A layperson's guide to Nene's budget statement

By **Ben Turok**

Minister of Finance Nhlanhla Nene caused quite a stir on 22 October when he presented the Medium Term Budget Policy Statement to parliament. Even though it was not an actual budget speech (with commitments on taxes, for example), it was nevertheless a very important statement.

Unfortunately, it takes a lot of effort to get behind the jargon used by ministers of finance – like "fiscal consolidation" and "quantitative easing", when they simply mean balancing the budget and increasing the amount of money. Similarly, the "current account deficit" mainly means that we are spending more on imports than we earn from exports.

The key indicator of our economy's health is its growth rate, which is now only 1.4 percent. This actually reduces to near zero when you add the population growth rate of about 1.5 percent. So, let us accept the reality that growth is close to zero. Our economy has stalled.

Other countries which are growing at a higher rate, like the rest of Africa, are able to increase taxes to raise more money. If this is spent wisely on productive activity or infrastructure, then there is a return on investment, which can then be reinvested for further growth. Or a part can be used for social services and welfare, thereby improving the lives and capabilities of the people.

Why is our economy stagnant?

Government blames the fact that world markets for our goods have shrunk, due to the global recession in Europe and the US, and the slowdown in China. But some economists hold that this accounts for only a third of our lower growth. If so, then domestic problems are the main reason for stagnation.

Another sign of our economy's stagnation is that the increases in government spending that have been used since 2008 to counter the recession have not stimulated our economy.

Instead, we have some very worrying figures: the budget deficit is 4.1 percent of GDP, the trade deficit is 5.5 percent. With our domestic debt at 48 percent of GDP, over 10 percent of the total tax revenue will need to be spent on debt service costs – a very large sum.

The US and the UK have debt of over 100 percent. Japan's debt is over 200 percent. Many other countries have higher debt than South Africa without talk of crisis – but their interest rates are less than 1 percent. Ours is 4.5 percent. This means that our debt escalates very fast. Also we borrowed a great deal after the 2008 recession and will have to repay about R194 billion in the next few years. That will really be a crisis. Why don't we reduce our interest rate? It is because our high interest rates attract the foreign capital inflows we need to pay for imports and local investment.

Minister Nene says that he will not reduce spending on infrastructure or on social services and welfare. His cuts will be elsewhere. This is in line with the current IMF position in Europe and elsewhere that advocates infrastructure spending in order to escape from stagnation. Will it work in South Africa?

There are grounds for scepticism

The problem is that our real economy – the sectors that produce goods and services – has been in decline for decades. We de-industrialised in 1995, in the name of "opening up" to the global economy. In 1994, manufacturing was 21 percent of GDP; now it is 11 percent. Cuts in government capital spending also retarded growth.

For the last 20 years, national government investment has averaged 0.5 percent of GDP. The resultant loss of jobs led to the falling purchasing power of the population and hence a slowdown in local manufacturing. There has been a downward spiral ever since.

No one knows how we are going to recover from that, and Minister Nene has no answer.

The fact is that our economy is not working well. The state-owned corporations are not providing services at prices that help industry. Electricity is expensive, freight and port charges are very high, red tape is killing enterprise, and corruption is eating up between R20 billion and R100 billion.

We need a totally new approach to economic development: a joined-up government and a joined-up economy, where state institutions complement the private sector in a mixed economy.

We need to recognise that the global obsession, led by the IMF and the rating agencies, with "getting the fundamentals right" – which in practice has meant displacing real economy investment with repeated adjustments of monetary policy – has hurt most economies. Accordingly, we need to ensure that the promised 1.3 percent increased spending is properly targeted on real multipliers.

We need to launch the kind of physical infrastructure spending that allows the economy to move, especially the construction and engineering sectors (and not only schools, and clinics, etc.)

We need to grow the domestic market; stimulate infant industries, especially black-owned enterprises; and regulate monopoly industries to ensure that they introduce differential prices for domestic users as against their international clients.

We need greater vigilance against transfer pricing by international corporations operating in South Africa.

We need to be clear about the sell-off of "nonstrategic assets" (another euphemism), and how this impacts the state's influence on economic decision-making in the private sector.

Finally, we need evidence that the government is serious about its economic programme. This has been in question for some time.