as having been "emasculated". In other words, it lacks the ability to make its authority felt. This is of course not complete across society, but there are prominent examples of it. In July 2021 the state effectively lost control of parts of the country as rioting broke out following the incarceration of Jacob Zuma. "Mafias" have emerged to extort rents from businesses.

The widespread failure of local government has come at huge cost to the liveability of communities, and has forced residents to undertake tasks for which they are already taxed.

Engaging with this reality poses questions about South Africa's potential as an attractive emerging market and thus about its attractiveness as an investment destination. It provides a framework for understanding the hindrances that confront South Africa in appealing to investors, and the choices that might be made to address them – and perhaps most importantly, the limitations attending the options available.

What this brief survey of South Africa's trajectory illustrates is that the state of governance – the complex of policy, its implementation and the administration of the state – is central to the malaise. The blunt reality is that the South African state is simply not up to the task of managing the economy, although it has not surrendered the ambition to do so. Much of what has brought South Africa to this point can be attributed to choices that have consciously been made, as a result of what one commentator once described as "ideological overreach".[53] Or, as KN – mining engineer, fund manager and analyst – said during an interview for this study: "It all starts with policy."

"Uncertainty", "certainty" and their consequences

The combination of ideological impulses, an interventionist policy stance, along with often weak and compromised institutions create a difficult business environment. This is typically rendered as "uncertainty". This is an issue that is at times acknowledged by the state. Establishing "certainty" around a range of policy issues, for example, was flagged in the NDP as a necessity for investment.[54] A National Policy Development Framework, approved by Cabinet in late 2020, likewise noted the importance of policy certainty.[55]

For PT, an executive at a business organisation interviewed for this study, this is the country's macro-conundrum: "It is trite to say that one invests when there is a reasonable prospect of a return. A socialist may say this is a terrible thing, until you factor in what this produces – jobs, wages, pension funds et cetera. The reality is that South Africa is a very unstable place to do business. There are serious social cleavages. There is huge complexity in the regulatory environment, along with wide latitude to policy administrators to interfere and set their own terms. Think about competition policy ... So, there is standard commercial risk in making an investment, and the sense that one is making a bet on the direction of what future policy will look like. Some of it is downright anti-investment, like the National Health Insurance."

PT adds that this comes on top of growing weaknesses in the economic foundations, in terms of infrastructure, crime and so on (these are discussed briefly below). There is a real concern about future failures in these areas given the country's record thus far. Cumulatively, this adds up not only the risks but the costs of doing business in South Africa and weighs against a willingness to commit funds to the country – all of this functions as an additional "tax" on business. This makes South Africa a hard sell for investors, particularly those contemplating direct investments. Foreign investors tend to be restrained in their enthusiasm for South Africa, and to keep it as a minor item on their portfolios, despite considerable opportunities in fields like mining. Local investors too are seeking foreign opportunities. This is a respectable strategy for growing investors' holdings, but it seems increasingly now to be driven less by the outsized rewards of new markets than by concerns about South Africa's subdued prospects.

He comments further that there is a disjunction between what the state (and other stakeholders, such as the labour movement) assumes to be true about business operations and the latter's realities. There is a widespread assumption that profits constitute a large (and morally unconscionable) part of business turnover. This is incorrect: "Take into account the costs of operating a business, spending to make up for a lot of what the public sector doesn't get right (like having back-up power), as well as the social contributions: wages, other staff costs, taxes, and so on. Profits are not great. They're often not particularly competitive, and remember that it's out of that that you will get the funds for further investment."

Larger and more complex investments – ironically, the sort of value-adding operations that official industrial policy seeks to promote – might offer greater returns, but require large outlays and long lead times. Where the direction of policy is unclear, or where policy makers seem oblivious to the realities of business operations, these are commitments that investors are reluctant to make. As KN says regarding mining: "Policy determines how your existing operations work... mining wants certainty. It's a decade before you see returns. There are huge burdens and expectations on mining, but very little understanding of it."

EH, a prominent economist and investment advisor, also attributes South Africa's poor investment performance to the state of governance. Wealth creation, he says, has three preconditions: security of property rights; freedom to trade; and sound money. However, the state is unable to protect property (even the lives of its citizens) and threatens the security of assets through such measures as the custodial taking of mineral rights and the Expropriation without Compensation (EWC) agenda. The freedom to trade is compromised through intrusive labour legislation, licensing (often inefficiently implemented) and empowerment demands. The value of money is undermined – the best efforts of the SA Reserve Bank notwithstanding – by the rise of administered prices. Interestingly, however, he argues that South Africa is not subject to policy uncertainty, but to policy certainty: the counterproductive and interventionist policies have arisen from the ANC's ideological beliefs. This makes reform a very difficult prospect.

However one may evaluate the competing perspectives, the inescapable conclusion of the foregoing discussions is that improving the flow of investment into the country demands a serious recalibration of the role of the state. Governance is simply not up to the task of driving anything like the ambitious agenda that it has tried to set for itself. Attempts to do so have not produced the desired results, and have arguably achieved the opposite.

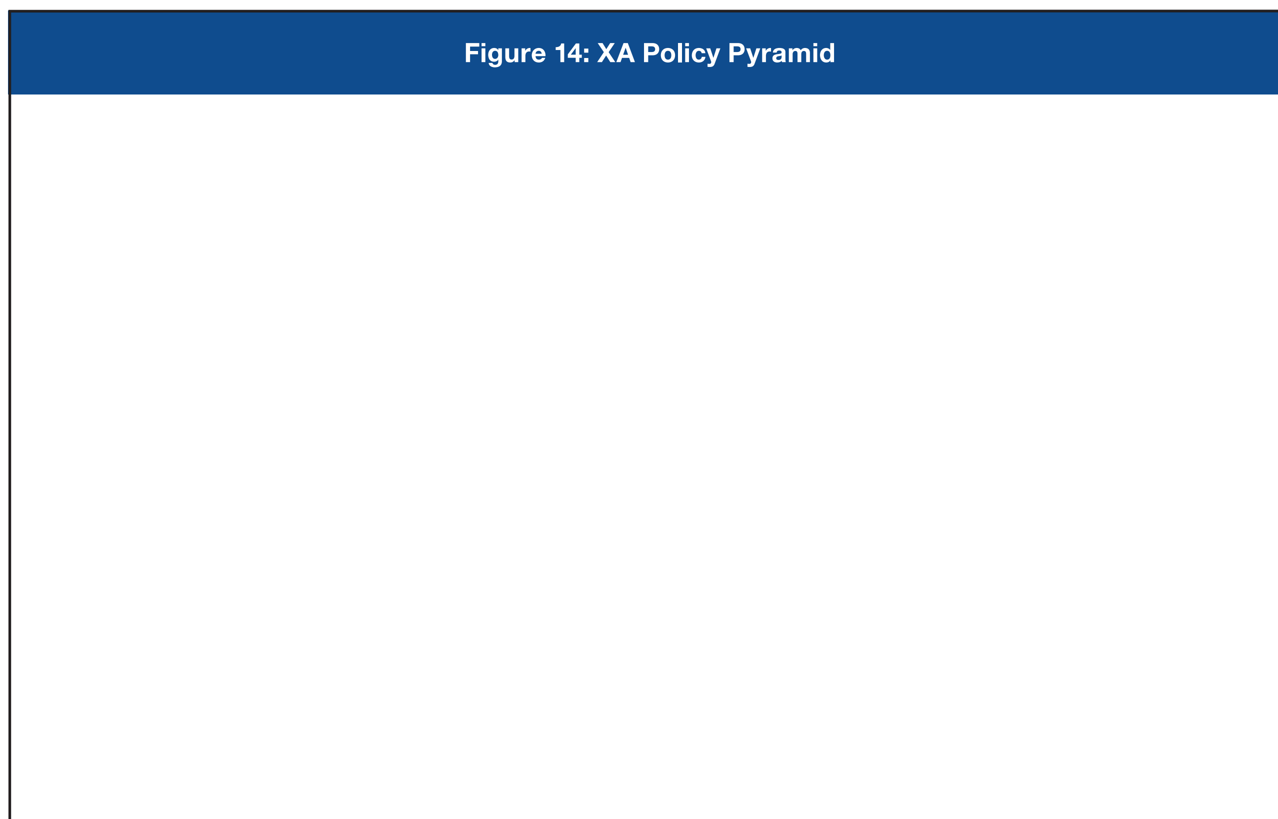
Indeed, an important recent contribution on South Africa's growth possibilities places the issue of failing state capacity under scrutiny. This study, Growth through Inclusion in South Africa,[56] was produced by The Growth Lab at Harvard University, and identifies two generic brakes on growth as the failings in state capacity, and the country's extreme spatial exclusion. The first of these refers largely to the state of power, water, logistics and security, public goods for which the state is responsible, and which it has long resisted relinquishing control over. The second is a function of South Africa's history, which sought to keep communities apart, and resulted in large populations being located far from economic opportunities. Building state capacity will demand a new approach to the management of the state, and will clearly entail some tough choices to achieve this – some being antithetical to the prevailing ideological preferences of the country's political and administrative leaders. Taking action to overcome spatial exclusion will be impossible without a skilled and effective state to oversee it.

This means that in some sense, the state must be "fixed". (The IRR's study of and recommendations for administrative reform, In Service of the Public: Reforming South Africa's Public Administration,[57] proposes a way forward.) This is, in turn, certain to be a long-term project. It will need to be undertaken alongside measures to improve South Africa's investment attractiveness, since the latter is critical to South Africa's future economic viability. What follows is intended to provide a discussion of some of the key hindrances to investment – or, better said, to the creation of a propitious investment environment – as well as possible solutions, taking into account the limitations inherent in South Africa's current governance.

South Africa's investment challenges

Accepting that South Africa has performed poorly on investment, and that poor governance has played an important and deleterious role in this, it is necessary to delve deeper into understanding how this is manifesting itself. To illustrate this, a simple but revealing schematic put together by XA Global Trade Advisors is a useful tool.

Figure 14: XA Policy Pyramid



Source: XA Global Trade Advisors

It is structured like a pyramid for good reason: it mirrors Maslow's hierarchy of needs. In the case of the XA pyramid, the factors captured on the lower levels are more broadly critical for success, while those on the top represent bespoke interventions requiring particular capabilities. It should be noted that XA's primary focus (as per its name) is trade. However, the hierarchy of concerns are generically applicable to economic activity, and are thus applied in this analysis to investment.

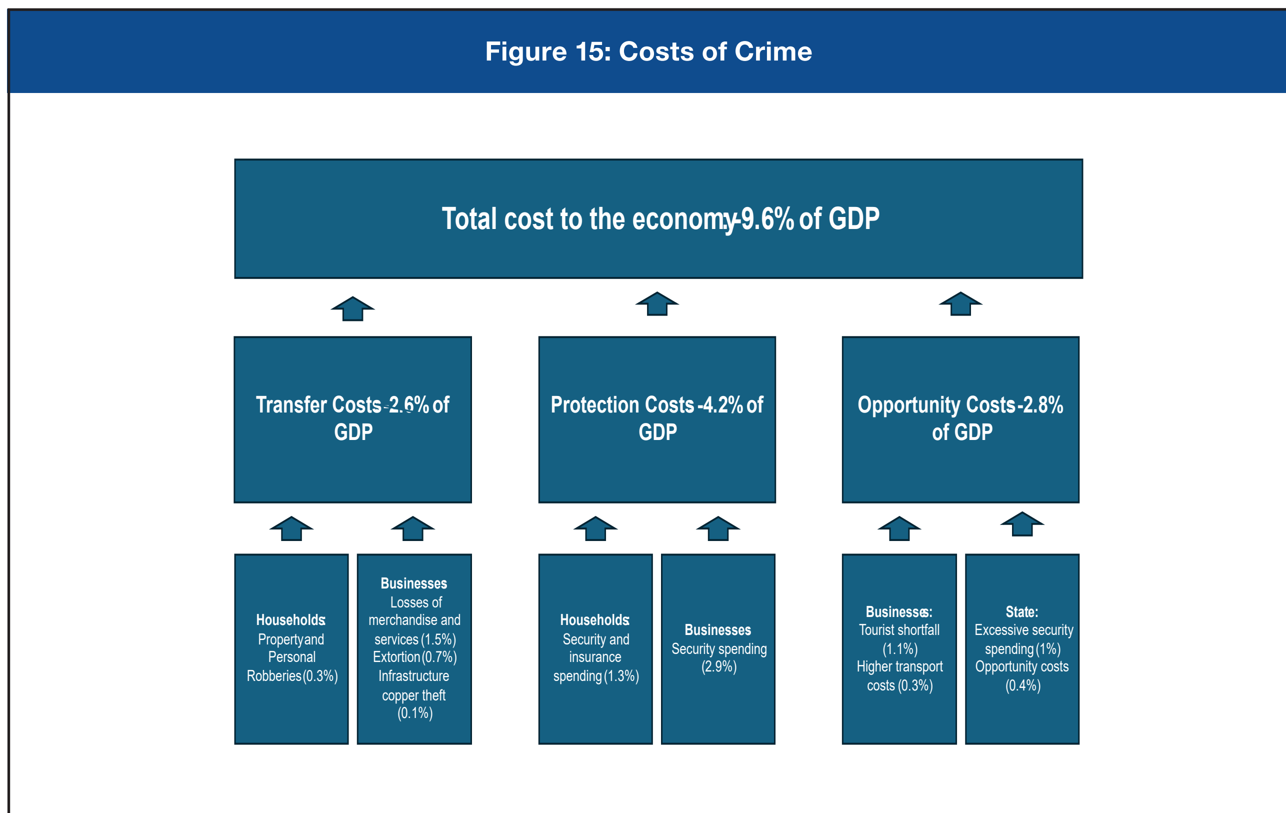
Using this as a guide, the following analysis considers three sets of factors. The first isfoundations, corresponding to safety and security and infrastructure. These are the basic conditions that make economic activity – indeed, societal activity – possible.

This can be termed the area of “good enough governance”. The second id value-adders, conditions that are necessary for more complex activities, such as the skills base available, the quality of the regulatory environment and the understanding of the operations of the economy on the part of policy makers and officials – and hence the ability to act and intervene constructively. This may be described as the “good governance” area. The third is the drivers, the high-level interventions that act as economic accelerants. This is broadly the terrain of “developmental governance”, the ability to leverage state support and policy, and to coordinate with (or indeed to direct) business to act in a manner that promotes the broader national interest.

Foundations: “good enough governance”

There is little debate that South Africa suffers from a number of weaknesses in its foundations. One of the more obvious is the failure of **physical security**. Security underwrites the predictability that makes an investment possible, and also the psychological assurance that one will be around to enjoy its fruits. Conflict has been a major brake on economic activity, especially in Africa.[58]

Much the same is true for crime. For South Africa, crime – both against persons and property – has come with severe economic implications. In terms of raw costs, a 2023 World Bank report put the costs of crime in South Africa at the equivalent of around 9.6% of the country's GDP. Direct losses come in at 2.6% of GDP, expenditures such as security and insurance at 4.2%, and opportunity costs at 2.8%.[59] This is distributed thus:



Source: World Bank

The Global Organised Crime Index[60] — which measures and ranks the state of organised crime across countries — gives South Africa an overall “Criminality” score of 7.18 out of 10 (higher scores reflect greater criminality) in 2023. This places South Africa seventh globally, third among African countries, and first in Southern Africa.

The index places South Africa in a worse position than such jurisdictions as Colombia, Nigeria and Mexico.

Its "Resilience" score — reflecting its institutions, calibre of leadership and similar — stood at 5.63 (higher scores denote better resilience). This places South Africa 50th globally, fourth among African countries, and first in Southern Africa. South Africa is, in other words, highly vulnerable by international standards to organised crime, but indifferently able to respond to it. Its favourable regional rankings should not be overstated, since South Africa has a highly sophisticated economy, with the need for resilience being consonantly greater than its peers.

Of particular concern is that organised criminal networks have been able to penetrate the state and legitimate business value chains.[61] South Africa hosts a wide array of organised criminal activity, originating both in the country and abroad. This includes the trafficking in drugs, firearms, people and murder for hire. Extensive corruption within the state has made it a tempting target for criminal groups – for example, fraud perpetrated during the Covidpandemic – while there have been allegations of links between political and criminal figures.[62] Certainly, there exist concerning continuums between state failings and the criminal world, as studies of the illegal firearm trade have revealed.[63] Politics in parts of the country is marked by intimidation and assassination, albeit typically reflecting competition with organisations rather than between them.[64] Other criminal groups have taken to extorting businesses to allow them to operate – this has been most intently evident in the so-called "construction mafia". Interestingly, these have phrased their demands in terms of state "empowerment" policy.[65] Indeed, state corruption and the deliberate commandeering of the state apparatus by the ruling party have constituted something approximating organised crime.

The outcome has been a state that is finding it extremely difficult to maintain law – and in which the assumption that it actually seeks to do so is by no means universal.

Added to this is a high level of inter-personal and opportunistic crime, often marked by violence. While comparative data is incomplete, the World Bank's database allows the following comparison for murder for 2020. Vietnam reported a rate of 1.5 per 100,000 people in 2011 (the latest available), while sub-Saharan Africa as a whole reported 13.3 the following year.

Figure 16: Homicides, 2020 Figure 15: Costs of Crime

Source: World Bank[66]

Much of this is difficult to quantify, but if the numbers shown above are an indication, the impact is likely to be stark and severe. Above all, there is some evidence that businesspeople are reluctant to consider ventures in South Africa because of its reputation for criminality. This reflects concerns about the security of investments as well as for their personal safety. SDC, a South African machinery manufacturer with markets across the world, recalls that a potential deal with a correspondent firm in the United States fell through on these grounds. The client firm insisted on viewing the South African plant as part of its due diligence, but after some rudimentary internet enquiries, decided that visiting the location would constitute too great a personal risk for its staff. That the South African firm produces state of the art equipment and provides high-wage, high-quality employment in a generally depressed part of the country underlines just how damaging the consequences of these reputational issues can be.

This is the case for "property crime" too. A survey of crime on South Africa's commercial farms for 2017 put the cost at some R7.7 billion. Close to 40% of farms reported stocktheft, 37% the theft of infrastructure, 35% of tools and equipment, 28% illegal hunting, and 25% robbery. Moreover, only 25% reported all instances of crime to the police, and 52% some instances, with a large proportion of respondents feeling that doing so would be pointless.[67] This conveys both the damage that crime inflicts and the stoic acceptance that those operating in the economy have developed to cope with it.

WM, a farmer and agricultural economist, says that for the most part, farmers have learned to contend with the high-crime environment. Adaption strategies such as extra security features, and the use of drone technology to monitor farm activities have mitigated the danger somewhat but come with their own costs. "If a farmer has to install security features, that's another line item on the budget. And that's money that's not being used for expansion."

He adds that the consequences of what may seem like a simple act of theft can have ramifications that outside observers may not fully comprehend. For example, the theft of a bull could disrupt a long-term breeding scheme, which points to the considerable financial losses that such a crime will incur. Smaller operators, meanwhile, tend to lack the resources to deal with a loss like this, and can effectively be ruined.

This is a pattern noticeable elsewhere. A study of some 446 small and emerging firms across South Africa's urban centres in 2008 – admittedly dated, though it is unlikely that the trends it describes have changed much – found that over half had experienced at least one crime over the past year. Smaller operators were especially vulnerable, and the report noted that those "on the verge of entering" the formal economy were at particular risk, a matter with grave implications for growth-focused economic activity.[68]

GG Alcock offered a supporting view in an interview for this study.[69] Crime, he says, has been a growing problem for the township economy, particularly as extortion demands have become organised and institutionalised – variants of the "mafias" mentioned previously. These started targeting foreign-owned businesses but have expended to demanding payments from South African operators too.

On infrastructure, meanwhile, the problems are well known (and have been canvassed in an earlier IRR study, Reinforcing South Africa's Growth through Infrastructure). A reliable supply of power is foundational to a modern economy, and South Africa entered the democratic era with some of the world's cheapest electricity, and a surplus to boot. The latter was rapidly consumed as electricity provision was expanded, but without a concomitant increase in generation. This was compounded by policy decisions intended to advance particular business interests (typically to push B-BBEE, or to advantage politically connected businesspeople), and by the malfeasance that took hold at the state utility.[70]

The upshot is that South Africa endured close to two decades of "load shedding" – while 2024 has seen a reprieve, it is unclear whether the crisis is over, still less whether the capacity exists to underwrite significant growth. The table below gives an indication of the problem.

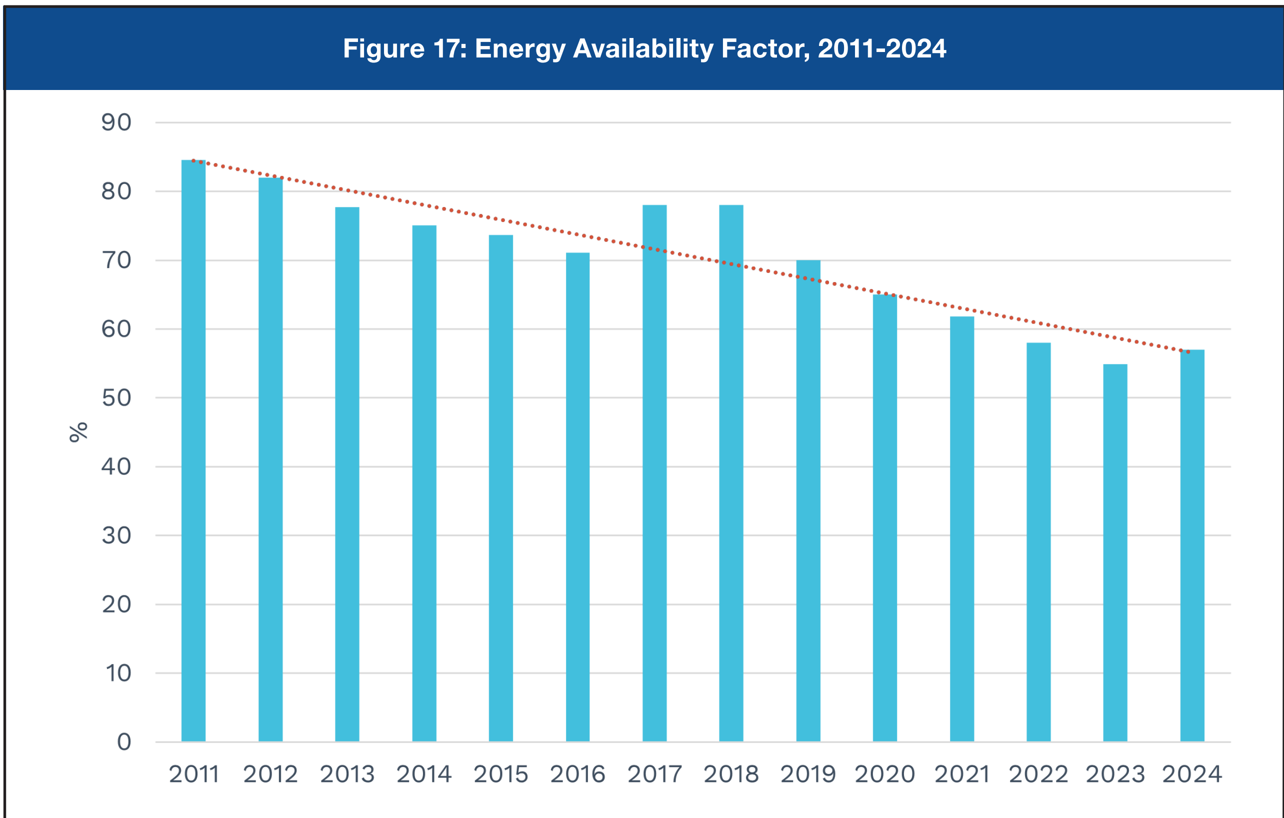


Figure 17: Energy Availability Factor, 2011-2024

Source: Centre for Risk Analysis

The Energy Availability Factor is a measure of power station availability that takes account of energy losses that are not under the control of plant management and internal non-engineering constraints. Its decline is apparent from this graph. In 1999, the EAF stood at 91%. When the first rounds of the power crisis hit, in 2007/08, the EAF was at 85%. In 2013, it dipped below 80%, and in 2020, below 70%. In 2024, it sat at a dismal 57%. In other words, over that period, South Africa's EAF has fallen by a staggering 34 percentage points.

Similarly, an effective logistics network is indispensable for an economy to move goods. Rail transport is an essential hard sinew of transport, but the state of South Africa's rail network has long been of concern. South Africa's freight service, Transnet and its passenger service, PRASA, have been in distress for years, mired in corruption scandals and beset by vandalism and mismanagement of their assets.[71] As an example: in 2017/18 freight volumes stood at 226 million tonnes. By 2022/23, this had fallen to 149,6 million tonnes. A small upturn in the 2023/24 year (when the freight volume stood at 151.7 million tonnes) was a positive sign, although still indicative of a crisis.[72] In the 2022/23, the Minerals Council South Africa estimated that R150 billion in potential revenue through ore exports was lost as a result of Transnet's failings.[73]

The decline of the rail system has pushed ever more cargo onto an overused and undermaintained road network, with the associated costs, as well as safety concerns (drivers and their cargos being a target of criminal groups), as well as considerations relating to carbon emissions, a matter of not inconsiderable importance when goods are sold in environmentally conscious markets.[74]

Ports, meanwhile, connect a country with the world, making global trade possible. But research by the World Bank and S&P Global Market Intelligence, the 2023 Container Port Performance Index, put the Port of Gqeberha (Port Elizabeth) at 391 of the 405 surveyed, Durban at 398, and Cape Town at 405. South Africa's neighbours performed better, with Mozambique's Beira at 347, Maputo at 317 and Namibia's Walvis Bay at 380.[75]

All of these push up the costs and difficulties of doing business, and hence also of investment. It should be noted that this discussion has presented a bird's eye view; however, as PT notes, infrastructural failings are also experienced locally, and can have destructive consequences for a community's economy. He points specifically at the responsibilities that municipalities carry to provide electricity to consumers, residential and commercial, and the consequences of the collapse of local networks or the failure to render accurate accounts.

A great deal has been written about the crisis in local government, and need not be rehearsed in detail, though a comment from the Auditor General captures the concerns:[76]

> For years, local government has been characterised by deteriorating standards of living, service delivery failures, dysfunctional municipalities, council and administrative instability, financial mismanagement, service delivery protests and crumbling municipal infrastructure. Citizens continue to express their dissatisfaction and frustration through the media and other platforms, calling for urgent attention to address their plight.'

Unsurprisingly, poor municipal performance is correlated strongly to what businesses – and especially smaller businesses – spend on maintaining their operations.[77] In one striking example, poultry processer Astral Foods fought repeated court battles with the Lekwa municipality in Mpumalanga over the municipality's failure to manage its affairs and render the services that the food plant required. Eventually, Astral obtained a licence to draw raw water from the Vaal River itself, an extraordinary case of a business having to supply its own infrastructure.[78]

For smaller and informal enterprises, the failure of public infrastructure can have ruinous consequences, since such businesses do not have the resources to make alternative arrangements. GG Alcock comments: "I was speaking to a guy who ran a township bakery. He was doing 2,000 loaves of bread a day. That's a big operation. He told me he was closing down because of the power situation. Remember, we're no longer talking about load shedding, but load reduction. The grid has not been maintained or upgraded to deal with demand, so whole areas are now being shut down. You can't operate like that."[79]

In sum, the foundational conditions for investment, the "good enough governance", represents major hindrances to investment. PT notes that it is on these issues – crime, electricity and logistics – that business has focused its attempts to cooperate with the state. They are existential and resolving them promise outsized rewards. (These are also issues where ideology is likely less in evidence – at least since the principle of private participation and provisions has been conceded – and so offer the possibility of forward momentum.) For all those interviewed for this study, the infrastructural challenges are critical to the problems faced by the industries which they are familiar with. "We're importing maize from Argentina to Cape Town, because the state of the transport network makes that option more cost-effective than bringing it in from the Free State," WM comments. LM, an executive in organised mining, concurs, noting that failings in the rail system have had a serious impact on mineral exports, although given that various rail lines service particular mines (and therefore transport particular commodities) the impact is uneven. To take up shortfalls, trucking fleets have been used, although this is an expensive option, stresses the roads and is only economically viable when the price of the particular commodity is high – should it fall, so does the viability of the transport model.

Indeed, the inability to maintain the foundational facets of the economic environment speak to an effective "demodernisation" of the economy, the wearing away of its foundations and the circumscription of its prospects in higher value-adding activities.

Value-adders: "good governance"

To move an economy beyond factor-dependent activities, a more sophisticated economic environment is necessary. **Human capital** – a skilled and productive workforce – is the key ingredient of innovation, providing the basis to leverage new ideas into workable economic processes. Brain power is a more effective value multiplier than muscle power. For this reason, education is regarded virtually universally as a necessary service to be provided to a population's young people.

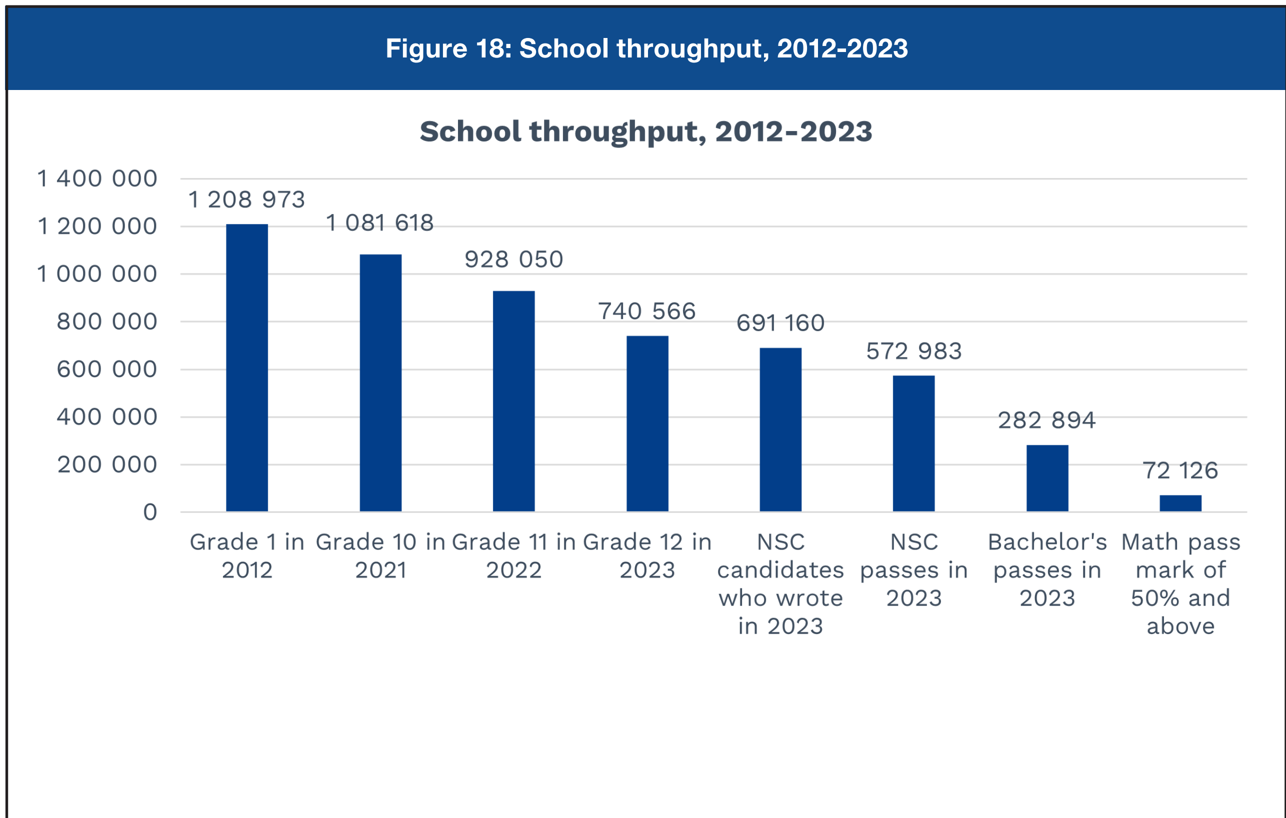
For partly ideological reasons, state policy has been reluctant to venture into low-wage employment as an economic strategy. AR, a banker whose interests cover multiple jurisdictions across the world, points out that this has differentiated South Africa from other emerging markets, such as Indonesia. South Africa seeks to bypass the lower rungs of the developmental ladder and ensure entry for millions of hitherto excluded people at its middle. This would assume a skills base – as one necessary condition – being available.

Indeed, the imperative of imparting skills to meet the demands of the economy and to prepare individuals for the sort of work that will provide them with opportunities for socio-economic mobility has been recognised for decades – long before the political transition. But equally, the deficient standard of preparation that many of South Africa's young people receive has long been a choke on development, even though it has been acknowledged,and declared a nominal priority, by successive governments. This is dealt with at length in the Generating Jobs and Skills for Prosperity and Growth, a recent IRR study.[80]

The state of education and skills development in South Africa bespeaks nothing short of a profound crisis. Two respected international benchmarking exercises, the Progress on International Reading Literacy Study (PIRLS) and the Trends in International Mathematics and Science Study (TIMMS), illustrate the magnitude of the problem: in the 2021 PIRLS study, 81% of Grade 4 pupils and 56% of Grade 6 pupils in South Africa could not read for meaning,[81] while just 41% of mathematics pupils and 36% of science pupils surveyed in the 2019 TIMSS study were proficient in basic skills and content.[82]

To understand this from a somewhat different perspective, consider the school throughput for the generation entering the education system (Grade 1) in 2012.

Figure 18: School throughput, 2012-2023

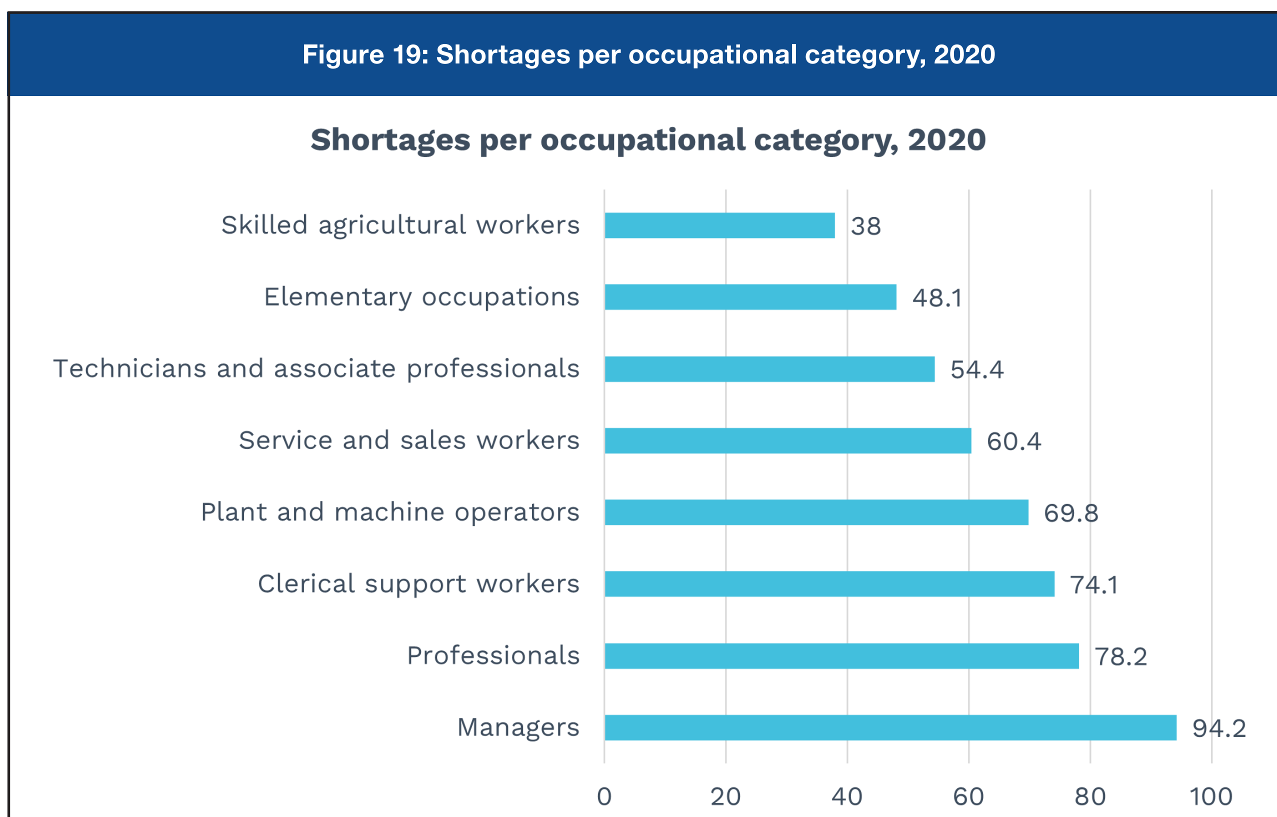


Source: Centre for Risk Analysis

Barely half of the cohort entering school would write the National Senior Certificate Exams in 2023, and well fewer than half of the Grade 1 entrants actually passed. Just under half of the passes enabled entry into a bachelor's degree programme – and the latter group represent less than a quarter of those who started this educational journey.

Only around a quarter of those who achieved a bachelor's pass did so with a 50% pass mark in maths – or only 6% of those who started Grade 1 in 2012. Maths opens the door to scientific and engineering fields, which are critical to an innovative modern economy; it is also closely correlated with finding a livelihood that supports a sustainable middle-class standard of living.

In South Africa's workforce, a 2022 study by the Labour Market Intelligence Partnership (LMIP) looked at occupational shortages. It used the Occupational Shortage Index – a composite measure of wage pressure, employment pressure, and talent pressure – to estimate skills shortages in South Africa. The Index is expressed in scores over a range of -100 (indicating a surplus) to +100 (indicating a shortage); 0 represents equilibrium for a given occupation. This is shown in the table below.

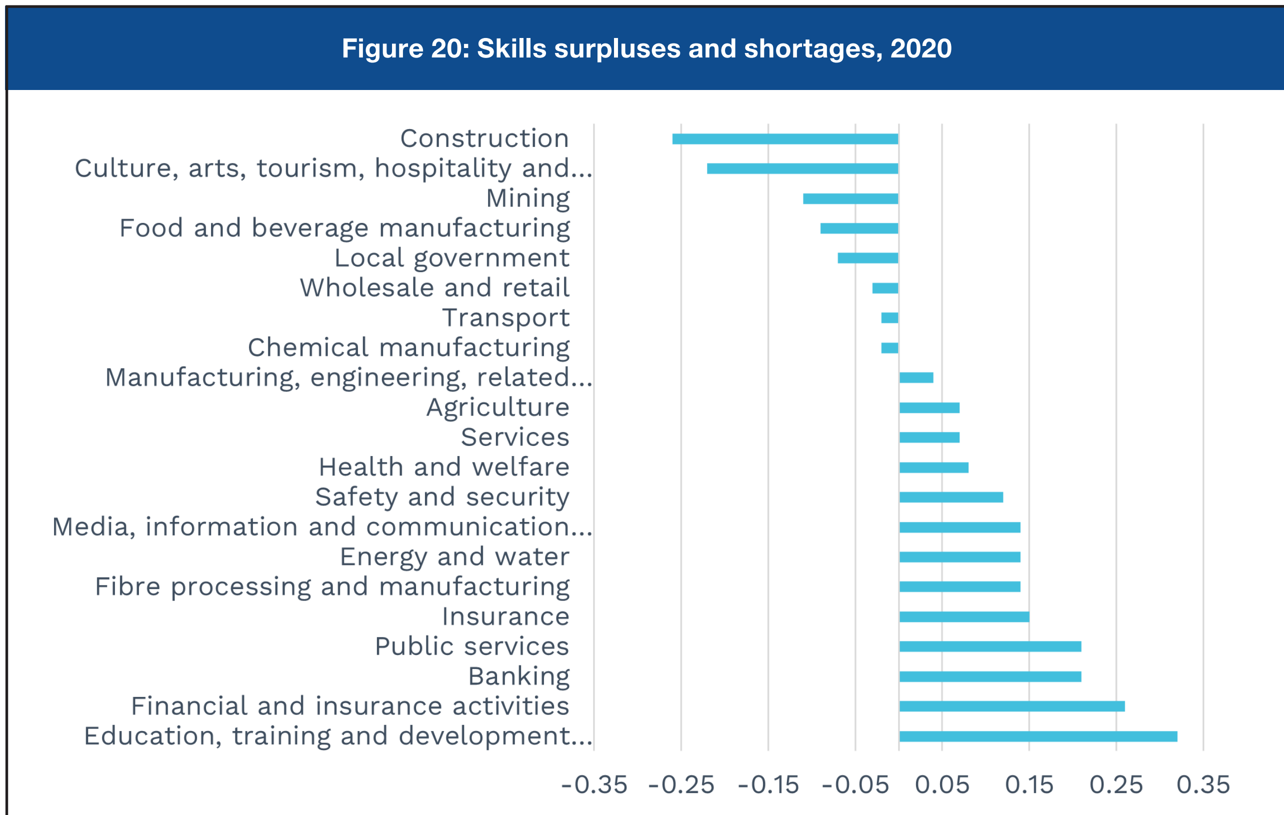


Source: Labour Market Intelligence Research Programme[83]

The findings revealed significant shortages in managerial and professional occupations, with rates of 94.2 and 78.2 respectively. This points to the considerable dearth in higher-end talent. But even in the capacity for mid-level tasks, extensive shortages existed. The score for clerical support workers was 74.1, for plant and machine operators was 69.8, and service and sales workers was 60.4.

LMIP further examined the scale of skills shortages, plotting the state of various sectors on a scale between -1 and 1, with lower scores representing a surplus, and higher scores a shortage.

Figure 20: Skills surpluses and shortages, 2020



Source: Labour Market Intelligence Research Programme[84]

It should also be noted that skills requirements evolve as industries develop. Where investment in new ventures lags, available expertise may disappear (through retirement or emigration) or become dated. LM sees this as a strategic issue for the mining industry. "We've been mining for over 150 years in South Africa. The industry has shed a lot of its skills and capacity, and some of what remains is now obsolete. This hits exploration, and it hits investment in new projects."

As is apparent, and as is noted in the report, it is in the higher reaches of the skills hierarchy that the shortages are most acute. It should be noted that it is in these areas – sophisticated service industries, high value-added manufacturing and so on – that other middle income countries are finding their opportunities. State policy also hopes to create opportunities here. But the struggle to find the necessary skills reduce the prospects for large-scale success. For example, the imperative of "greening" the economy is widely endorsed, and is a target for investment. Over R300 million is expected to be spent on green hydrogen, yet a study of the value chain noted extensive skills deficits in the scientific and artisanal skills that would be required to bring this to fruition.[85]

Commenting on the state of the skills environment, PT says: "While there are vocations listed that would not be out of place in most countries, there are others where it is clear that SA has a unique skills problem. For example, I'm not sure that many other countries would identify 'General Manager' as a scarce skill." He adds that South Africa's long-running approach to immigration policy (to which it seemed deeply hostile, or hopelessly incompetent) kept the country outside the global competition for skills, even where South Africa might have been an attractive destination. "Until recently, our immigration policy effectively prevented us from attracting foreign talent, hobbling our firms and economy. This counter-productive policy has been reversed, which hopefully bodes well."

A **regulatory environment** is intended to safeguard public wellbeing, pursuing what might loosely (and often controversially) be termed "the public good". South Africa has taken a regulation-heavy path, and one in which the benefits are doubtful and the capacity of the official systems to implement them is questionable to say the least. It is even more questionable whether the benefits they might offer compensate for the burdens they impose.

A useful bird's eye view of regulation was produced in 2004 by SBP (formerly known as the Small Business Project), which sought to measure the cost of regulations in South Africa. These it put at some R79bn or 6.5% of GDP.[86]

This can be explored and understood through the case study of small business, the promotion of which has been a nominal goal since at least the 1980s. The compliance burdens that official demands make have a disproportionate impact on smaller firms, forcing them to spend relatively larger amounts of time and resources dealing with what are effectively distracting, non-business activities, While this is two decades old, and no work on this scale appears to have been done subsequently, small business advocates have argued persuasively that the regulatory burden has not appreciably abated, and has remained a key hindrance to small firms, and the possibilities they envisaged for investment and expansion. (Note that this no peripheral issue, since small businesses are a major global engine of economic activity.)

SBP's later research – its SME Growth Index – found that small business owners perceived the business climate as difficult if not hostile, and that the regulatory burden was a significant factor inhibiting their growth (some of which was bound up with the state of municipal governance, discussed above).[87] This theme has been taken up by the Small Business Institute, which has decried both the scale of the regulatory burden, and the fact that it was written with large firms in mind[88] (this being an inevitable outgrowth of the institutional social partnership that state policy has tried to foster since the 1990s). Academic analyses have reached similar conclusions, with an article by Cecile Nieuwenhuizen noting:[89]

> The results of the primary research study confirmed [that] most businesses experience problems with regulations and compliance issues especially with regard to labour laws (HR and IR), SARS, tax-related issues and skills development. The businesses perceived regulations and compliance issues to be burdensome, both in terms of time and cost. The business owners also found that there was insufficient knowledge in their businesses to keep up with ever-changing regulations and to personally attend to all compliance issues.

Meanwhile, a complex regulatory environment has often been paired with indifferent enforcement. A regular refrain, as Nieuwenhuizen notes, relates to inefficiencies in the South African Revenue Service, despite its reputation as an organisation that functions well (or did until the State Capture era). This includes tardy refunds and a failure to issue clearance certificates expeditiously. In other words, the state is often not able to meet its own obligations, to the detriment of the country's economy. SBP captured this well in the title of a policy commentary: "A country over-regulated and under-governed".[90]

The state of municipal governance deserves a mention here. As noted above, this is intimately linked to infrastructural failure. The local municipal regulatory situation is often deleterious, especially for smaller businesses, and for informal businesses looking to expand and scale up. Alcock points to an official posture fixated on formalising business activity, with little regard for the impact on particular operations, as well as a rigid approach to zoning that makes it difficult for entrepreneurs to access desirable land.

Another area in which a heavy and counterproductive regulatory burden is evident is in the field of racial "transformation". This has been an ongoing theme across the economy that prompts intense acrimony as well as an element of pretence: given the sensitivities around these policies, and their centrality to the ANC's worldview, business often speaks about them without much sincerity.[91]

Racial regulation in the economy takes two basic forms. The first is in labour and employment matters, governed largely by the Employment Equity Act and the associated regulations, with a state commission to enforce it. In the broader business environment, it is meant to confirm to the overall B-BBEE policy ideal, which is overseen by the Broad-Based Black Economic Empowerment Act, and various other pieces of legislation, such as the Preferential Policy Framework Act, the latter having been repealed and replaced the new Public Procurement Act.

Government leaders, including President Ramaphosa, have repeatedly reiterated that the policy is non-negotiable. During the coronavirus pandemic, for example, he rejected suggestions that it might be an opportune moment to deregulate the economy and scrap these policies: "The Broad-Based Black Economic Empowerment policy thrust of this government, if anything, needs to be enhanced."[92]

The risks inherent in B-BBEE were clear from the beginning. Experience elsewhere had shown that preferential policies could be captured by elites, or would disproportionately benefit a small group of people placed to capitalise on them to the detriment of cost as a whole. Thus, as one 2007 study commented: "In discussing the benefits of BEE we included the social benefit of the avoidance of populism and noted that individual firms could not benefit from the whole extent to which they helped to provide a social benefit. In addition to social benefits however, there may be social costs of BEE. A clear one is that [Narrowly-Based] BEE via the forging of links between firms and politically connected people may lead to rent-seeking and the introduction of regulations and policies that favour existing incumbents. This can reduce market competition and innovation and it can also distort government policy. This may appear as benefits on firms' balance sheets because it increases profits, but it is obviously a cost for society and likely reduces economic growth."[93]

This is what has happened. The IRR has written extensively about the flaws in BEE and proposed alternatives based on socio-economic standing.[94]

Empowerment demands have been a particularly serious issue for the mining industry, with the Mining Charters – the broad frameworks setting out official aspirations for the industry, and demands on it – requiring extensive commitments by mining companies, including ceding equity.[95] LM remarks: "The Mining Charter has always been a tool the government could wield without considering the implications." He adds that even though there has been some indication from within the government that some of these demands (such as effective free carry equity for communities) might be revised, this has yet to be properly written into the regulatory architecture. His concerns are echoed by both KN and AR, a banker with global exposure, who speak about the damage that the Mining Charter and the demands for ceding ownership have done to the domestic industry – despite South Africa's pedigree as a mining destination, exploration has effectively dried up.

More directly, the Zondo Commission pointed to the abuse of preferential procurement provisions as a prime means of corrupt extraction during the State Capture period. The Commission's report pointed out that procurement could legitimately be used to advance empowerment goals, but that this needed to be done with due consideration for the prudent stewardship of public resources and the provision of public goods to society as a whole. [96]

> There are of course many cases, one hopes the vast majority, in which the award of the tender satisfies both objectives of the Constitution but undoubtedly there are other cases some of which may well be high-value tenders in which one or other of these two objectives must be preferred, and it is in such cases that the [current] legislation fails to give guidance.
>
> In the view of the Commission the failure to identify the primary intention of the Constitution is unhelpful and it has negative repercussions when this delicate and complex choice has to be made, by default, by the procuring official.
>
> Ultimately in the view of the Commission the primary national interest is best served when the government derives the maximum value-for-money in the procurement process and procurement officials should be so advised.

However, the newly introduced Public Procurement Act, widely hailed as a remedial measure against abuse, makes provision for "set-asides" which stand to fortify the procurement practices that were used to provide a veneer of respectability for State Capture in the first place. According to Treasury, the existing system of premiums was "too limited", raising the prospect that BEE spending will be ramped up. Treasury has declined to indicate just what the effective BEE premium is that is being funded through procurement spending (in other words, money paid for contracts as opposed to the possible costs if value-for-money was the only criterion). For this reason, IRR policy fellow Gabriel Crouse has warned that the new Act could herald State Capture 2.0.[97]

Recent amendments to the Employment Equity Act, meanwhile, seek to introduce effective quotas into the workforce, with crippling fines for failing to comply. The former minister of employment and labour, Thulas Nxesi expressed his department's intention to be "harsh" to enforce workplace transformation.[98] Concerns about the failure of workplaces to adequately "transform" have been expressed repeatedly by the Employment Equity Commission, but it is notable that the latter body seldom attempts to understand or explain this meaningfully. Given the absence of mature debate around it, a discourse has developed that attributes the failure to achieve greater representivity to active resistance if not outright racism.

Even assuming that these factors play some role, it's hard to discount the impact of education failing – as set out above – on differentiated career options across the economy and the generally dismal rate of economic growth that has afflicted the country. (The late Tito Mboweni, once noted as governor of the South African Reserve Bank that qualified black staff were frequently inclined to seek more lucrative opportunities after having been trained at the institution,[99] an inevitable consequence of being part of a limited pool of people for whom an intrinsic characteristic, race, had a premium.)

The Department of Employment and Labour has announced plans to employ some 18,000 inspectors to monitor compliance with labour legislation, particularly employment equity, and that there is no intention to step back from racial policy.[100]

If business has navigated these issues cautiously, there is a vocal community of concern about the economic damage it is inflicting. William Gumede, Associate Professor in the Public and Development Management Department at the Graduate School of Business Administration at Wits University, has argued that empowerment deals have transferred some R1 trillion. But this, he said, had been to the benefit of "a handful of politically connected politicians, trade unionists, and public servants." Far from expanding the economy, this "had crowded out genuine black entrepreneurs and killed the development of a mass entrepreneurial spirit in black society."[101]

In investment terms specifically, both European[102-103] -based organised business have raised concerns about the impact of BEE on their operations.

In a sharply worded analysis on the state of South Africa's economy, the Centre for Development and Enterprise commented:[104]

> There is no need here to review all the criticism of BBBEE, most of which revolves around the fact that empowerment has been too narrow and that it has been pursued at the expense of policies that would have led to more inclusion and less poverty. Our focus, instead, is on the impact of BBBEE on economic growth. There are, essentially, three ways in which BBBEE has impacted on South Africa's growth:
>
> - It has diverted resources and energy away from building businesses by both established business and emerging entrepreneurs;
> - It has generally raised the costs of doing business;
> - It has introduced new uncertainties that affect investment plans.

The theme of racial policy as a barrier to investment was reiterated by several of those who commented for this study. SDC says of his experience of rent-seeking behaviour by prospective partners (without value add for his operations), and the intrusive demands by officials monitoring employment equity: "They have no idea what happens inside a business, or the responsibilities that come with running one. At the end of the day, we employ dozens of local people at good wages – better than they could hope for anywhere else in this part of the country. We have to turn a profit, we have to maintain our productive standards, all of which is alien to them." He adds that regulatory failures across the board – added to the foundational problems – are contaminating the value chains in which he operates. This meant that he has now been compelled to look abroad not only for export opportunities, but for a production and marketing base. He now spends most of his time abroad, with his South African assets mostly maintained, though with no plans at present for major new investment.

This raises the question of **knowledge** – how government and other actors understand realities and bring their insights to bear in effective policy. This can be considered the integration systems of good governance. As noted earlier, it was a willingness to take experience and evidence and to change course accordingly that made economic progress possible in a number of peer countries.

South Africa has been resistant to doing this. A deeply ideological view of the world, and the imperatives of mollifying particular interests, has meant a dogged refusal to act on experience, even where it has been negative. Its stance on labour legislation, racial empowerment and mining policy are testimony to this (this has been explored above, and is dealt with again in the following section).

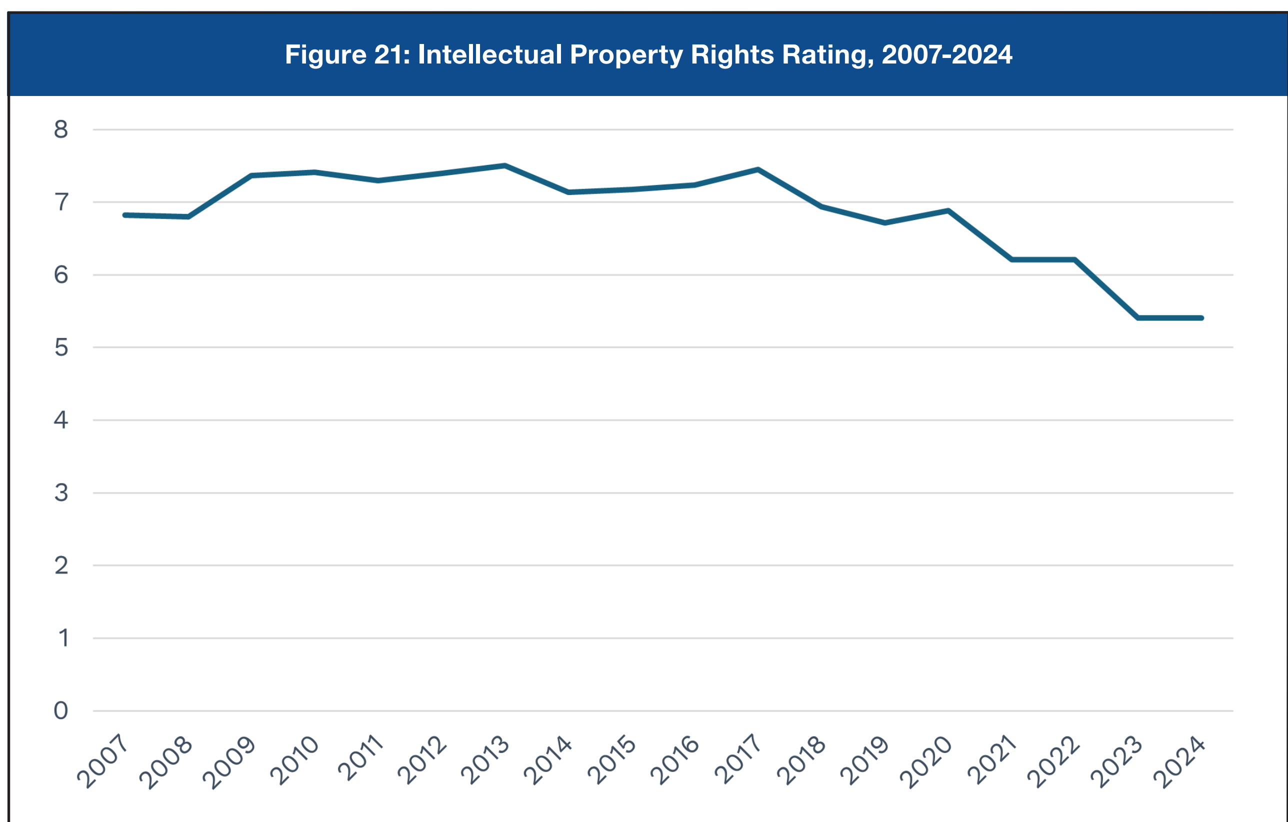
Key to the deployment of knowledge in an economic setting is understanding the difference between what is desirable and what is feasible. A common refrain is that South Africa has good policies but poor implementation, although that mistakes the fact that policy designed for an administrative apparatus that does not exist is not good policy. This is often lost in South Africa's authorities. Not only has there been a reluctance to learn from and adapt to evidence, but in such matters as the prioritisation of political control over managerial and technical capacity in the public service, choices have proceeded from a severely distorted view of priorities.

Thus, despite the intention to professionalise the public service, the ANC has not disavowed cadre deployment – and actively defended it prior to the 2024 election.[105] This has had far-reaching consequences in each of the foundational factors underwriting economic success, and has undermined the value-adders. Currently, the ANC – if not all its partners in the government – is committed to introducing a system of comprehensive state control of medical funding in the envisaged National Health Insurance. This is despite the implausibility of its successful implementation, and the consequences for the country's health-care system.[106]

Equally important is the capacity for problem solving. In broad terms, this reflects the research and innovation system, the protection of intellectual property and so on. Here, the picture is mixed. South Africa has some excellent research and development institutions, and high-quality scientific and commercial thinkers. Although many have decamped abroad, the nature of the global economy and communications system means that their expertise need not necessarily be irrevocably lost.

South Africa also performs respectably in terms of intellectual property protections.

Figure 21: Intellectual Property Rights Rating, 2007-2024



Source: International Property Rights Index[107]

As of 2024, South Africa's score regarding intellectual property was 5.404 against a scale or 0 (the weakest) to 10 (the strongest). This placed it 52nd of the 125 jurisdictions evaluated, and 3rd in the African region. Note, however, that over the past two decades it has declined notably. South Africa has (not uniquely) long experienced a tension between intellectual property protections and the presumed imperative of the state to override them in the public interest. The most prominent early instance of this concerned so-called parallel imports of medicines.[108] Recently, amendments to copyright legislation – passed by Parliament but not at this writing signed into law – have been criticised for permitting extensive latitude to disregard copyright provisions.[109] This accounts for the latter decline in South Africa's ratings.

Disappointingly, there have been instances in which expert advice has been wilfully disregarded. A current concern in South Africa is the state of its water infrastructure and consequent water supply. Yet precisely this issue was flagged by Prof Anthony Turton in 2008, probably South Africa's foremost water scientist, when he was affiliated with the Council for Scientific and Industrial Research (CSIR). Among his concerns was the state of the infrastructure and the declining availability of water expertise – and also the lack of engineering experience in many municipalities. In response, probably because of the awkward questions that this would have raised about the priorities of government, he was effectively forced out of the CSIR.[110]

The summary consequence of these trends is that South Africa has failed to foster the good governance that would make it a desirable investment destination that is hospitable and nurturing to higher value-adding activities. For WD, a European business journalist and long-time South Africa watcher, it is the failures of this part of the economic system that has been the greatest disincentive to value-adding businesses that might see possibilities in South Africa. "You can't operate in an environment where there is a constant need for checking," he says, "An efficient state is extremely important. When you load BEE demands and shifting regulations on top of dysfunctional municipalities and in infrastructure and officials who have no idea how business works, you have a set of extreme disincentives. European investors in particular, and also Asian investors increasingly, are used to a particular result-oriented mindset. They expect to deal with reliable officials who can perform their tasks and who don't expect backhanders. It's a mindset thing that helps the business environment to 'click' for them. As it happens, right now, this doesn't exist across most of South Africa. There is a lot of reliance on senior officials to wave things through – this is common across Africa – but that is only possible for large, connected firms. Smaller operators don't have the time or resources and will look elsewhere for their opportunities."

Drivers: "developmental governance"

It was noted earlier that the experience of the East Asian Developmental States exercised a powerful attraction to the ANC. This was the terrain in which political power could be leveraged for economic results and offered the possibility of importing political solutions (with which the ANC was very comfortable) into the economic sphere (which it failed properly to comprehend). It is in this sphere that Industrial Policy Action Plans, investment conferences and social compacting operates.

XA Global Trade Advisors' schematic groups two streams of activity here: prioritising sectors and picking champions. These are described as "Heartbreak Hotel".

In essence, these are interventions that act as multipliers for a business environment already in place. The basic premise has always been that the application of government power and resources could be a significant accelerator for the economy as well as an important mediator of the distribution of benefits. This has taken the moniker of the "developmental state" and latterly the "capable state".

It would, in other words, help to drive growth while ensuring development, in the sense of economic resilience and rising living standards. Developmental governance is unlikely with first being "good", or at least "good enough". Given the deficiencies outlined above, there is some irony that it's at this level that a great deal of public attention to economic policy takes place.

This background is essential to understanding the course that the business environment has taken. As Dr Neva Makgetla, economist at Trade and Industrial Policy Strategies, put it: "Industrial policy presumes a mixed economy, where government has to manage private actors to achieve socially desirable aims, not simply seek to replace them with government agencies. An effective industrial policy thus requires a functional paradigm for dealing with business, as well as capacity to understand and respond to domestic and global economic developments that lie outside government control."[111]

In broad terms, industrial policy has attempted to stimulate and support local value-addition. There is in fact a long history of doing this in South Africa: in common with many other countries, in the early part of the 20th Century it was geared at establishing domestic industries to service the local market, rather than relying on imported products. As the country found itself isolated internationally, these measures were important in dealing with embargos – as in the case of armaments, in which field South Africa became an exporter.

Following the political transition in 1994, South African industry was shaken by exposure to foreign competition. While industrial policy always had some role in economic thinking, it gained particular traction with the National Industrial Policy Framework, adopted by cabinet in 2007. The overall goal subsequently has been to try and claw back some of the ground that South Africa lost when its partly isolated economy re-entered the global mainstream: "reindustrialisation". Such industries are believed to offer better jobs and benefits (the "decent work" agenda that appeals to the ANC and to its trade union allies even more). As was pointed out earlier in this report, it is also through economies of this nature that the rapid rise of middle-income economies was built.

To drive this process, the government has employed a range of preferments to try and encourage selected business sectors, and particular participants within them.

The case of steel is illustrative. Steel is a foundational input for an industrial economy, and South African production has its roots in the early 20th Century. Indeed, this was a product of industrial policy for the young country. The South African Iron and Steel Industrial Corporation (Iscor) was established as a state-owned enterprise, although it was privatised after the erstwhile National Party government began to take on free market ideas in the 1980s.

But steel is a product that can be sourced from numerous producers globally, and South Africa's contribution is modest. Of the estimated 1.9 billion tonnes produced globally, South Africa produces 4.9 million, or around a quarter of 1%. The World Steel Association ranks South Africa at position 32.[112]

Government policy has been to preserve the existing industry from competition but also to expand the industry to new entrants. To assist new entrants, the Industrial Development Corporation has invested extensively in smaller steel mills (so-called "mini mills"). These reprocess scrap metal, and to supply them, regulations demand that recyclers offer the scrap at preferential prices – the Price Preference System – which are set below global rates. Only if there is no interest from this sector can scrap metal be exported, but then only with an export duty. Meanwhile, ArcelorMittal, the successor to Iscor and producer of some 50% of South Africa's steel was struggling to compete with Chinese steel imports. To deal with this, stiff tariffs were introduced to shield it from competition.

But with the subsidies paid to the mini mills, they were able to produce steel at prices that undercut even the Chinese imports. As Donald Mackay of XA Global Trade Advisors explains, this has created incentives to establish mini mills out of all proportion to the market need. "Why wouldn't you want to be in the mini mill business?" he asks.[113]

The funds that have been sunk into this are large and reflect the perverse incentives. The IDC's exposure to mini mills stands at some R14 billion – while the market capitalisation of ArcelorMittal is only R1.4 billion.[114] MacKay adds that two thirds of the value of the IDC's investments that are in business rescue are mini mills.

Moreover, MacKay argues that in attempting to push agendas in trade and business promotion, South African industrial policy has undermined the entire basis of efficient market operations. It is no longer merely a case that certain firms or sectors are beneficiaries of preference, but that the incentives have been skewed, so that a focus on competitiveness is giving way to one of rent seeking. It is increasingly difficult in some areas to determine what an accurate price should be. South Africa, he says, is becoming a "subsidy economy".

A key element of this is the effective capture of policy. In the steel industry, this has been pushed by a "working group" within the Steel Masterplan Committee. Their identities were kept secret until being revealed in litigation in 2021. (They were a mixture of state officials, businesspeople connected with mini mill sector and organised labour; representatives of the scrap metal industry were not included.) The working group has successfully ensured the longevity of the PPS measures, as well as an export ban on certain products. and even managed to bring products other than steel within the remit of the policy.[115]

For its part, the protection afforded ArcelorMittal has not resolved its challenges. Demand for its products is below what it would need to make its integrated operations (those producing steel from iron ore to precise specifications) viable, while the country's infrastructural deficiencies contribute to pushing up its costs further. Its largest plant, in Newcastle in KwaZulu-Natal, faces closure, with the loss of 3,500 jobs, and additional implications for the various operations along its value chain (the mines supplying the plant, and also the businesses relying on its products).[116]

For SDC, whose manufacturing processes rely on high-quality steel, the state of the steel market was the "final straw" that saw him looking to set up foreign operations. Steel tariffs introduced from 2015 largely at the behest of ArcelorMittal had ramped up the price of imported inputs, which coincided – in his observation – with a precipitous decline in the quality of locally produced products. He recounts having to send staff to inspect orders piece by piece to ensure that they were of satisfactory quality. The upshot is that the local value chain is increasingly unable to fulfil the requirements of his company. Indeed, other manufacturers have spoken out publicly in terms similar to SDC's.[117] Peter Bruce, a veteran journalist who has covered industrial policy in detail over the past few years, writes: "We are trying to re-industrialise to make and sell the things we are good at. The things we need to re-industrialise are often made better and cheaper elsewhere. So what? Let entrepreneurs import what they need. Then give them work and they'll fix this place."[118]

The overall outcome is that one part of the value chain is effectively subsidising the inefficiencies of another, with state patronage. A range of participants have lost out. These include the lowliest "pickers", through to scrap merchants and downstream industries. With supreme irony, the latter includes manufacturers whose contributions represent genuine, market-capable activities. ArcelorMittal has benefited to an extent, although not enough to provide an enduring solution – it is in any event now invested offshore, and its South African assets may not be of great importance to it. The mini mills have individually gained, and to the extent that they have been able to supply clients with cost-effective products, the latter have gained too. But all indications are that this is a highly inefficient commitment of resources that is playing a distortionate rather than a developmental role.

Similar themes have been noted in other areas of the economy. Measures to protect the domestic chicken industry have had adverse consequences for consumers, particularly low-income households for whom chicken is a primary protein.[119] The possibility of the innovative Starlink satellite internet system being introduced into South Africa – broadband access being another perennial weakness in the business environment – has been held up by demands that it would need to comply with empowerment criteria.[120] State policy is committed to fostering "black industrialists", but as PT observes, there is virtually no transparency around where specifically the resources are directed, nor are there public assessments of the initiative's efficacy.

Chris Hattingh, director of the Centre for Risk Analysis, remarks:

> When industrial policy, in the form of tariffs and subsidies, is not targeted, timed, and consistently assessed against objective, transparent, measurable criteria, the incentives are such that some businesses continually benefit (even when they do not perform), others with potential never receive any assistance, and whole industries and sectors of the economy are insulated from the market signals (domestically and globally) they need to adapt their operations, improve their products and services, and over time add to the complexity and value-add of the economy as a whole.
>
> For South Africa, when one looks at the track record of industrial policy in sectors such as automotive, steel, and poultry, there is no doubt that jobs have been created and companies have been assisted by the government. Whether those subsidies could have been better targeted is a legitimate question, as well as highlighting that should basic government service delivery in areas such as electricity, logistics, and crime prevention have been adequately administered many existing companies would not have needed additional forms of state support to paper over the costs imposed by failures in these areas. Additionally, it will likely never be known exactly how many new market entrants were prevented from ever coming into existence because the costs were too prohibitive, and vested interests were able to secure state support for themselves.

In addition, initiatives such as EWC drive, suggestions for prescribed assets to fund mismanaged state-owned enterprises, and the pending introduction of the National Health Insurance – the latter an uncosted mega project with profound implications for every South African and for the economy, and in respect of which input from business has largely been disregarded – all point to the enduring nature of this approach. When confronted with concerns from European investors about empowerment and localisation demands (the latter are addressed above) former Minister of Trade and Industry Dr Rob Davies replied: "Localisation is not something we will be able to renounce. Nor are we going to be able to renounce BEE."[121] The reality behind these comments is a refusal to contemplate change. "It's in the DNA," comments EH.

WD points to the reliance on investment conferences and measures to attract business from abroad. The thinking is that by showcasing some of the country's advantages, making a pitch to businesspeople and explaining the rationale behind investment-hostile policies, along with some personal bonding, will produce investment. This assumes that an argument can overcome the hard realities of doing business in the country. This is, he says, "nonsense". KN comments on the same theme that even if South Africa's policies could be justified as the government hopes, this does not alter their impact on business – "just look at the results".

All of the above raises a serious conceptual issue for South Africa's aspirations (or pretentions) to be a developmental state: the relationship between the state and business. A productive relationship between business and the government can be a useful developmental asset, helping each party to understand the other and to find points of mutual interest and vulnerability. This allows them to recognise the inevitable tensions in their relationship, but to act in a manner that is of benefit to both – and if the state has a suitably developmental orientation, the action can be structured to serve the interests of society as a whole.

In a 2016 contribution, the late Michael Spicer described relations between the state and business as having been inherently strained by completely different worldviews, by strong anti-business sentiment by some within the ANC, and then by the collapse into patronage that attended the Zuma years. The state was happy to play divide-and-rule with business (by effectively extending patronage to a racially exclusive breakaway organisation, many of whose members were actually public servants and not businesspeople), and was increasingly disinterested in policy. Business, for its part, was generally prepared to play along without conviction.[122]

As the case study of the steel industry suggests, what has emerged is a collusive relationship between the state and particular business interests, as well as politically connected insiders and rent-seekers. The intersection between politics and money has been central to many of the scandals that have rocked the country and undermined the state.[123] B-BBEE has been a key enabler of corruption.[124]

AJ, an economist and investment analyst, describes this as one of the most serious shortcomings afflicting South Africa's economy. "The simple fact is that the relationship from the ANC's side was driven by ideology. A market economy versus a control economy, and they couldn't get beyond the idea that the market was all about profits and that there was a need for the government to take care of society. If government and business had been able to find each, the potential for a different path would have been massive. Massive. I wouldn't know how to quantify it. A productive relationship would have meant more rational regulations and a better investment environment, more private investment and the resources for more public investment. It's a tantalising case of what could have been. But the reality is that relationship became extremely polemical and government has been extremely suspicious of anything to do with the private sector."

The reality is that the government simply lacks this expertise, and confronts a complex system with deep structural problems. Hence the term "Heartbreak Hotel". Lofty aspirations are crippled by the implausibility of the conditions in which they are being implemented and by the conflicting objectives and inabilities of those who hold them – or indeed, where policy is designed so as to be inimical to business activity. For SDC, this is a frustrating reality. "You can do something about individual problems. Security, infrastructure, all of that. You just can't do much when policy is deliberately arranged to act as a truncheon against you."

Opening South Africa for investment

How could South Africa be pivoted from the realities described above to one in which investment is coming in with growing momentum, and driving up the growth rate to the 5%-plus that the country direly needs?

This begins with accepting some key premises.

- Investment is necessary, from the public sector and the private sector, in large amounts and in modest amounts;
- Investment will be attracted to an environment in which there are reasonable and realisable prospects for returns;
- South Africa is at present not a particularly attractive option for investors;
- Not everything can be achieved at once, making prioritisation the key; and
- There is no substitute for evidence in policy making, and this applies without qualification to attracting investment.

At present, AR sums up the frustration felt by many investors – from South Africa and abroad – with the state of the country and the difficulties of operating in it: “It’s a pain-in-the-ass place to do business, with champagne tastes and a beer budget.”

Yet it is important to state that South Africa’s manifold challenges should not overshadow some of its underlying strengths.

MG, a consultant based in the United States, points out that South Africa remains Africa’s most sophisticated economy. Its financial and corporate sectors are well developed, and fairly well managed. It has enormous mineral wealth, and a long-standing mining economy. While accounting for a small share of its overall GDP, its agricultural sector remains productive and resilient. Its manufacturing sector is sizeable, though struggling to remain globally competitive.

Cultural factors, such as the widespread use of English, and long-established relations with markets in Europe and America (and increasingly in Asia), make it a simpler environment for foreign businesspeople to operate in than those of some of its peers. Demographically, South Africa is at a point where its labour force comprises some two thirds of the population. This means its dependency ratio – the economically productive in relation to those out of the workforce – is positioned for accelerated economic growth.

MG comments: “Labour costs are making a lot of activities in Europe and America uncompetitive. The same thing is happening in Asia, even in China – we’ve seen countries like Vietnam benefiting from this. But even in those late industrialisers, this is becoming an issue. South Africa is sitting on a high-growth continent, and has a workforce that has a skills base that is not available everywhere else. Investors should be salivating about the possibilities.”

WD concurs. South Africa, he says, offers an excellent quality of life for foreign businesspeople, and cultural affinities with the Western world that would count for a great deal. “Investment is often influenced by soft factors – language, residential options, good weather, the availability of quality education and health care, the existence of expatriate communities, connections to home countries. South Africa has these to offer European businesspeople. It’s a far easier place to settle in than Vietnam or China. It wouldn’t take much to capitalise on these advantages, if strong economic foundations could be established.”

Indeed, on the latter point, while Africa suffers from a litany of its own problems and shortcomings, there are enormous opportunities for South African firms, which a properly actualised African Continental Free Trade Area would unlock.

Of critical importance, South Africa's institutions – often abused – have remained functional. Despite enormous socio-economic stress, its democracy has endured, and its legal system is respected.

In addition to this, Alcock points to the enormous potential of the country's informal sector and its "township economy". This, he emphasises, is far larger than is commonly supposed, and far more dynamic than is commonly accepted. He expresses frustration at hearing from policy makers that entrepreneurs need to be enticed into South Africa's townships – ignoring the vibrant entrepreneurial culture that already exists. "We have systems that actually work," he says, "the challenge is to stimulate them, make them more efficient, help them to contribute to the tax base."

These are factors that can be leveraged, if a properly pro-investment policy and governance agenda is to be carried out.

Get governance in order

The Harvard Growth Lab's contention about the economic implications of poor state capacity is supported and illustrated by the material presented in this study. The basis of South Africa's recovery will be addressing this, and without doing so robustly, there is no realistic possibility to lifting South Africa out of the current low-investment path.

Regardless of any ideological predisposition, a country like South Africa needs a functioning state. This demands a commitment to and operationalisation of three broad principles for policy and government action.

- The first principle is realism: what can reasonably be achieved at any time with the extant advantages and challenges. South Africa is not a developmental state, and to attempt to structure growth around industrial policy or state guidance will only compound the malaise.
- The second principle is a focus on outcomes: policy and action must be geared to achieving particular, defined goals. This demands that competing objectives be ordered and prioritised. Not everything is possible (or indeed desirable) and it is critical to decide where the greatest benefits are to be had, where resources are to be committed, and how different policy options will fit together.
- The third principle is merit: South Africa's governance environment has been strained by what the National Planning Commission termed a "rejection of meritocracy". The overt politicisation of the public service, as well as a drive for demographic representativity as an overriding (official) priority have undermined this and contributed to widespread incapacity. Where merit – skills, qualifications, experience, and so on – is relegated to a secondary place in governance thinking, efficacy will invariably suffer, and pathologies will be enabled, sometimes unwittingly, sometimes deliberately.

A state committed to fostering an environment conducive to investment is one that would provide stable, predictable governance, and be able reliably to provide the foundations of societal activity. This is particularly the case at local government level, which is where responsibility for the management of most day-to-day interactions between citizens and the state resides.

As the IRR has argued in a recent paper on public service reform, this requires changing the manner in which the public service is run, both in its organisational conception and in its general management. These would include an enhanced role for the Public Service Commission, dispensing with demographic considerations in recruitment and promotion, requiring managers to lead and maintain discipline among their subordinates, and ultimately developing a distinct, non-partisan organisational culture.

This is of course a long-term project, but quick wins are possible – if only by signalling that changes are afoot – provided they are politically supported.

Rebuild and fortify South Africa's economic foundations

The two foundational enablers of economic activity – safety and security, and infrastructure – are in some ways South Africa's most important encumbrances. Each arises from profound governance failings and will take time and concerted effort to deal with.

In the security field, the country suffers from deficient professionalism in its policing and prosecutorial (and to an extent, its judicial) processes, as well as its correctional systems. Perhaps more than anything, rewards for criminal activity are not countered by the risk of suffering their consequences. There is cold rationality at work here.

The solution to this is complex and will require changes to institutional staffing and management – similar to what is set out regarding the public service, above. One innovation would be decentralised police management, to link policing more closely with the communities that individual stations serve. Recruitment and career progression must reflect a steadfast commitment to merit. And rooting our corruption in the security systems must be a priority: nothing undermines security more fatally than compromised agencies meant to ensure it.

Specifically, better investigative and forensic capabilities, as well as dedicated teams for investigating and prosecuting organised crime would be needed to deal with the growing hold of organised crime.

Infrastructure needs funding. Substantial sums could be found in using the existing resources better. This can be supplemented by borrowing and issuing bonds. But increased input from the private sector is critical: in the rehabilitation, maintenance and operation of existing assets, as well as the construction of new ones.

There is a long history of resistance to this, although recently the government has begun to see the imperative of doing so. The rollout of solar power is an example of what is possible in this regard. And, given the need for infrastructural investment, capital should be welcome from abroad.

Progress is also being made in respect of logistics. This owes much to the involvement of the private sector. "The scale of the challenge," says LM, "gave the private sector the legitimacy to propose certain interventions with their specific expertise. The private sector initiated this, and frankly, the state was not in a fiscal state to take on this responsibility itself." This arose as a crisis response, but shows the possible wins of a cooperative approach.

A particular mention must be made of digital technology. This is now indispensable to a modern economy, and access needs to be expanded. The idea that something like the Starlink system might be excluded from South Africa because of empowerment demands is self-defeating in the extreme. It is also important that the reality of a substantively post-cash economy be realised. The possibilities in the use of electronic devices for payment in the informal sector need to be encouraged; something that demands inputs from both government and financial institutions.

Of course, sorting out the infrastructure will be impossible if projects intended to do this are also attempting to deal with subsidiary issues. Using road building or the refurbishment of power stations to advance race-based empowerment will likely open the door to extraction – a good part of what produced the crisis in the first place.

Importantly, successfully tackling infrastructure will rest on effective law enforcement. The plundering and vandalism of the country's infrastructure, in all its forms, calls for proper protection of its assets, and combating the syndicates that profit from undermining it.

With some progress to show on these issues, key hindrances to investment would be removed, or at least mitigated.

Enhance the stock and pipelines of human capital

South Africa's economy requires a level of expertise that it is struggling to meet. If it hopes to advance along the value chain and make a compelling argument for higher-end activities, it will need to up the skills of its workforce. The education and training sector is in a dire state, and simply not fit for purpose. This is despite reasonable levels of spending.

It is unlikely in the extreme that simply funnelling more resources into a failing system will be of much effect, at least not unless issues relating to professionalism and leadership are resolved.

Getting this right demands taking on aggressive entrenched interests, particularly the South African Democratic Teachers' Union, which has effectively taken charge of large parts of the country's education landscape and contested most efforts at accountability or to improve the standards of schooling.

The IRR has proposed expanding choice in education through a voucher system.[125] This would enable families to choose better- performing options for their children and offer a way out of dysfunctional schools. Teaching would not be able to function as a sort of sheltered employment, but a competitive one where outcomes are measured and valued.

This will not be an easy process, or one with quick wins, but it is one that could in principle be achieved without significantly greater outlays: it would function on the basis of redirecting existing resources, rather than requiring more.

Training for workplace skills, meanwhile, needs a new approach – or rather, perhaps, to revitalise an old one. Greater use of vocational and technical training at school level is one approach; the use of a greatly expanded apprenticeship system is another. At a minimum, it is the private sector that should take the lead here. As Brian Pottinger commented in The Mbeki Legacy, the academics and bureaucrats have had their chance and failed at it.[126]

Finally, South Africa needs to join the worldwide competition for skills. As PT notes: "Skills don't have to be autochthonous: in fact, all countries compete for global talent. Until recently, our immigration policy effectively prevented us from attracting foreign talent, hobbling our firms and economy." Reforms to this to make immigration easier – long discussed, but having gathered momentum under Minister Leon Schreiber – need to be pursued. South Africa's offerings to mobile foreign investors and professionals, often able to conduct their business in other markets, are limited, but an inefficient and parsimonious bureaucratic system should not undermine those that the country has.

Reform the policy and regulatory environment

A highly regulated environment need not be a barrier to investment, provided the regulations serve a rational purpose – one that enhances the environment for investment – and provided that it is competently overseen. This is transparently not the case in South Africa.

South Africa needs to conduct a thorough review of its policy and regulatory environment, and sher demands on business down to what is necessary to protect clear and legitimate public interests. Environmental protection, for example, is a reasonable ground (as long as it can be properly and expeditiously enforced – which is only possible with a skilled inspectorate), but there is a strong case to be made against a raft of labour and "empowerment" regulation.

Thus, a productive and investment-capacitating regulatory environment would be structured around:

- **Prioritising regulation** that is strictly necessary, for example, in relation to monitoring and protecting South Africa's scarce water resources, and deregulating where possible;
- Ensuring that wherever regulations are imposed they can, as a matter of practicality, be **implemented efficiently** and that necessary permissions can be processed and issued expeditiously to firms meeting regulatory requirements;
- **Recognising that B-BBEE has failed** and should be abolished in its current form. While it has benefited a small cadre of people – not infrequently those with political cache rather that business acumen – it has added to the costs and complexities of doing business. Demands that equity or equity equivalents be surrendered as a condition for operating fully in the South African economy is wholly counter-productive. The IRR has proposed an alternative approach, Economic Empowerment for the Disadvantaged, which would incentivise investment and promote enhancing the living standards of the country's poorest people;[127]
- **Reorienting policy on the informal sector**, to enable it to thrive and maximise its contribution to the economy. This means understanding it on its own terms and recognising that it is a multifaceted phenomenon. The informal economy comprises both survivalist activities as well as scalable, profit-oriented operations. The former are a necessary part of the system providing livelihoods, and many engaged in these activities would be open to stable, wage-based employment. The latter present a real opportunity for investment and growth. They could benefit from targeted support for premises, access to capital and integration into corporate value chains (some of which is already happening).

For Alcock, this is encapsulated in the idea of hybridity, accepting that multiple solutions are necessary for multiple areas of the economy; different types of enterprises demand different levels of regulation, for example. This would demand policy makers and public servants with sufficient understanding of the informal economy – and the associated ideological flexibility – to design and implement suitable policy solutions;

- **Reforming labour legislation.** Business activity in South Africa is weighed down by agreements negotiated between large firms, organised labour, and the government. This is invariably to the exclusion – and to the detriment of the interests – of those not party to such bargaining: unemployed people, the unskilled, small businesses, and so on. FC, a business investor and public analyst remarks that the regulation of the labour market is misaligned with the skills available. This has in particular been a disincentive to labour intensive investment, and has compounded the unemployment crisis. This system needs to be abolished, and either limited strictly to those who actively participate in it, or who choose to be covered by it, or replaced by the principle of free association and competition;
- **Providing stability and certainty for investors.** Threats to property rights or the dilution of the value of assets – as in the campaign waged for EWC, or in the demands made through industry charters – must be done away with. They signal that investments are not secure, and "radical" changes to policy are a real future possibility. This remains a permanent damper on investment,[128] and
- **Ensuring that each regulation and piece of legislation is properly vetted.** South Africa should require assessments to probe impacts of such measures on growth and investment. While a variant of this exists (the so-called Socio-Economic Impact Assessment), these are often pro forma exercises intended to legitimate rather than to interrogate a proposal. If the country is serious about investment, this needs to be done properly. It also speaks to the need for capacity in the state: people able to apply their minds to the consequences of policy, rather than its political utility or its alignment to ideology.

LM notes that it is not only the nature of policy and regulation, but the manner in which it is implemented. He points to the various permissions that are required for mining projects, often dealing with substantively similar issues, though processed by multiple authorities. "They act in tandem with one another, not alongside one another. We need a 'one-stop shop' that can get applications processed quickly to reduce the time between conceptualising a project and starting extraction. At the moment, the times involved are a significant disincentive."

KN argues that the present policy environment is too hostile to facilitate a business revival. However, he sounds a note of optimism: "Anything can be turned around if the problem was caused by people in the first place. This needs strong, able leadership and big, decisive choices – don't tinker with policy, catapult it!"

Reset the government-business relationship

The adversarial approach towards business that dominates much thinking within the state has played a central role in degrading thinking and debate around the role that business can and should play in South Africa's development. This, unfortunately, follows from the ANC's ideological worldview, and has been consolidated by the extent to which patronage, rent-seeking and corruption has grown.

Here, a mindset shift is critical. For the ANC, it will mean stepping away from some of what has made it the organisation that it is; many of its leading lights will not be able to do this. But it is a necessary part of the modernisation process that is essential to South Africa's progress.

For business, too, some reorientation is in order. Large firms have tended to dominate organised business and to participate in setting up an economic management system that has worked against smaller operators. There has also been a degree of timidity when confronted with destructive policy and governance choices. This has meant that business has been complicit in fostering environments which it does not regard as optimal for investment. It has also deprived reformers in the state of critical support: former finance minister and head of the National Planning Commission Trevor Manuel once memorably described business as "cowards" for failing adequately to contest union demands. "If we're going to have cowards in business, we're not going to get very far either. You must have that counterweight if you want that progress," he said in a debate in 2009.[129] The same logic applies to relationship between business and the state.

One area where business might fruitfully invest some effort is in resuscitating the local-level business chamber movement. Since much of South Africa's failures are most acutely visible in its municipalities, a strong voice for business is critical. Given the dysfunctionality of much of the municipal sphere, though, business would need to go beyond attempting to interact with the municipal leadership. Rather, business would need to explore creative options for partnerships with interlocutors in civil society and at other levels of government.

Business is hardly without influence, and nor would the positions it might take with regard to policy positions necessarily be unpopular. This was suggested by the evident blowback that followed President Ramaphosa's signing of the NHI Bill into law[130] If a productive relationship is not possible, business should be frankly transactional in its approach.

Concluding thoughts

In 1998, an opinion piece was published in The Wall Street Journal calling attention to the economic challenges that the newly democratised country was facing, and the stakes for failing to do so prudently. Pointing to crime, labour costs, the ideological bent of government and lingering political risk, it stated: "South Africa has the biggest need for external capital and the lowest potential for attracting it of any emerging market." It went on to warn ominously: "Unless it starts delivering increased prosperity soon and thus the hope for a better life, it is not only the economy that will break down, but the country itself."[131]

It is worth noting an observation made by Hirsch in 2005: "The bottom line for government is that there are two key driving strategies. The first is to ensure that the medium- to long-term cost structure of the economy improves. Regulation and competition are important, and so are public investment strategies. The second key strategy is to ensure that, at least for a selected set of industrial and service sectors, the private and public actors agree on long-term strategies, and work together to achieve them."[132]

This is not how things have transpired.

Somewhat ironically, a significant element of policy debate around economic matters revolves around specific government interventions intended (at least in theory) to drive particular outcomes – the long-term strategies. This essentially establishes the basis for the regulation described.

It is the terrain of development plans, industrial policy, charters, investment roadshows and the like. The operating assumption is that judicious application of state authority will serve as an economic accelerant. Not only can the state be a catalyst in pushing growth and development forward, but it can be decisive for the nature of that growth.

This absolutely mistakes the nature of the economic challenges and the consequent lack of investment. The cost-structure of the economy is unattractive.

The immediate emphasis must be on the foundations of the stagnant economy. Getting the basics working efficiently is imperative; this will also take time to achieve. But even a demonstration that these matters are seriously and credibly being addressed could spark confidence in the country's future and its attractiveness for investment.

AJ argues that this is the basis on which investment can be ignited. "Essentially, just get a move on with the investments that the government claims to have in the pipeline, and which the country needs. What we are seeing is a lot of intention, but that things don't come to fruition. Upgrading the electricity grid would put around R400 billion into the economy over time. Recapitalise the rail and road networks. The water supply system needs to be fixed. The knock-on effects of all this could be huge."

This would, of course, need to be paired with the reorientation of South Africa's administrative apparatus to govern effectively, as well as its education and health services to provide the services they are mandated to – and which are critical to fostering a competitive workforce. There are islands of excellence that can be encouraged and nurtured, but the grandiose visions that so exercise the official mind are beyond current capacities and must be abandoned.

Indeed, South Africa's state has been set up – in effect if not explicitly in intent – as a burden on business and investment.

As Alma Kanani and Marco Larizza, a pair of World Bank economists, put it: "Institutions are as good as the capacity of the State that upholds them. Institutions are embedded in a country's social context, which affects the way they function as well as their effect on economic outcomes."[133] In South Africa, the state is inefficient and beholden to select elites and vested interests. The commitment to "empowerment" has meant that economic progress has been held hostage to the interests of a small community of politically connected businesspeople; alliances with trade unions have protected restrictive labour legislation, and also served to drive protectionism. Economic efficiencies and a competitive investment environment are compromised.

The American sociologist Peter Evans in his seminal study of developmental states, Embedded Autonomy, discussed at length how properly capacitated states, whose officials are linked to the economic interests but independent of them, have been able to drive high-end developmental endeavours.[134]

With this in mind, it is past time to rethink policy: labour legislation and empowerment demands as well as industrial policy.

Part of this is simply to step back and recognise that there is a fundamental difference between accepting that industrial policy can be a useful mechanism for growth and investment and believing that the South African state is in a position to achieve this. The interventions that have been introduced need to be reassessed, and scaled down, if not abandoned. In the short term, independent expertise (possibly from abroad) could be contracted to help design a better approach.

Fortunately, there are signs that this may be happening, though quietly and on a limited scale. AJ notes that there has recently been a large turnover of managers at Eskom to account for merit. Eskom was at one point an easy target for racial preferencing, but the realities of the power crisis and keeping the supply intact has compelled a rethink. "If we get this right, and create a meritocratic environment, the skills can be found, and things can be turned around." He adds: "There are a lot of retired engineers who would be happy to come back and contribute."

It is also worth noting that the ANC has compounded the suite of failures illustrated in this analysis by repeatedly threatening a turn to destructive policy positions: obvious examples of this being the "debate" around nationalisation of South Africa's mining industry and latterly the introduction of EWC to drive land reform.

These have been advanced within a narrative of "radicalism" and framed as initiatives of redress. In practical terms, they have served only to unsettle the policy environment, and to suggest its imminent deterioration. This has aggravated policy uncertainty sufficiently to make planning difficult, while introducing prospective certainty that future policy would be negative. Millenarian policy prescriptions like EWC are disastrous and should be disavowed. Whatever satisfaction ideologues may find in these ideas, they have imposed costs on society.

The misaligned politics and governance in South Africa needs to change. The current path has brought the country to its current malaise. And while the state can, conceptually, play a useful role in encouraging investment, the extant circumstances call for a new approach. Market analyst Peter Attard Montalto has observed a belief on the part of South Africa's leadership that by persuasion and cajoling and by "counting" projects, investment and growth can be willed into being: "There [is] a strange belief evident in the countability of individual investments: if you just have more individual commitments from individual companies with rand amounts attached, and more hands on which to count them, you will be fine. In this conception, because a certain company is investing in this industry and another in another industry it's a sign of life in each industry. Never mind if a handful of other investors have turned down opportunities or become frustrated and put plans on ice."[135]

"Capital goes where it's welcome and stays where it's well-treated". So wrote the late Walter Wriston, CEO of Citigroup. These are words that would be well heeded in South Africa. The country needs a new path, a new approach and a new stream of imagination. Investment will come where the environment for it is propitious. All of this comes down to understanding things in an appropriate order of priority: what must be done and what might be done; what is possible within available capabilities, and what is implausible. A failure to do so has inflicted great damage on South Africa.

Endnotes

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